S&P Global
Ratings

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Keurig Dr Pepper Inc.

Primary Credit Analyst:
Diane M Shand, New York (1) 212-438-7860; diane.shand@spglobal.com

Secondary Contact:
Chris Johnson, CFA, New York (1) 212-438-1433; chris.johnson@spglobal.com

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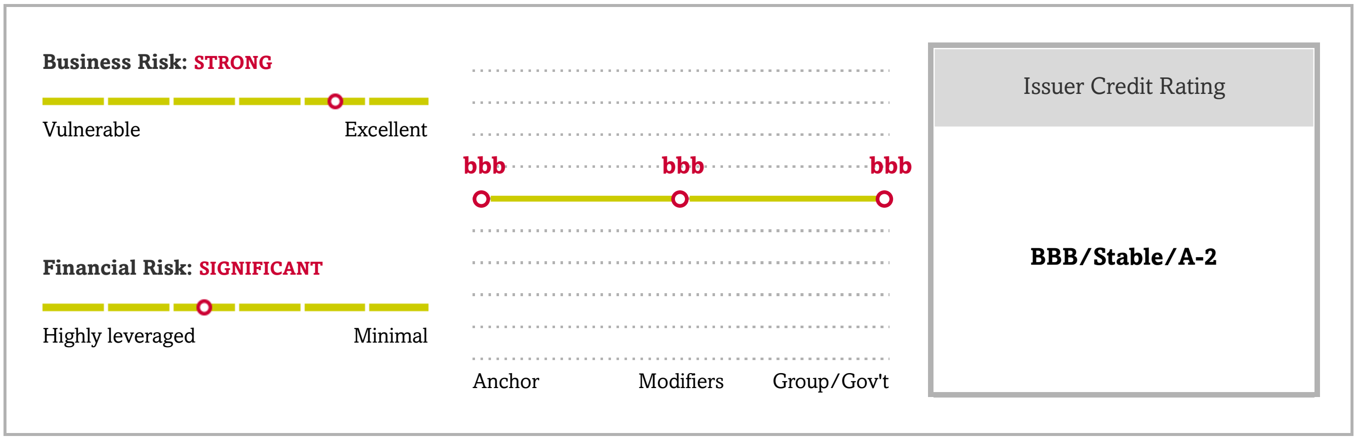


Credit Highlights

Overview

Key strengths	Key risks
Solid market positions in categories with good growth trends.	High leverage because of largely debt-financed merger in 2018.
Benefits from product diversification and a comprehensive distribution network.	Limited geographic diversity compared to global beverage and food peers.
Good negotiating power with retailers and suppliers because of scale and diversity.	Distant third market position in cold beverages.
Strong cash flow because of high margins.	Key competitors have greater financial wherewithal.

Keurig Dr Pepper Inc. (KDP) is executing well in this unpredictable and difficult environment. KDP has seen a spike in demand, initially because of pantry loading and now because of strong replenishment demand due to shelter-in-place mandates related to the COVID-19 pandemic. KDP's volume grew 5.6% for K-Cup pods, despite a significant decrease in away-from-home business late in the first quarter. Its package segment posted a 9.1% increase, with volume mix up 8.7% in the quarter. Consolidated sales, excluding foreign exchange, rose 4.5%, and the EBITDA margin expanded to 30.1% from 29.2% in the year-ago quarter because of positive mix, productivity programs, and merger synergies. We expect at-home consumption to exceed lost sales in the away-from-home channel in calendar year 2020, but sales will be flat in the second quarter because of the massive number of closures of restaurants, bars, entertainment venues, and office buildings. We believe KDP's broad product portfolio and its scalable, multichannel selling and distribution system can meet the shift in consumer demand. Although it is too soon to determine medium- to longer-term changes in consumer behavior that will occur as a result of the pandemic, we believe KDP will benefit from increased at-home coffee consumption over the next few years because consumers' recently reduced on-premise consumption is accelerating household penetration of KDP's coffee products. KDP remains the dominant manufacturer with dollar market share of 82% in single-serve coffee pods.

KDP has industry-leading margins. The company's EBITDA margin expanded to 30.1% in the first quarter, up from 29.2% in the year-ago period. This compares favorably to PepsiCo Inc.'s 2019 EBITDA margin of 20% and Molson Coors Beverage Co.'s 22.3%, as well as packaged goods peers such as General Mills Inc., The J.M. Smucker Co., Conagra Brands Inc., Campbell Soup Co., and McCormick & Co. Inc., which generate EBITDA margins in the low-20% area. The Coca-Cola Co.'s (Coke's) 2019 EBITDA margin of 33.8% is the highest among peers. This is attributable to its large scale and asset-light business model.

Expanding margins and strong cash flow will rapidly reduce leverage. KDP's leverage was 4.5x in the trailing 12 months ended March 31, 2020, down from 5.8x at the close of the transaction in July 2018. We forecast a decline in leverage to the mid-3x area in 2020 and to the low-3x level in 2021 through a combination of debt paydown and EBITDA growth. In addition, we forecast that KDP will generate $1.6 billion of discretionary cash flow (DCF) in 2020--up from $1.3 billion in 2019--but DCF will then fall closer to $1.4 billion in 2021 as delayed capital expenditures (capex) ramp back up. The improvement in 2020 is the result of margin expansion from cost cutting and post-acquisition synergies, better working capital management, and delayed capex in response to the current economic landscape.

Outlook

The stable rating outlook on KDP reflects our expectations that it will grow earnings and cash flow and rapidly reduce leverage. We believe KDP will generate 3%-4% top-line growth and maintain the EBITDA margin over 32% over the next two years. We forecast KDP will generate $1.6 billion in DCF in 2020 and $1.4 billion in 2021. This should enable the company to reduce leverage toward the mid-3x area in third-quarter 2020 (two years after the close of the merger).

Downside scenario

We could lower our rating on KDP if the company cannot reduce leverage to below 4x in 2020 due to not achieving anticipated cost-cutting goals, operating performance deterioration (possibility because of a prolonged severe recession), or if management's financial policies become more aggressive, resulting in an inability to reduce debt in line with our base-case forecast such that leverage remains above 4x.

Upside scenario

We could raise the rating over the next two years, if KDP achieves long-term benefits from the current increased consumption of its products and reduces debt using its strong cash flow. A higher rating would also depend on KDP demonstrating EBITDA improvement by increasing operating efficiencies and achieving $600 million in planned synergies, resulting in EBITDA margins expanding to close to 35%. This should lead to a decline in leverage to below 3x. In addition, we would expect that management would adhere to a financial policy consistent with maintaining leverage below 3x.

Our Base-Case Scenario

We forecast KDP will continue to generate good sales growth and benefit from consumer demand for non-cola carbonated and distilled beverages and single-serve coffee products. Moreover, we believe household penetration of its single-serve coffee pods will modestly accelerate because it has captured new occasions for coffee drinking as a result of consumers sheltering in place because of COVID-19, and some of this will continue after the economy reopens. We also believe consumers will drink more coffee at home during the recession to save money. KDP's national distribution capabilities and ability to pivot operations to address changes in channel mix will support revenue growth, and its productivity will more than offset inflation.

S&P Global Ratings acknowledges a high degree of uncertainty about the rate of spread and peak of the coronavirus outbreak. Some government authorities estimate the pandemic will peak about midyear, and we are using this assumption in assessing the economic and credit implications. We believe the measures adopted to contain COVID-19 have pushed the global economy into recession (see our macroeconomic and credit updates here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

Assumptions

- U.S. GDP contracts 5.2% in 2020 and grows 6.2% in 2021. Canada's GDP contracts 5.3% in 2020 and grows 6% in 2021.
- Sales of KDP's cold beverages grow 2% in 2020, well above GDP growth. Still, that is below our prior estimate because of the loss of on-premise and convenience store business because of social distancing related to COVID-19.
- Hot beverage revenue grows about 4.5% in 2020, above economic growth, because of strong sales of coffee pods and good growth of KDP's coffee machines, given the shelter-in-place mandates and an increase in the number of consumers working from home.
- In 2021, we believe the cold beverage business will grow more than 3.5% because of strength in its core business, brand innovation, and the return of most of its on-premise business.
- Coffee sales in 2021 grow 4%, slightly below projected economic growth as KDP's strategy to reduce prices in order to increase household penetration will partially offset volume gains. In addition, coffee mix will be unfavorable because lower-priced private-label products will outpace sales of KDP's premium brands while consumers look to save money during and after the 2020 recession.
- EBITDA margin expands to about 32.8% in 2020, up from pro forma 31.4% in 2019. We believe the margin will rise to about 34.2% in 2021 and approach 35% in 2022, reflecting a $400 million benefit from cost-savings initiatives and synergies. Productivity improvements will more than offset the negative shift in price mix in its coffee business.
- Cash flow benefits from a working capital inflow of $270 million in 2020 from a combination of accounts

Key Metrics

	2019	2020e	2021e
EBITDA margin (%)	31.4	32-33	33.5-34.5
Debt to EBITDA (x)	4.5	3.5-3.8	3-3.3
DCF to debt (%)	8.3	10-12	10-12

e--Estimate. DCF--Discretionary cash flow.

receivable, accounts payable, and inventory management, as well as depreciation and amortization exceeding capex.

- Capex of about $425 million in 2020 and nearly $550 million in 2021. We believe some projects planned for 2020 will be pushed into 2021.
- Dividends of about $850 million annually in 2020 and 2021.
- DCF of $1.6 billion in 2020 and $1.4 billion in 2021, up from $1.3 billion in 2019. The decline in cash flow in 2021 reflects our expectation for higher capex and little benefit from working capital.
- No share repurchases and limited mergers and acquisitions (M&A).

Base-case projections

KDP's well-diversified cold and hot beverage portfolio offers steady organic growth. We forecast KDP can grow organic sales 3%-4% annually over the next five years because of its above-average volume growth in several brands across its carbonated, non-carbonated, and its large and diverse single-serve coffee portfolio. We've raised our expectation from our prior forecast of 2% growth because we believe KDP will benefit from increased at-home daily beverage consumption and increased household penetration during and after the pandemic, as well as its ability innovate and renovate brands.

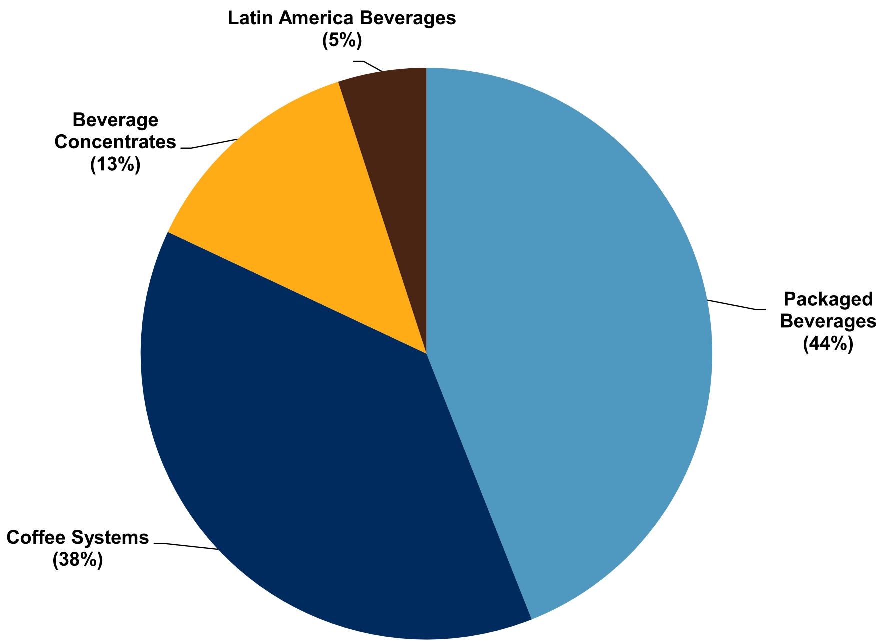
KDP's margins continue to improve because of synergies and its ongoing cost-savings programs. KDP achieved $200 million of merger synergies in 2019. We expect it to achieve the remaining $400 million in 2020 and 2021. We expect about half of the $600 million run-rate savings to come from reduced selling, general, and administrative expenses, a third from cost of goods sold, and the remaining one-sixth from distribution. As a percent of Dr Pepper Snapple Group's 2017 revenues, deal synergies are about 9%, which is modestly above the 8.5% median of large transactions in the global consumer products industry between 2000 and 2017.

Company Description

KDP is a major beverage company in North America with a diverse portfolio of flavored (non-cola) carbonated soft drinks (CSDs), specialty coffee and non-carbonated beverages, and the No. 1 single-serve coffee brewing system in North America. KDP has a national distribution system that provides its portfolio of more than 125 owned, licensed, and partner brands to consumers. Its coffee business is modestly more profitable than its cold beverage business.

Chart 1

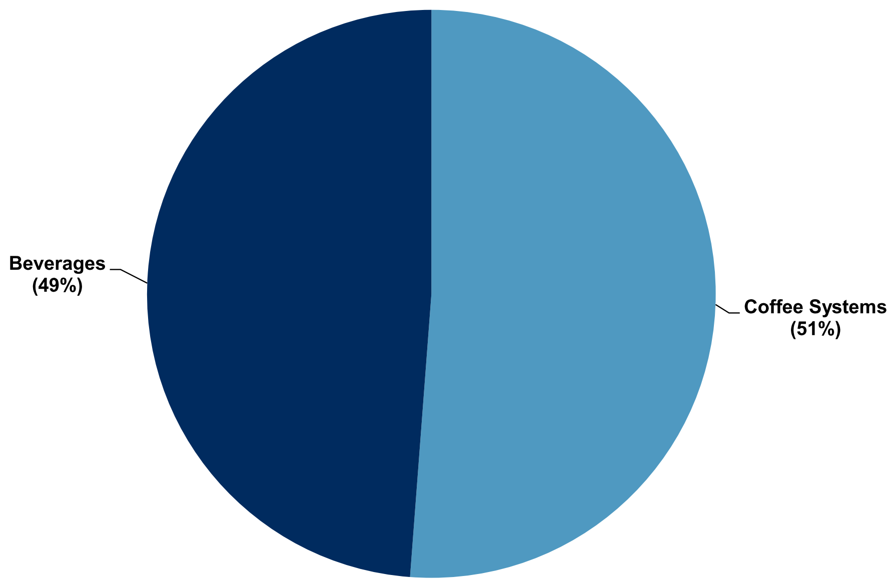
Product Mix
2019



Source: Keurig Dr Pepper Inc. data.

Chart 2

EBITDA Mix
2019



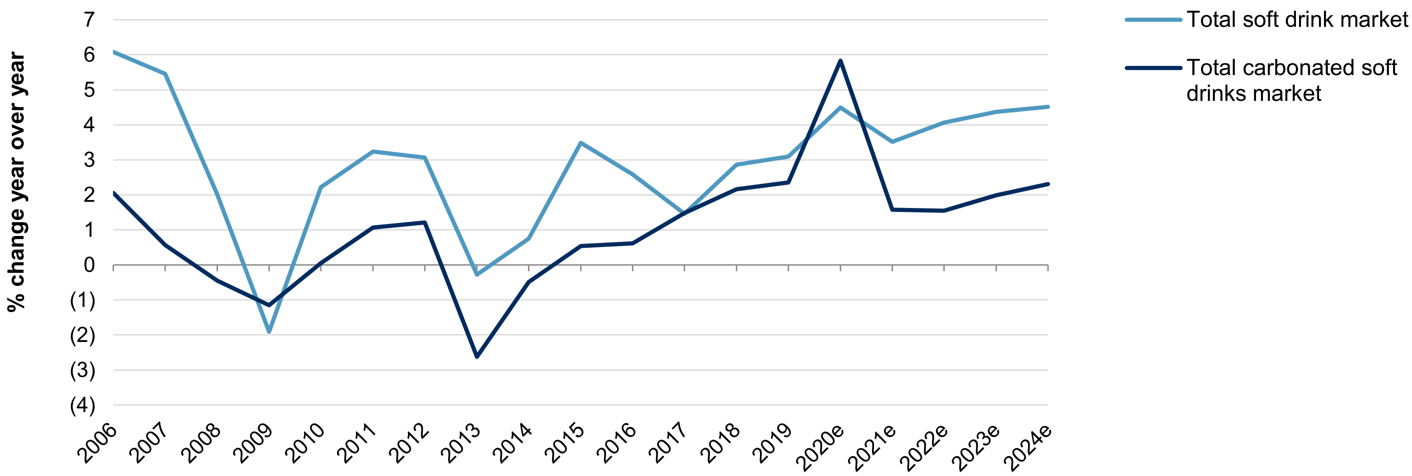
Source: Keurig Dr Pepper Inc. data.

Business Risk: Strong

KDP is a formidable competitor in the beverage industry. It is the No. 1 player in the North American single-serve coffee sector, and it holds the No. 3 position in the North American liquid refreshment beverage industry. We expect single-serve coffee to continue as the fastest-growing segment of the coffee market and non-flavored carbonated beverages to grow faster than the overall carbonated beverage market. We believe KDP's diversified portfolio of hot and cold beverages and single-serve hot coffee, as well as its scalable, multichannel selling and distribution system, should enable it to steadily grow sales and profits. KDP should be able to generate positive sales growth this year, despite the disruption in its away-from-home and convenient store business as a result of COVID-19. KDP is focusing on having the right product in the right place and prioritizing profitable sales.

Chart 3

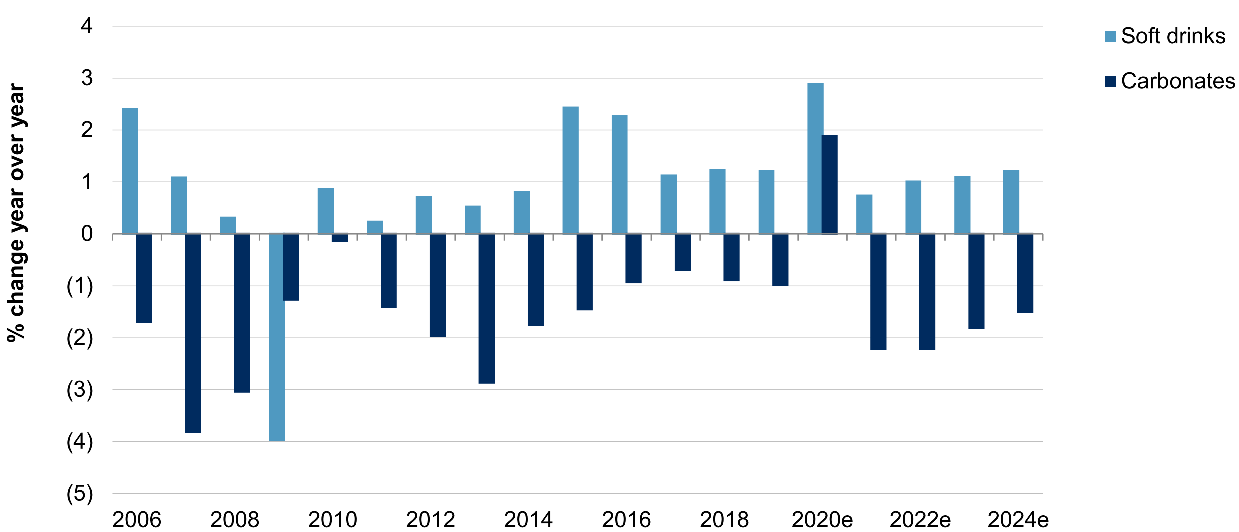
The North American Soft Drink Market Continues To Have Good Growth
We expect the soft drink market to grow 3%-4%.



e--Estimate. Source: Euromonitor.

Chart 4

Overall Industry Volume
Since the Great Recession, overall industry volume has been positive as consumers shift to non-carbonated beverages.



e--Estimate. Source: Euromonitor.

On the cold beverage side, KDP has very defendable market positions, given the strength of its core and difficult-to-replicate Dr Pepper brand, customer loyalty, and favorable demographic trend across many of its flavored carbonated drinks (including the fast-growing Penafiel brand in Mexico), as well as its strong brands in non-carbonated drinks (including Motts and the Core and evian water brands). Moreover, its core CSD business does not overlap much with that of its large competitors, Coke and PepsiCo. KDP's strategy focuses on fragmented categories. The North American off-premise soft drink category is large, at $154 billion in 2019, according to market research firm Euromonitor. We believe industry sales in off-premise channels will grow 3.5%-4.5% rate annually over the next five years because of price mix. This is an acceleration in growth from our forecast last year that projected 1% annual growth. We expect the on-premise channel, which represents about 10% of KDP's sales, to plunge about 40% this year and jump 35% in 2021. We forecast the channel will grow at a compound annual growth rate (CAGR) of 2.5% from 2022 through 2024.

The non-cola flavored carbonated market has been growing faster than the cola market, and KDP's portfolio has benefited from the strength of its Dr Pepper and Canada Dry brands. According to Euromonitor, off-premise retail sales in the North American carbonated beverage market declined about 1%-2% annually for the past 13 years. This trend, with the exception of 2020, is expected to continue over the next five years because of consumers' shift toward drinks with lower sugar contents as well as energy drinks. Moreover, growth trends in non-cola carbonated drink share outpaced those of the industry. Indeed, the Dr Pepper brand's market share increased to 18% in 2019, up from 15% in 2010, which compares favorably to Coke's less than one-percentage-point gain and a three-percentage-point decline in PepsiCo's market share. We attribute this to the difficult-to-replicate taste of its Dr Pepper brand and the popularity of its Canada Dry brand as mixers in alcoholic beverages.

Table 1

Carbonated Beverage Market Share

Keurig Dr Pepper Inc. and small to midsize brands have been gaining market share in the carbonated beverage market.

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Share change (2019 vs. 2010)
Coca-Cola Co.	36.6	35.9	35.9	36.0	36.1	36.0	36.3	36.4	36.6	36.9	0.3
PepsiCo Inc.	31.7	30.9	30.1	29.8	29.9	29.4	28.8	27.8	27.0	26.3	(5.4)
Keurig Dr Pepper Inc.	15.0	15.9	16.1	16.2	16.5	16.8	17.2	17.7	17.9	18.0	3.0
Private label	8.6	8.8	8.5	8.1	7.6	7.5	7.2	6.9	6.7	6.6	(2.0)
Other	8.0	8.5	9.3	9.8	10.0	10.6	10.6	11.4	11.7	12.2	4.2

Source: Euromonitor.

We believe KDP will also benefit from its non-carbonated drinks portfolio. The company should be able to compete in the water segment, which is the second-largest segment of the soft drink market and has better growth prospects compared to all other sub-categories of the soft drink industry, given consumers' shift toward healthier beverages. KDP purchased Bai in 2017 and Core in 2018, and it has a long-term distribution agreement with Danone Waters of America to sell, distribute, and merchandise evian in North America. According to Euromonitor, Nestle S.A. is the clear branded leader in the category, with its portfolio of water brands commanding a 20.1% share of the industry. Coke is the next-largest player; its water brands have a 10.1% share. PepsiCo has a 7.8% water brand market share. Still, the category is very fragmented, and no individual brand has more than an 8% share. Most brands have less than a 1% share. KDP currently has a 0.4% share of the market. KDP has an advantage over smaller and regional brands, given its national distribution capabilities. We expect KDP to build on the premium water segment, as well as other faster-growing categories such as sport and energy, ready-to-drink (RTD) tea, and coffee. Although KDP is a small player in the fast-growing energy segment, we consider it a major participant given consumers' use of coffee as an energy lifter. Overall, we believe KDP's cold beverages will gain share because of its focus on non-cola beverages, its water offerings, its RTD Peet's coffee, and its allied brands.

Table 2

Bottled Water Should Continue To Take Share From Carbonated Beverages

Shift is measured by share of off-trade volume.

	2015	2016	2017	2018	2019	2020e	2021e	2022e	2023e	2024e	Share change (2019 vs. 2015)	Share change (2024 vs. 2019)
Bottled water	34.5	36.0	37.4	38.6	39.1	39.9	41.0	41.8	42.5	43.1	4.6	3.9
Carbonates	38.2	37.0	36.4	35.8	34.8	34.5	33.5	32.4	31.5	30.6	(3.4)	(4.2)
Concentrates	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Juice	14.5	13.9	13.4	13.0	12.6	12.2	11.6	11.3	11.1	10.8	(1.9)	(1.8)
RTD coffee	0.5	0.5	0.6	0.6	0.7	0.7	0.7	0.8	0.8	0.9	0.2	0.2
RTD tea	3.9	4.0	4.1	4.2	4.1	4.1	4.2	4.2	4.3	4.4	0.3	0.2
Energy drinks	2.4	2.4	2.5	2.5	2.8	2.7	2.9	3.2	3.5	3.7	0.4	0.9
Sports drinks	5.9	6.0	5.7	5.3	5.8	5.9	6.1	6.3	6.4	6.5	(0.1)	0.7

e--Estimate. RTD--Ready-to-drink. Source: Euromonitor

Table 3

Retail Selling Price Growth, Year Over Year

Keurig Dr Pepper Inc. participates in faster-growing categories such as bottled water, ready-to-drink coffee and tea, and energy drinks.

	2015	2016	2017	2018	2019	2020e	2021e	2022e	2023e	2024e
Soft drinks	2.6	1.5	2.9	3.1	4.5	3.5	4.1	4.4	4.5	4.5
Bottled water	6.9	2.6	3.9	3.4	6.3	4.9	4.6	4.1	4.1	4.1
Carbonates	0.6	1.5	2.2	2.4	5.8	1.6	1.5	2.0	2.3	2.3
Concentrates	(3.2)	(2.0)	(0.9)	(0.9)	(2.0)	(0.6)	(0.2)	(0.4)	(1.1)	(1.1)
Juice	(0.9)	(1.6)	(1.1)	(1.3)	1.6	(2.5)	(0.1)	0.9	1.2	1.2
RTD coffee	11.6	11.4	8.7	9.7	3.6	9.8	11.7	12.2	12.3	12.3
RTD tea	8.1	5.5	3.8	2.9	6.5	5.2	5.1	6.3	6.5	6.5
Energy drinks	2.8	4.1	8.2	9.3	0.2	12.1	12.4	11.8	11.0	11.0
Sports drinks	4.7	(3.6)	3.6	5.7	6.5	5.9	5.7	5.3	4.8	4.8

e--Estimate. RTD--Ready-to-drink. Source: Euromonitor.

KDP has the No. 1 position in the single-serve coffee segment in North America. It is successful because it has more than 125 brands and large distribution. The company's dollar share of pods manufactured in the U.S. was 82% in 2019. The North American coffee market is large; it accounted for $19.7 billion of sales (excluding retail coffee shops) in 2019, according to Euromonitor. Single-serve constituted a 40% share in 2019 on a dollar basis in North America, up from 2% in 2008. The category is currently benefitting from an expansion of work-from-home policies and consumers' inability to visit coffee shops because of shelter-in-place mandates related to the COIVD-19 pandemic, and single-serve coffee growth is accelerating. We believe at-home coffee occasions have risen and that demand compared to 2019 levels will be higher for at least the next five years. According to Euromonitor, coffee pod volume should grow 13% in 2020 and at a CAGR of almost 6% from 2021 to 2024. This is up from its 2019 expectation of a CAGR of about 3% from 2019 to 2022. The overall coffee category volume growth is expected to accelerate to a CAGR of 2% over the next five years from prior expectations of no growth and slight contractions from 2014 to 2018. Single-serve coffee category volume growth slowed in recent years due to market maturation and consumers' environmental sustainability concerns. The category also faces competition from cold brew coffee because it offers the same convenience as single-serve coffee, which is a key demand driver. We expect KDP to grow in line with the market because of its large market share, vast number of brands, and broad distribution. Sales growth will be below volume growth because KDP is lowering prices to increase household penetration. In addition, KDP competes in the RTD coffee market with its Peet's RTD offering. This should help KDP target millennials, given they drink more cold coffee than hot.

Table 4

Coffee Market Volume Growth

Volume growth of single-serve coffee leads that market, and we expect that growth to accelerate.

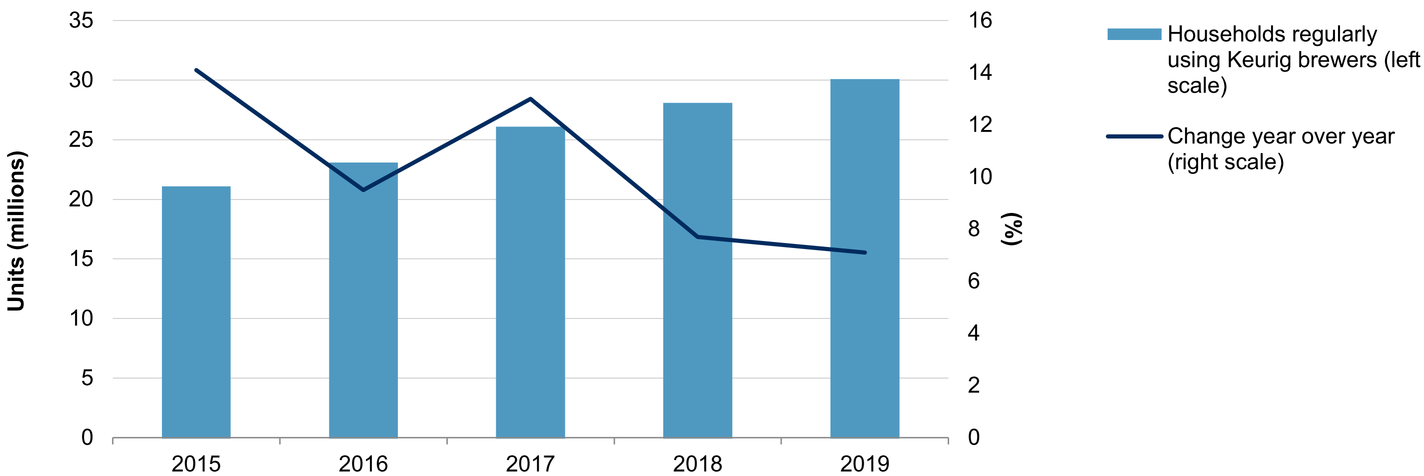
	2015	2016	2017	2018	2019	2020e	2021e	2022e	2023e	2024e
Coffee	1.3	(0.2)	(1.5)	1.4	1.7	6.7	(3.4)	2.1	2.3	2.4
Fresh coffee beans	2.7	4.4	(0.8)	2.9	2.5	8.7	(3.7)	1.5	1.8	2.0
Fresh ground coffee pods	17.5	11.6	3.5	6.4	6.6	13.0	2.7	7.4	6.8	6.5
Standard fresh ground coffee	(0.3)	(1.8)	(2.1)	0.7	1.1	5.6	(4.2)	1.3	1.6	1.8

e--Estimate. Source: Euromonitor.

Given its large share, KDP will need to grow household penetration. Household penetration increased to about 23% in 2019, up from 17% in 2015. The number of households using Keurig brewers grew to about 30 million in 2019, up 7% from 2018. Shipments of single-serve pods grew 8% in 2019. There is still plenty of room for growth, given there are 128 million households in the U.S. and 89 million at-home coffee drinkers. Household penetration in France is 65%, and it is 63% in the Netherlands. We think KDP can increase household penetration in the U.S. because it has reduced the price of pods to broaden its customer base, improved the quality of its brewers, invested in advertising, and upgraded in-store displays for brewers. The company's pods in Canada are 100% recyclable, and by the end of 2020, all of its pods in the U.S. will be recyclable. This should help increase household penetration among environmentally conscious consumers.

Chart 5

Number Of U.S. Households Regularly Using Keurig Brewers
The number of regular users by household is growing.



Source: Keurig Dr Pepper Inc. data and 2019 Omnibus study.

In its hot coffee business, KDP competes against large brands with deep financial resources, such as Kraft Foods Group Inc.'s Maxwell House and J.M. Smucker's Folgers, as well as coffee retailers such as Starbucks Corp. and Dunkin' Brands Inc. In the single-cup coffee segment, KDP competes against companies such as Nestle, which leads the global category with about $9 billion in coffee sales. KDP also competes against coffees and teas sold through supermarkets, club stores, mass merchants, specialty retailers, and food service accounts. In single-serve, KDP has a competitive advantage, because it controls innovation on brewers and pods, and it has multiyear strategic relationships with Starbucks, Dunkin' Donuts, Kraft-Heinz, Smucker, Eight O' Clock Coffee, and others. KDP has more than 125 brands in its system, including 18 of the top 20 brands, which creates a significant competitive advantage because no other single-serve system offers more choices for consumers. We believe KDP will maintain a very strong share in the U.S. and Canada markets because of its successful history of developing innovative products. Its pipeline of new innovative brewers and marketing initiatives should enable it to gain additional share.

Peer comparison

KDP has several close beverage peers including Coke and PepsiCo. Both Coke and PepsiCo are larger and have greater product and geographic diversity. Their credit protection measures are stronger than KDP's.

KDP's business strength is greater than Molson Coors' because it has more product diversification and higher margins. KDP's DCF to total debt is higher than all of its peers we've mentioned, except for Molson Coors, which has a ratio slightly better than that of KDP.

In comparison to its packaged goods peers, KDP is rated the same as J.M. Smucker, General Mills, and Kellogg Co. (as of May 13, 2020). These peers have similar business risks given their leading market positions, diverse brand and product portfolios, good margins, and cash flow generation. In addition, these peers generate most of their sales in the U.S. KDP competes directly with J.M. Smucker in the coffee category. KDP's DCF to total debt is higher than that of all of these peers.

Table 5

Peer Comparison

	Keurig Dr Pepper Inc.	The Coca-Cola Co.	PepsiCo Inc.	Molson Coors Beverage Co.
Ratings as of May 7, 2020	BBB/Stable/A-2	A+/Negative/A-1	A+/Stable/A-1	BBB-/Negative/A-3
	Fiscal year ended Dec. 31, 2019	Fiscal year ended Dec. 31, 2019	Fiscal year ended Dec. 28, 2019	Fiscal year ended Dec. 31, 2019
(Mil. $)				
Revenue	11,120.0	37,266.0	67,161.0	10,579.4
Annual revenue growth (%)	49.4	17.0	3.9	(1.8)
EBITDA	3,497.0	12,649.0	13,434.0	2,360.1
FFO	2,520.2	9,560.2	10,069.6	2,002.8
Capital expenditure	365.0	2,054.0	4,232.0	585.5
FOCF	2,168.2	8,702.2	5,828.6	1,367.5
Debt	15,886.1	37,598.0	31,981.4	8,940.3
Adjusted ratios				
Return on capital (%)	6.7	21.4	23.1	6.2
Debt/debt and equity (%)	40.6	64.1	68.3	39.5
DCF/debt (%)	8.3	2.0	(8.1)	10.5

FFO--Funds from operations. FOCF--Free operating cash flow. DCF--Discretionary cash flow.

Financial Risk: Significant

Although KDP's leverage following the Dr Pepper acquisition is high, with debt to EBITDA currently at 4.5x, we forecast the company will continue to focus on reducing debt over the next two years. The company payed down $1.3 billion of debt in 2019. We forecast net debt will decline a similar amount in 2020. Leverage has already materially declined: Pro forma leverage was 5.8x at the close of the merger in July 2018. KDP is steadily improving cash flow, prioritizing debt repayment, and it has no plans to increase its shareholder returns. We believe KDP will reduce leverage to about 3x by 2021, given its strong DCF. We estimate the ratio of DCF to adjusted debt will be strong at about 11% in 2020 and 12% in 2021, up from 9% in 2019. We consider this a key factor in our ratings. Our forecast assumes no share repurchases, and we expect M&A activity to be leverage neutral during the forecast period. KDP has shown a willingness to use equity to finance acquisitions (e.g., Core).

KDP generates strong cash as a result of its high margins. KDP's cash flow also benefits from working capital improvements through a combination of better management of accounts receivable and payable, as well as inventories. We believe KDP will repay debt this year through a combination EBITDA growth and working capital gains; thereafter, it will pay down debt predominantly through EBITDA growth. We expect the company's accounts-payable days will be about 145 days at year-end 2020. Its accounts-payable days are currently 132 days, and we believe the industry norm is about 120 days. We have added 25 days payable to debt, this increases leverage by 0.1x.

Liquidity: Adequate

In our assessment, KDP's liquidity is adequate, reflecting our expectation that projected sources will cover uses by more than 2.5x over the next 12 months. We expect sources will continue exceeding uses even if forecast EBITDA declines 30%. Although KDP's ratio of sources to uses would qualify for a more favorable liquidity assessment, we believe the company could not absorb high-impact, low-probability events without refinancing. KDP recently increased the size of its 364-day credit facility and issued notes to increase liquidity given the current uncertain environment. The company has debt maturing next year, and it could use these funds to repay a portion of the maturities. That said, we believe KDP has a strong standing in the credit markets, strong relationships with its banks, and EBITDA cushion of over 15% on its debt-to-EBITDA covenant.

Principal Liquidity Sources	Principal Liquidity Uses
• Cash of about $197 million as of March 31, 2020; • Full availability under its $2.4 billion revolving credit facility maturing 2023 and $1.5 billion available under its 364-day facility; • Funds from operations of more than $2.6 billion; • Working capital inflow of more than $200 million in 2020; and • Debt issuance of $1.5 billion.	• Repayment of almost $1.2 billion of debt including commercial paper, other debt maturities, and amortization in 2020; • Seasonal working capital requirement of over $100 million; • Capex of $425 million in 2020; and • Dividends of about $850 million in 2020.

Debt maturities

As of April 30, 2020:

- 2020: $350 million
- 2021: $2.35 billion
- 2022: $3.35 billion
- 2023: $3.58 billion
- Thereafter: $8.23 billion

Covenant Analysis

Compliance expectations

We forecast KDP will maintain a covenant cushion of above 15% over the next two years. This calculation includes pro forma synergies.

Requirements

KDP is subject to maintenance financial covenants under its senior unsecured revolver, 364-day credit facility, and term loan executed in 2019. The company is subject to a leverage covenant of 5x that tightens to 4.5x beginning June 30, 2020, and 4x beginning March 31, 2021.

Environmental, Social, And Governance

We view environmental and social credit factors for KDP as broadly in line with those of industry peers, especially given its coffee business and portfolio of noncarbonated drinks, which add diversity to its CSD portfolio. Ongoing changing consumer tastes away from traditional CSDs and societal efforts to reduce the sugar content of beverages has reduced demand for certain soft drinks. In response, KDP invests in diversifying its portfolio toward categories like premium water, sports, and energy. This strategy has yielded good organic sales growth while improving the portfolio mix toward faster-growing, more socially acceptable offerings. KDP so far has not been materially affected by efforts to raise taxes on sugary foods. These efforts tend to temporarily reduce sales and consumption, but sales typically rebound after a year or so. For example, Mexico enacted a sugar tax in 2014 and consumption did fall in the subsequent year, but stabilized thereafter. The global anti-plastic movement is also an inherent environmental risk factor, and KDP is focusing on using fully recycled and recyclable products in its packaging. The company's coffee pods are 100% recyclable in Canada, and its pods in the U.S. will all be recyclable by the end of 2020. The modest capex requirements and cost saving of increasing recycled inputs should not compromise KDP's strong free cash flow generation.

Issue Ratings - Subordination Risk Analysis

Capital structure

KDP's capital structure consists of senior unsecured debt, all of which is issued at the KDP level. The company has no secured debt or priority subsidiary debt.

Analytical conclusions

KDP's unsecured debt is rated 'BBB', the same as the issuer credit rating, because we believe that any subordination risk that may exist is not significant enough to warrant a notch down.

Reconciliation

Table 6

Reconciliation Of Keurig Dr Pepper Inc. Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. $)

	--Rolling 12 months ended March 31, 2020--									
Keurig Dr Pepper Inc. reported amounts										
	Debt	**Shareholders' equity**	**Revenue**	**EBITDA**	**Operating income**	**Interest expense**	**S&P Global Ratings' adjusted EBITDA**	**Cash flow from operations**	**Dividends**	**Capital expenditure**
	14,646.0	22,640.0	11,229.0	3,068.0	2,346.0	638.0	3,508.0	2,297.0	845.0	469.0
S&P Global Ratings' adjustments										
Cash taxes paid	--	--	--	--	--	--	(489.0)	--	--	--
Cash interest paid	--	--	--	--	--	--	(457.0)	--	--	--
Reported lease liabilities	880.0	--	--	--	--	--	--	--	--	--
Operating leases	--	--	--	90.0	19.2	19.2	(19.2)	70.8	--	--
Postretirement benefit obligations/deferred compensation	17.4	--	--	--	--	--	--	--	--	--
Accessible cash and liquid investments	(187.2)	--	--	--	--	--	--	--	--	--
Share-based compensation expense	--	--	--	69.0	--	--	--	--	--	--
Nonoperating income (expense)	--	--	--	--	(29.0)	--	--	--	--	--
Debt: Other	315.0	--	--	--	--	--	--	--	--	--
EBITDA: Restructuring costs	--	--	--	305.0	305.0	--	--	--	--	--
EBITDA: Derivatives	--	--	--	(7.0)	(7.0)	--	--	--	--	--
EBITDA: Other	--	--	--	(17.0)	(17.0)	--	--	--	--	--
Depreciation and amortization: Impairment charges/(reversals)	--	--	--	--	(24.0)	--	--	--	--	--
Total adjustments	1,025.2	0.0	0.0	440.0	247.2	19.2	(965.2)	70.8	0.0	0.0
S&P Global Ratings' adjusted amounts										
	Debt	**Equity**	**Revenue**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**	**Cash flow from operations**	**Dividends**	**Capital expenditure**
	15,671.2	22,640.0	11,229.0	3,508.0	2,593.2	657.2	2,542.8	2,367.8	845.0	469.0

Ratings Score Snapshot

Issuer Credit Rating

BBB/Stable/A-2

Business risk: Strong

- **Country risk:** Very low
- **Industry risk:** Low
- **Competitive position:** Strong

Financial risk: Significant

- **Cash flow/leverage:** Significant

Anchor: bbb

Modifiers

- **Diversification/portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Neutral (no impact)

Stand-alone credit profile : bbb

Related Criteria

- Guidance | Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria - Corporates - General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | Industrials: Key Credit Factors For The Branded Nondurables Industry, May 7, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012

- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

	Financial Risk Profile					
Business Risk Profile	Minimal	Modest	Intermediate	**Significant**	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	**bbb**	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Ratings Detail (As Of May 18, 2020)*

Keurig Dr Pepper Inc.	
Issuer Credit Rating	BBB/Stable/A-2
Commercial Paper	
Local Currency	A-2
Senior Secured	BBB
Senior Unsecured	BBB
Issuer Credit Ratings History	
14-May-2018	BBB/Stable/A-2
29-Jan-2018	BBB+/Watch Neg/A-2
13-Nov-2013	BBB+/Stable/A-2

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.