PepsiCo's objective was to reposition itself as a beverage and snack food company, strengthen its balance sheet, and create more consistent earning growth. PepsiCo received a one-time distribution from Tricon of $4.7 billion, $3.7 billion of which was used to pay off short-term debt. The balance was earmarked for stock repurchases. In 1998, PepsiCo acquired Tropicana Products, which controlled more than 40 percent of the US chilled orange juice market. Because of the divestiture of KFC, Pizza Hut, and Taco Bell, PepsiCo sales fell by $11.3 billion and assets fell by $7.0 billion between 1997 and 1999. Profitability, however, soared. Operating margins rose from 11 percent in 1997 to 14 percent in 1999 and ROA rose from 11 percent in 1997 to 16 percent in 1999. By focusing on high cash flow market leaders, PepsiCo raised profitability while decreasing its asset base.

Fast-Food Industry

According to the National Restaurant Association (NRA), food service sales increased by 5.4 percent to $358 billion in 1999. More than 800,000 restaurants and food outlets made up the US restaurant industry, which employed 11 million people. Sales were highest in the full-service, sit-down sector, which grew 7 percent to $121 billion. Fast-food sales grew at a slower rate, rising about 5 percent to $110 billion. Fast-food sales surpassed the full-service sector during the mid-1990s; however, maturation of the fast-food sector and rising incomes among many Americans helped full-service restaurants again overtake fast-food as the largest sector in the restaurant industry.

Major Fast-Food Segments

Eight major segments made up the fast-food segment of the restaurant industry: sandwich chains, pizza chains, family restaurants, grill buffet chains, dinner houses, chicken chains, non-dinner concepts, and other chains. Sales data for the leading restaurant chains in each segment are shown in Exhibit 2. Most striking is the dominance of McDonald's, which had sales of more than $19 billion in 1999. McDonald's accounted for 15 percent of the sales of the nation's top 100 restaurant chains. To put McDonald's dominance into perspective, the second largest chain—Burger King—held less than 7 percent of the market. The full-service and fast-food segments were expected to make up about 65 percent of total food service industry sales in 2000.

Sandwich chains made up the largest segment of the fast-food market. McDonald's controlled 35 percent of the sandwich segment, while Burger King ran a distant second with a 16 percent market share. Despite continued success by some chains like McDonald's, Carl's Jr., Jack in the Box, Wendy's, and White Castle, other chains like Hardee's, Burger King, Taco Bell, and Checker's were struggling. McDonald's generated the greatest per store sales of about $1.5 million per year. The average US chain generated $800,000 in sales per store. Per store sales at Burger King remained flat and Hardee's per store sales declined by 10 percent. Franchisees at Burger King complained of leadership problems within the corporate parent (London-based Diageo PLC), an impending increase in royalties and franchise fees, and poor advertising. Hardee's corporate parent (CKE Enterprises), which also owned Carl's Jr. and Taco Bueno, planned to franchise many of its company-owned Hardee's restaurants and to allow the system to shrink as low performing units were closed. It also planned to refocus Hardee's strategy in the southeastern part of the United States, where brand loyalty remained strong.

Dinner houses made up the second largest and fastest growing fast-food segment. Sales of dinner houses increased by more than 13 percent during the year, surpassing the average increase of six percent among all fast-food chains. Much of the growth in dinner houses came from new unit construction, a marked contrast with other fast-food chains, which had already slowed US construction because of market saturation. Much of the new unit construction took place in new suburban markets and small towns. Applebee's and Red Lobster dominated the dinner house segment. Each chain generated more than $2 billion in sales in 1999. The fastest growing dinner houses, however, were chains generating less than $500 million in sales such as On The Border, The Cheesecake Factory, O'Charley's, Romano's Macaroni Grill, and Hooters. Each of these chains increased sales by more than 20 percent.

Increased growth among dinner houses came at the expense of slower growth among sandwich chains, pizza chains, grilled buffet chains, and family restaurants. "Too many restaurants chasing the same customers" was responsible for much of the slower growth in these other fast-food categories. However, sales growth within each segment differed from one chain to another. In the family segment, for example, Friendly's and Shoney's were forced to shut down restaurants because of declining profits, but Steak 'n Shake and Cracker Barrel expanded their restaurant base by more than 10 percent. Within the pizza segment, Pizza Hut and Little Caesars closed underperforming restaurants, but Papa John's and Chuck E. Cheese's continued to aggressively grow their US restaurant bases. The hardest hit segment was grilled buffet chains, which generated the lowest increase in sales of less than 4 percent. Dinner houses, because of