Barclays Global Consumer Conference

September 8, 2020

Lauren Lieberman: Okay. Great. So next up in our conference, I'm pleased to welcome Keurig Dr Pepper. Two years into the merger of Dr Pepper Snapple and Keurig Green Mountain, both the cold and hot value propositions are coming together with shared gains across the soft drink business and quicker than anticipated adoption of the brewer pod model for coffee, since the start of the COVID-19 crisis. Joining me for a Q and A session to dig a little bit deeper into recent trends and the strategy going forward, we have Chairman and CEO, Bob Gamgort and CFO Ozan Dokmecioglu, which I've done before properly, sorry.

Lauren Lieberman: Anyway, thank you both for joining us today, but seeing as you had some news out this morning, I wanted to maybe start there. So Bob, KDP announced that the company is going to be switching its trading platform from the NYSE to NASDAQ. So, if you could just help us understand the rationale behind that decision.

Bob Gamgort: Yeah. First of all, thank you for hosting us and welcome to everyone who's joining us right now. Lauren, as you said, two years ago we closed the merger between Dr Pepper Snapple and Keurig Green Mountain. We talked about ourselves being a challenger in the beverage industry, and as we're really done with integration and we've moved more to activation of this new model, we've been describing ourselves as a modern beverage company and NASDAQ is home to tech-forward companies and fast growth companies and we thought that was the neighborhood that we should be in. If you look at our business, we've got a really broad portfolio. As you said, we're the first to combine hot and cold beverages together at scale.

Bob Gamgort: But we also have taken very seriously the whole opportunity to use data and technology to drive our business faster. We talked on our last earnings call for

the first time about the size of our eCommerce platform, for example, being more than 10% of our sales, we also gave examples of how we were using cutting edge technology, real time demand data, for example, to navigate through this crisis. And then we also on our last earnings call, talked about the launch this quarter of our first connected and smart brewer, which really gives you an indication of where we're going next with that whole platform. And so that's why it seemed like a very good fit.

Bob Gamgort: In addition, it gives us an opportunity to enter passive indexes and that expands our investor reach and improves our trading dynamics. So if you looked at it right now, we would rank about 50 in the NASDAQ 100 index. So it was a combination of those two that made it attractive for us to move. Although NYSE was a great partner for these first two years.

Lauren Lieberman: Okay. And then, of course, the other news of the morning is that your largest shareholder, JAB is going to be distributing some additional shares to minority partners. So I was just wondering if there's any additional color that you could share on that as well.

Bob Gamgort: Well, as you know, there's been a series now of shared distributions and some secondaries. JAB, and people tend to put JAB as one entity, it's really JAB and its partners we always talk about, made a substantial investment in KGM about five years ago, and they've been great partners and they've been really supportive of the company. What's happening here is a continued program to provide some liquidity to some of its partners. And so it’s standard practice in private equity to do so. What's most important though, is that the private investors to do it in a disciplined manner. And so making sure that they do it at the pace in which the market can accept the additional shares, which is exactly what's been happening here.

Bob Gamgort: The other thing I would point out is that, today is a shared distribution. There have been secondaries, there was a previous share distribution. Some investors put those all in the same bucket. They're really different. The shared distributions have lockups on them. And if you think about some of the entities that are getting the shares, BDT, Quadrant as an example, they intend to be long-term public shareholders. So you'll see them move over to the public shareholder list and we'll be treating them as among our very largest public shareholders over the long term. And so now this latest move gets our public float up to about 44% plus MDLZ owns about 12%. And so all of this is good for our journey to go from private to controlled to now widely held and it reduces volatility. And it allows a number of institutions who haven't been in our stock, who have told us directly that the float wasn't big enough, this is all an opportunity for them to get in.

Lauren Lieberman: Okay, great. So back to this regularly scheduled programming in terms of what I'd planned to ask you about today. So, day back from Labor Day, we're all several cups into home brewed coffee. So, let's talk coffee first if that's okay.

Bob Gamgort: Sure.

Lauren Lieberman: So Bob, channel closures, consumer staying home more, working from home, has accelerated the coffee system story. Household penetration for brewers, for Keurig brewers to be clear, I think, was at 23% at the end of '19. I know the plan is to update us on that number annually, but I was still curious, just your insights work in what it's telling you, if there's a quicker path to get that 30 to 50% target that you've cited historically as the long-term opportunity and how much brewer innovation plays a role in driving that further?

Bob Gamgort: Yeah. When we did our investor day at the launch of KDP back in March of 2018, we talked about our line of sight to getting beyond 50% of US households and provided the roadmap to get us there. And it was a combination of innovation, and we've seen a significant amount of innovation the past two years, new features, new benefits, better aesthetics, improves sustainability, which continues to drive household penetration. You've seen good marketing, the improvement in quality, both the brewers and the coffee, and the fact that the cost per cup, which I know in the early days of this created some angst among the analysts and investor community, it was all part of the strategy to increase household penetration. And we've been increasing household penetration at about a rate of 7% per year, which there aren't many businesses in the CPG world that have my insight to real growth of 7% per year for a very long period of time.

Bob Gamgort: So we look at it as very much a long-term play. If you want to know what's happened during the crisis. Yeah, it's had a positive impact on our at home business. As I always emphasize, it had a major negative effect on our away from home coffee business. So we've had to navigate that mix issue. But driving the at home business, there's no question that household penetration has been positively impacted by that. People are working from home, we've seen a lot of current Keurig consumers upgrade their machines. If you take a look at sales of brewers, and we've talked many times, brewer sales aren't necessarily a direct correlation, it's a supportive metric. You're seeing that Keurig machines are outselling coffee makers by a significant margin. And so it's not just that everybody's moving to at home and buying coffee, they're buying Keurig machines on top of it.

Bob Gamgort: But I think it's worth just going through the math for a minute. Because I don't want people to get ahead of us here. If we grow household penetration at 7% a year, we're adding about 2, 2.1 million households, per year, into the system. And we've said before, very sticky once they come in. If we were to take that household penetration, let's say from 7% to 10%, that's a fairly modest number. That goes up to 3 million households. That Delta in brewers would mean that our brewer growth rate would more than double in a year. Because we have such a large installed base that when you add that incremental million households that I'm using as just being illustrative on top of our normal growth rate, you see the brewer growth rates more than double.

Bob Gamgort: And so my conclusion on that is the pandemic has been a nice bump up, but it's the long-term trends that really matter and the installed base is so large and the inherent growth is so big, that it's a nice plus up, but it's not a game changer on here. It's all part of this ongoing path.

Lauren Lieberman: Okay. As, just closer in though, also as consumer mobility has increased coffee shops have begun to reopen. I think we're not quite where we can bring true on-premise coffee back into the conversation with offices and so on. But, are you seeing any slowdown in the attachment rates, or just in layman's terms, how much coffee each brewer is making right now?

Bob Gamgort: This is an area we're seeing the opposite of that. We've seen a significant increase in attachment rate. And remember, we have a connected panel. So we have about 10,000 households that have been connected to smart machines for about three years. And we get real time consumption data, minute by minute. And you can go back and look at those first days of the shutdown and see the attachment rate spike.

Bob Gamgort: So, that level that we've seen is not something we believe will continue post pandemic. Although we think there's an element that will be elevated because of people discovering how easy it is and how much their quality is improved. There's another factor too, which is, let's say there's a recession coming out of this. That's actually a positive for us because the cost differential versus away from home coffee is substantial, in our favor.

Lauren Lieberman: Okay, great. Let's switch to the cold side of the business. So Bob, KDP's seen very positive share growth in CSDs and tracked channels. And these share gains, it's not just Dr Pepper and Canada Dry, right? It's been pretty broad based. So, could you just talk a little bit about what's enabling such broad performance and how sustainable you expect it to be?

Bob Gamgort: Yeah. This has been an area that's been a real positive for us, as we talk about this mix management, is that we've been able to accelerate our at home beverage business. So if you take a look at total LRBs, we've grown share LRB, we've grown share in 90% of our retail base, every category except for one in which we compete, we've expanded share. If you take a look at CSDs, underneath LRBs, it's been a real star within there. In the past 13 weeks, we've gained one and a half share points of CSDs and every single one of our CSD brands has grown share. What's driving all of that is household penetration growth. So we break it down. Is it, are current consumers drinking more? Is it new households entering our franchise? The numbers are convincingly in the direction of new households entering our brands, which is very promising for the future. Being able to hold onto those franchises as they rediscover our products or discover them for the first time, versus a temporary blip because people are at home and they just drink more. So that's very positive.

Bob Gamgort: If I go down on that level further to your question and say, what's driving the household penetration, why are we doing so all of that? It's a combination of

innovation... So we've got innovation out before the pandemic hit and items like Canada Dry Bold, the Dr Pepper and Cream Soda right here, which is the number one CSD innovation this year, have been a big contributor. Marketing has been strong. So yeah, we've backed off of some marketing like everyone did, and that's the appropriate thing to do during the pandemic. But our relative spend is still very robust, and that showing up in the share numbers that you see. And then our in store execution has been terrific.

Bob Gamgort: Company owned DSD has shown its true value. We have centrally controlled company owned DSD, which is a real differentiator, performed incredibly well. We focused on core SKUs. I talked about the data that we had access to that's informed which products we should distribute in which stores, we've adjusted our promotion schedule. And so when you add that all up, it's always a number of things that are brought together, but there's no question that the execution has been a big driver at this as well.

Lauren Lieberman: And so to that point, the distribution network has clearly been a pretty major asset and particularly the last couple of months, but you have also talked about optimizing routes to market. You're leveraging your network to also address white space opportunities, partnering with strong and emerging brands like Polar and Evian. Then you've got A SHOC and now it's plant based protein. So there's a lot that's going on that really, I guess, looks to leverage what you've already got, but also make it even better.

Lauren Lieberman: So maybe we could just, I guess, first I'd love to start with the Polar and Evian pieces. They're both big, established brands. So could you help us understand how these relationships are something more than just renting out your distribution system? Differences in your level of involvement with the two brands and how you might tie that back to what the old allied brand model looks like versus what you're trying to build going forward?

Bob Gamgort: Yeah, that's a good question. So, we got this base of distribution that we're proving that we can execute very well. I think it is surprising number of people in the industry, how strong the KDP company owned DSD network, combined with our independents that cover the space, the part of the geography that we don't cover, how well that's performed. So we can continue to enhance that and improve it. But it also works really well if we take new brands and put it through that existing system, which is what you're referring to. And we said that we wanted to change the allied brand strategy going forward. So we can do it four ways. We can develop products on our own, but we've mainly used that a tool for innovation or renovation, we can acquire straight up as we did with CORE, but we're really sensitive to paying high multiples.

Bob Gamgort: We say this all the time, that all of those big deals in the industry that we can study have all destroyed value. And so we do not think that that's our primary way to go forward. You talked about seed investment with path to ownership. That's A SHOC and Don't Quit! Which is our latest example. But if we're in categories where there's white space in our portfolio where we know we can

drive growth, and unsweetened flavored sparkling water is one of those examples. And we could go through it and buy something, we could do it on our own, we could try to do a seed investment. And we've got a 30 year partner in Polar who's got the highest velocity brand in the category, but it's only a third of the country, then we're willing to enter into a partnership because we can't own the brand.

Bob Gamgort: The family is not willing to sell the brand. We can enter into a really unique partnership that mimics ownership, but gives us both what we want. So we're able to take this brand national, we're going to do the manufacturing and the distribution in the territory that we're in. They get to keep the brand within the family. And we get the leapfrog competition by taking this high velocity business nationally. And we study every other route, on that category I can tell you, we studied all of those paths and decided this was by far the best path. And these are very long-term relationships that are very difficult for either side to get out. So I say they mimic ownership, it's everything but the ownership and that's same with Evian.

Lauren Lieberman: Okay. And then, in terms of optimizing the distribution network, my guess is we were going to talk a bit about this at the investor day in March. So I don't really know how to ask the question because I was excited to spend a couple hours hearing about it, but maybe what you could offer. You've already made a few moves, but as you think about this optimization and of a better way, maybe through specific examples of changes you've already made or at a high level, if that's a better way to get at the conversation.

Bob Gamgort: Yeah. Just to refresh everyone's memory, we have the ability to go direct to store outside of the Coke and Pepsi systems to a hundred percent of the country. 75% of the geography or population is covered by our company owned system. The other 25% is covered by independent relationships. So we've gone down three paths on here. One is we've said we want to invest in our own company owned DSD. And that's an investment in capabilities, data technology and we've talked about that already and there's more to come and more of a story to tell there.

Bob Gamgort: The second area is to strengthen our partnerships with our independents, to make sure that we've got a win-win set up for the long-term. The fact that we're doing this deal with Polar, that we talked about before, I'm just using that example, who's a 30 year partner of ours for the New England area, really does strengthen both sides of that relationship. We've become true partners for the long-term.

Bob Gamgort: And then the third area is to take areas where we see overlapping territory, where we have a truck and one of our independents has a truck and there's complete inefficiency to have two trucks. We're not shy to offer to buy that back from them. And we've done it. We've done that in L.A., We've done it in Evansville. We did a unique deal with one of our partners called Buffalo Rock that was written about down in the South.

Bob Gamgort: And the whole idea here is if we see an opportunity to reduce the number of trucks, to be able to increase the load size with one of our partners, we'll figure out a partnership to get there as well. So it's a combination of those three at a very high level. I can spend a lot of time talking about it, I'm trying to stay high, that will get us a much better distribution system, but you'll hear more from us in the future on this topic.

Lauren Lieberman: Okay. All right. Great. And then another topic I think we probably would've hit on a bunch at the investor day would have been around the fact that we're getting closer, I guess, the final year of the integration process, synergy plans and so on, so I think it's maybe fair to start talking a little bit longer term. So, Ozan, I was hoping you could talk a bit about the longer term growth algorithm, investment needs post synergies, cost savings available post synergies. Because I think, and at that time too, you'll have reached your leverage targets. So you'd be less encumbered from a balance sheet perspective in terms of a corporate development. So maybe if you could frame some of the building blocks of that longer term outlook, it would be great.

Ozan Dokmecioglu: Yeah, of course. Thank you Lauren. First of all, provide a minute to take a quick pause and analyze the situation because we are the only a few companies right now that have given quite a bit of visibility to the investor community with regards to the 2020 financial deliverables. That includes the full year and not just the next quarter, for example. And that visibility as we discussed many times, included double digit EPS growth, coupled with a significant debt reduction. And we definitely continue to express our confidence in our ability to deliver on the financial commitments that we put out there, in regards to, as part of our merger thesis.

Ozan Dokmecioglu: In 2021, we likely and we do expect to continue and become another volatile as well as challenging year. Obviously we are going to share our financial algorithm and outlook on 2021 at the appropriate time. Of course, we have been working on post 2021 algorithm and our potentiality in terms of providing some optionality and preparing a toolkit for multiple scenarios, in fact. First of all, let's remember that we will be at a position that considerable debt reduction that will take place and we will put behind us, as we also communicated several times by now. At the end of 2021, we do expect our multiple leverage ratio to be at 3 times or lower, which would create obviously a really good optionality for us in terms of how we can use the company funds and deploy our capital.

Ozan Dokmecioglu: Also we do expect to continue to deliver significant productivity, as well as the efficiencies on the base of the investments that we have been making. Let me share some examples. The state of the art K-cup pod facility that we have been building in Spartanburg, Allentown for packaged beverages and our newest Ireland facility for a beverage concentrates. Definitely, we also do have a robust pipeline innovation, which makes us very excited. And as Bob was explaining, we will continue to invest and optimize and get the necessary productivities and efficiencies from our manufacturing, our logistics, as well as distribution

network, which has been a very important cornerstone for us. That will include the DSD and across the other distribution channels that we do have.

Ozan Dokmecioglu: Having said that, we should not also forget, Lauren, that we have plenty of white space in both cold beverages as well as coffee. Household penetration increase opportunities at the same time.

Lauren Lieberman: Let me focus first maybe on the balance sheet optionality piece, because Bob, you just went through the thought process on innovation and it's going to be a mix of how you go after this but, I guess, how much of the path so far and the way that you've been adding to the portfolio has in fact been informed by the fact that you have been balance sheet constrained? To what degree would you be doing different things if you didn't have these de-leveraging targets today or said another way, does the model shift in any way 12 to 18 months from now?

Bob Gamgort: Ozan, you want to cover that?

Ozan Dokmecioglu: Absolutely. Lauren, we never believed that our balance sheet situation was highly levered when we started. And as you know, we have been in a little over two years into our merger and integration process. We never believed that that was a problem of us or inhibitor to do any potential, let's say M&A activity. As you know, we did buy several brands, most notably CORE Hydration, that water brand that we have and has been doing excellent since then. And before our acquisition time as well, was performing very strongly and we were the distributor for the most part of our business. At the same time, as Bob explained as well, we do set some new ventures in terms of a shift of the previous allied brand portfolio management. And we are seeing quite a bit of traction and benefits of those things.

Ozan Dokmecioglu: What is important here to note, as Bob touched couple of minutes ago, is to pay the right price for the white space brands or the other portfolios that can be a good compatible overlap to ours. And we are very disciplined in our actions and we will definitely stay as such, therefore, as we communicated several times, our number one priority is to delever our balance sheet whilst continuing to deliver double digit EPS as well as continue to deliver on our top line commitments. Therefore, we believe the algorithm has paid off very handsomely and very nicely of all investors on the base of our, either in market execution or the financial results, that we have been delivering. And we do expect that trend to continue and we will continue to find the further productivity programs. As I was explaining a little while ago, we have been making a sizeable three large investments that have not even started to deliver anything. And we are expecting to kick in in 2021 and beyond.

Ozan Dokmecioglu: That's why when you look to our portfolio as well, from the innovation side, we stay very encouraged and very excited. And whenever there's an opportunity in terms of filling some of our white space from the category perspective, we don't mind to go after the M&A as was the case before, but we will always be disciplined. That's the name of the game for us.

Bob Gamgort: Yeah. The only thing I would add, I think, that's a hundred percent right, the only thing I would add to that, Lauren, is remember when we acquired CORE we used shares. So the debt on the balance sheet has not been a limitation. And the fact that we're going to get to our target at the end of 2021 gives us a lot of optionality for shareholder value creation. It doesn't have to be M&A, there's other paths that we can go with that.

Lauren Lieberman: Yep. Okay. And then Ozan, I think, you've gone through and mentioned, there's ongoing productivity, you specified the three programs and they do start to get some benefit in '21. But in the beginning of your answer to the question I think you talked about '21 as being another challenging and volatile full year. You'd give guidance at the appropriate time, of course. But when I tie it all together, it doesn't sound like there's any reason to believe '21 is not in line with the algorithm or the pre-merger or at the time of merger forecast on what your goals were. Is that fair, or are we focused more on the, it's volatile out there and we're just not sure?

Ozan Dokmecioglu: No, absolutely. The short answer is yes, as we have stated several times, we are definitely committed to deliver on our financial algorithm that we put out there that comes in three pieces, top line, the bottom line EPS, as well as the debt reduction or hitting the multiple leverage that we have. And actually, maybe we can step back for a quick minute and take a look. What has been happening in the COVID environment, '19 environment and how we delivered the numbers, for example.

Ozan Dokmecioglu: As we stated several times, by no means COVID-19 environment was a windfall for us. In fact, it was a product of a ruthless prioritization, as well as a mix management. When you look to our, for example, the channels, you would see a significant swings amongst them, but it is true that, at home consumption in hot and cold beverages increased. At the same time, we have seen sizable declines in office and hospitality coffee businesses, as well as in the cold beverages, we have seen significant decline in consumption in our fountain food service, as well as convenience and gas.

Ozan Dokmecioglu: Also, when we look to the products and the packaging, we have seen sizable shifts on the base of the latest emerging from the consumer side, shifting towards larger and the multi-pack sizes. So we had to drive our growth areas harder to offset these pressures and continue to deliver on our financial commitments. And also, as we said, we are a little over into two years of the merger and the integration process, which in fact, this process has provided us an incredible insights with regards to our cost drivers.

Ozan Dokmecioglu: So we actually went after even smarter and harder to provide a further cost reduction opportunities for us. And there were several other examples that we have executed very successfully and continue to deliver against our financial commitment. And also, it is important to note that this trend will continue. We also reduce our number of SKUs and the streamlined product offerings to help to improve supply chain efficiencies, and also, which is very important, maintain

capacity to meet the higher levels of the demand. So when you sum up all these factors, we believe that they are here to stay and also we'll continue into our future. That will also help us in 2021.

Lauren Lieberman: Okay. That's great. Thank you. Bob, I think we have two minutes left or so, to just do closing remarks, if you had any, I'll turn it over to you.

Bob Gamgort: Yeah. Let me just pick up where Ozan left off and we can close on that point, which is, we had our three year commitment that we put out there in 2018 to cover us through 2021. We entered COVID, it would've been really easy to drop that commitment. Instead, as Ozan said, we were one of the few companies who not only provided guidance, but provided guidance for double digit EPS growth. And we've been able to deliver that. Now that's not an accident. We're getting there because we've had to manage this mix issue that we talked about a number of times today, by making some really aggressive and bold choices along the way.

Bob Gamgort: The good news is we're enabled by a company that is proving out our investment or acquisition or merger thesis, a combination of portfolio, the route to market, the management team we have in place, the incentives we have, the technology that we're now building into the company. All of that gives us great optionality to navigate through whatever we're going to face. Continuation of COVID, a recession, a return to normal. Remember, we were doing great before, we're doing well during this. We're not a pandemic stock. We weren't a problem before, we were doing great in all those. So that gives us all the confidence in the world that whatever next is, and none of us know for sure what next is, we're ready for it.

Bob Gamgort: And I think that's the appropriate thought to leave you with. Thank you again for hosting us today.

Lauren Lieberman: All right. Great.

Ozan Dokmecioglu: Thank you.

Lauren Lieberman: Thanks so much to both of you for joining us.

Ozan Dokmecioglu: Thank you very much.

Bob Gamgort: Our pleasure.