MOODY'S

Rating_Action: Moody's upgrades KDP's unsecured ratings to Baa1, affirms P-2 commercial paper rating; outlook is stable

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New York, April 03, 2023 -- Moody's Investors Service ("Moody's") today upgraded Keurig Dr Pepper Inc.'s ("KDP") senior unsecured ratings to Baa1 from Baa2 and affirmed the company's Prime-2 commercial paper rating. The rating outlook remains stable.

The upgrades reflect KDP's continued strong operating performance and consistent improvement in financial leverage following the merger of Keurig and Dr Pepper Snapple Group in 2018. Moody's expects the company to continue to perform well over the next 12-18 months and focus on reducing financial leverage further. The rating change also recognizes management's new and more conservative financial policy with a commitment to further reduce leverage to a range of 2.0x-2.5x net debt to EBITDA (company calculated, 2.8x as of December 31, 2022) through both debt repayment and EBITDA growth. This is a reduction from the less than 3x previous target that is a positive governance factor. The company benefits from well recognized brands spanning the cold and hot soft beverage space. The company's consistent strong performance through the pandemic including considerable and consistent free cash flow, and ability to pass through pricing to mitigate cost pressures provides additional evidence of strong debt service coverage and financial flexibility in a range of economic environments.

Moody's expects KDP's revenue and operating profits to grow mid-single digit over the next 12-18 months. Moody's also expects the company to become more conservative with its working capital management by reducing its trade payables days outstanding with less reliance on vendor financing receivables through third party financial institutions that KDP helps to arrange for its suppliers. A reduction in such arrangements would be credit positive as Moody's views factoring programs that materially extend payables beyond industry norms as "debt-like" and less reliable given these arrangements are uncommitted and could become more costly or be terminated if the credit quality of KDP declines or credit conditions tighten. Moody's expects that reversing these programs will initially detract from KDP's free cash flow in 2023 as payables decrease. Free cash flow will still be meaningful in a $900 million - $1.0 billion range. Over time, the actions will potentially improve KDP's gross profits as more favorable pricing terms may be realized with suppliers. Moody's further expects that free cash flow in 2024 will be strong at more normalized levels of between $1.4 billion to $1.5 billion after factoring in annual dividends. The company expects to pursue more modestly sized acquisitions over the next few years as it focuses its priorities on integrating and growing its existing brands. KDP's liquidity remains strong with cash on hand of $535 million as of December 31, 2022 and $3.6 billion of availability under its $4.0 billion committed revolving credit facility that expires in February 2027 (unrated) after taking into account $399 million of commercial paper outstanding. The cash sources are meaningful relative to upcoming debt 2023-2024 debt maturities, consisting of $500 million of notes due December 2023 and $1.15 billion notes due March 2024.

The following ratings/assessments are affected by today's action:

Upgrades:

..Issuer: Keurig Dr Pepper Inc.

....Senior Unsecured Regular Bond/Debenture, Upgraded to Baa1 from Baa2

Affirmations:

..Issuer: Keurig Dr Pepper Inc.

....Senior Unsecured Commercial Paper, Affirmed P-2

Outlook Actions:

..Issuer: Keurig Dr Pepper Inc.

....Outlook, Remains Stable

RATINGS RATIONALE

KDP's Baa1 senior unsecured ratings reflect its well-known portfolio of brands, many with leading positions in their sub-categories, robust product and channel diversity, strong profitability and good liquidity. The company has moderate financial leverage with a focus on continued deleveraging over the next year. KDP's cold drinks product portfolio is skewed to higher growth flavored beverages and the company has expanded its alternative beverage portfolio through innovation and acquisitions, becoming one of the first beverage companies to bring together the cold and hot beverage portfolio. KDP also enjoys a strong market position in the faster growing and higher margin single serve coffee segment where it has a large and growing installed base of single serve coffee systems. The strong market position and good cost management lead to considerable free cash flow through economic cycles that provides good investment flexibility and debt service coverage. KDP has smaller scale relative to major soft beverage competitors and its geographic breadth remains narrower than its larger global peers. These factors can create exposure to more volatility from competitive pressures and regional economic downturns.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

The stable outlook reflects Moody's expectation that KDP will continue to experience good operating performance over the next 12-18 months with modest sales growth and a stable operating profit margin. The outlook also reflects Moody's expectation that the company will continue to generate strong free cash flows.

Ratings could be upgraded if the company maintains its strong market position and operating performance translating into continued strong free cash flow generation. An upgrade would also require a conservative financial policy such that debt-to-EBITDA is sustained below 3.0x, retained cash flow (RCF)-to-net debt is sustained at least in the high-teens, and maintenance of strong liquidity.

Ratings could be downgraded if operating performance weakens or the company pursues a more aggressive financial strategy such that debt-to-EBITDA is sustained above 3.75x. A downgrade could also occur if liquidity were to meaningfully deteriorate or the company pursues large debt-funded acquisitions or shareholder distributions.

ESG considerations

The overall neutral to low (CIS-2) Credit Impact Score reflects Moody's view that ESG attributes are considered to have a neutral-to-low credit impact on KDP's current credit rating, with neutral to low governance risk (G-2) characteristics the key factor. While the moderately negative E-3 and S-3 scores indicated more risk, they are a by-product of the company's beverage products. While the G-2 governance score and CIS-2 are not changing, governance remains a key driver of this rating action as the company reduced its financial leverage targets to a more conservative level of 2.0x to 2.5x (company calculated) from less than 3x previously, indicating further deleveraging over the next year.

The principal methodology used in these ratings was Soft Beverages published in September 2022 and available at https://ratings.moodys.com/api/rmc-documents/393388. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

Headquartered in Frisco, Texas, and Burlington, Massachusetts, Keurig Dr Pepper Inc. (KDP) is a leading integrated brand owner, bottler and distributor of mostly nonalcoholic beverages. Products include flavored carbonated soft drinks and non-carbonated beverages (juices, juice drinks, ready to drink teas and mixers). KDP is also a manufacturer of Keurig® single serve hot and cold brewing systems and beverages. These include specialty coffee, tea and other beverages in single serve packs for use with its brewers. Among the company's key brands are Dr Pepper, Canada Dry, A&W, Squirt, Sunkist, Snapple, Hawaiian Punch, Mott's, and Green Mountain Coffee Rosters, to name a few. The company has over 125 owned, licensed and partnered brands. The company primarily sells its products in the United States, Canada, Mexico and the Caribbean. JAB Holding Company S.a.r.l. owns about 31% of KDP. FYE 2022 revenues were around $14.1 billion.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

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At least one ESG consideration was material to the credit rating action(s) announced and described above.

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