

PEPSICO INC  
Form 10-Q  
April 28, 2011  
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 19, 2011 (12 weeks)

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-1183

PepsiCo, Inc.

(Exact Name of Registrant as Specified in its Charter)

North Carolina  
(State or Other Jurisdiction of

13-1584302  
(I.R.S. Employer

Incorporation or Organization)

Identification No.)

700 Anderson Hill Road, Purchase, New York  
(Address of Principal Executive Offices)

10577  
(Zip Code)

914-253-2000

(Registrant's Telephone Number, Including Area Code)

N/A

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Edgar Filing: PEPSICO INC - Form 10-Q

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

(Check one):

Large accelerated filer   
Non-accelerated filer

Accelerated filer   
Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES  NO

Number of shares of Common Stock outstanding as of April 21, 2011: 1,580,653,782

**Table of Contents****PEPSICO, INC. AND SUBSIDIARIES****INDEX**

	Page No.
<b><u>Part I Financial Information</u></b>	
Item 1. <u>Condensed Consolidated Financial Statements</u>	3
<u>Condensed Consolidated Statement of Income 12 Weeks Ended March 19, 2011 and March 20, 2010</u>	3
<u>Condensed Consolidated Statement of Cash Flows 12 Weeks Ended March 19, 2011 and March 20, 2010</u>	4-5
<u>Condensed Consolidated Balance Sheet March 19, 2011 and December 25, 2010</u>	6-7
<u>Condensed Consolidated Statement of Equity 12 Weeks Ended March 19, 2011 and March 20, 2010</u>	8
<u>Condensed Consolidated Statement of Comprehensive Income 12 Weeks Ended March 19, 2011 and March 20, 2010</u>	9
<u>Notes to the Condensed Consolidated Financial Statements</u>	10-23
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	24-39
<u>Report of Independent Registered Public Accounting Firm</u>	40
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	41
Item 4. <u>Controls and Procedures</u>	41
<b><u>Part II Other Information</u></b>	
Item 1. <u>Legal Proceedings</u>	42
Item 1A. <u>Risk Factors</u>	42
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	43-44
Item 4. <u>Removed and Reserved</u>	44
Item 6. <u>Exhibits</u>	44

**Table of Contents**

## PART I FINANCIAL INFORMATION

## ITEM 1. Condensed Consolidated Financial Statements.

## PEPSICO, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENT OF INCOME

(in millions except per share amounts, unaudited)

	12 Weeks Ended	
	3/19/11	3/20/10
<b>Net Revenue</b>	<b>\$ 11,937</b>	<b>\$ 9,368</b>
Cost of sales	5,447	4,463
Selling, general and administrative expenses	4,739	4,049
Amortization of intangible assets	25	16
<b>Operating Profit</b>	<b>1,726</b>	<b>840</b>
Bottling equity income		709
Interest expense	(180)	(154)
Interest income	17	6
Income before income taxes	1,563	1,401
Provision for/(Benefit from) income taxes	419	(33)
Net income	1,144	1,434
Less: Net income attributable to noncontrolling interests	1	4
<b>Net Income Attributable to PepsiCo</b>	<b>\$ 1,143</b>	<b>\$ 1,430</b>
<b>Net Income Attributable to PepsiCo per Common Share</b>		
<b>Basic</b>	<b>\$ 0.72</b>	<b>\$ 0.90</b>
<b>Diluted</b>	<b>\$ 0.71</b>	<b>\$ 0.89</b>
Cash dividends declared per common share	\$ 0.48	\$ 0.45

See accompanying notes to the condensed consolidated financial statements.

**Table of Contents**

## PEPSICO, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions, unaudited)

	12 Weeks Ended	
	3/19/11	3/20/10
<b>Operating Activities</b>		
Net income	\$ 1,144	\$ 1,434
Depreciation and amortization	523	376
Stock-based compensation expense	72	47
Cash payments for restructuring charges	(1)	(26)
Merger and integration costs	55	321
Cash payments for merger and integration costs	(117)	(85)
Gain on previously held equity interests in The Pepsi Bottling Group, Inc. (PBG) and PepsiAmericas, Inc. (PAS)		(958)
Asset write-off		145
Non-cash foreign exchange loss related to Venezuela devaluation		120
Excess tax benefits from share-based payment arrangements	(24)	(29)
Pension and retiree medical plan contributions	(59)	(640)
Pension and retiree medical plan expenses	119	113
Bottling equity income, net of dividends		46
Deferred income taxes and other tax charges and credits	(98)	(127)
Change in accounts and notes receivable	(271)	(155)
Change in inventories	(77)	309
Change in prepaid expenses and other current assets	(137)	(98)
Change in accounts payable and other current liabilities	(1,028)	(616)
Change in income taxes payable	362	186
Other, net	(83)	(122)
<b>Net Cash Provided by Operating Activities</b>	<b>380</b>	<b>241</b>
<b>Investing Activities</b>		
Capital spending	(433)	(274)
Sales of property, plant and equipment	12	16
Acquisitions of PBG and PAS, net of cash and cash equivalents acquired		(2,833)
Acquisition of manufacturing and distribution rights from Dr Pepper Snapple Group, Inc. (DPSG)		(900)
Acquisition of Wimm-Bill-Dann Foods OJSC (WBD), net of cash and cash equivalents acquired	(2,428)	
Investment in WBD	(164)	
Other acquisitions and investments in noncontrolled affiliates	(28)	(15)
Short-term investments, by original maturity		
More than three months purchases		(4)
More than three months maturities	6	8

Three months or less, net	<b>57</b>	(6)
Other investing, net	<b>(1)</b>	(3)
<b>Net Cash Used For Investing Activities</b>	<b>(2,979)</b>	(4,011)

(Continued on following page)

**Table of Contents**

## PEPSICO, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (continued)

(in millions, unaudited)

	12 Weeks Ended	
	3/19/11	3/20/10
<b>Financing Activities</b>		
Proceeds from issuances of long-term debt	\$ 9	\$ 4,216
Payments of long-term debt	(10)	(7)
Short-term borrowings, by original maturity		
More than three months proceeds	21	21
More than three months payments	(64)	(3)
Three months or less, net	1,160	1,010
Cash dividends paid	(769)	(712)
Share repurchases common	(361)	(735)
Share repurchases preferred	(2)	(1)
Proceeds from exercises of stock options	218	267
Excess tax benefits from share-based payment arrangements	24	29
Acquisition of noncontrolling interest in Lebedyansky from PBG		(159)
Other financing		(5)
<b>Net Cash Provided by Financing Activities</b>	<b>226</b>	<b>3,921</b>
Effect of exchange rate changes on cash and cash equivalents	92	(145)
<b>Net (Decrease)/Increase in Cash and Cash Equivalents</b>	<b>(2,281)</b>	<b>6</b>
<b>Cash and Cash Equivalents, Beginning of Year</b>	<b>5,943</b>	<b>3,943</b>
<b>Cash and Cash Equivalents, End of Period</b>	<b>\$ 3,662</b>	<b>\$ 3,949</b>
Non-cash activity:		
Issuance of common stock and equity awards in connection with our acquisitions of PBG and PAS, as reflected in investing and financing activities		\$ 4,451

See accompanying notes to the condensed consolidated financial statements.

Table of Contents

PEPSICO, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEET

(in millions)

	(Unaudited) 3/19/11	12/25/10
<b>Assets</b>		
Current Assets		
Cash and cash equivalents	<b>\$ 3,662</b>	\$ 5,943
Short-term investments	<b>367</b>	426
Accounts and notes receivable, less allowance: 3/11 \$157, 12/10 \$144	<b>6,937</b>	6,323
Inventories		
Raw materials	<b>1,907</b>	1,654
Work-in-process	<b>173</b>	128
Finished goods	<b>1,751</b>	1,590
	<b>3,831</b>	3,372
Prepaid expenses and other current assets	<b>1,715</b>	1,505
Total Current Assets	<b>16,512</b>	17,569
Property, Plant and Equipment	<b>34,797</b>	33,041
Accumulated Depreciation	<b>(14,468)</b>	(13,983)
	<b>20,329</b>	19,058
Amortizable Intangible Assets, net	<b>2,477</b>	2,025
Goodwill	<b>15,824</b>	14,661
Other Nonamortizable Intangible Assets	<b>15,418</b>	11,783
Nonamortizable Intangible Assets	<b>31,242</b>	26,444
Investments in Noncontrolled Affiliates	<b>1,408</b>	1,368
Other Assets	<b>1,117</b>	1,689
Total Assets	<b>\$ 73,085</b>	\$ 68,153



(Continued on following page)

**Table of Contents**

## PEPSICO, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEET (continued)

(in millions except per share amounts)

	(Unaudited)	
	3/19/11	12/25/10
<b>Liabilities and Equity</b>		
Current Liabilities		
Short-term obligations	\$ 6,256	\$ 4,898
Accounts payable and other current liabilities	10,243	10,923
Income taxes payable	341	71
Total Current Liabilities	16,840	15,892
Long-term Debt Obligations	20,942	19,999
Other Liabilities	6,657	6,729
Deferred Income Taxes	4,972	4,057
Total Liabilities	49,411	46,677
Commitments and Contingencies		
Preferred Stock, no par value	41	41
Repurchased Preferred Stock	(152)	(150)
PepsiCo Common Shareholders' Equity		
Common stock, par value 1 2/3 cents per share:		
Authorized 3,600 shares, issued 3/11 and 12/10 1,865 shares	31	31
Capital in excess of par value	4,407	4,527
Retained earnings	37,466	37,090
Accumulated other comprehensive loss	(3,035)	(3,630)
Less: repurchased common stock, at cost:		
3/11 and 12/10 284 shares	(16,773)	(16,745)
Total PepsiCo Common Shareholders' Equity	22,096	21,273
Noncontrolling interests	1,689	312
Total Equity	23,674	21,476
Total Liabilities and Equity	\$ 73,085	\$ 68,153

See accompanying notes to the condensed consolidated financial statements.

**Table of Contents**

## PEPSICO, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENT OF EQUITY

(in millions, unaudited)

	12 Weeks Ended			
	3/19/11		3/20/10	
	Shares	Amount	Shares	Amount
<b>Preferred Stock</b>	<b>0.8</b>	<b>\$ 41</b>	0.8	\$ 41
<b>Repurchased Preferred Stock</b>				
Balance, beginning of year	(0.6)	(150)	(0.6)	(145)
Redemptions	( )	(2)	( )	(1)
Balance, end of period	(0.6)	(152)	(0.6)	(146)
<b>Common Stock</b>				
Balance, beginning of year	1,865	31	1,782	30
Shares issued in connection with our acquisitions of PBG and PAS			83	1
Balance, end of period	1,865	31	1,865	31
<b>Capital in Excess of Par Value</b>				
Balance, beginning of year		4,527		250
Stock-based compensation expense		72		47
Stock option exercises/RSUs converted <sup>(a)</sup>		(160)		(248)
Withholding tax on RSUs converted		(40)		(29)
Equity issued in connection with our acquisitions of PBG and PAS				4,451
Other		8		39
Balance, end of period		4,407		4,510
<b>Retained Earnings</b>				
Balance, beginning of year		37,090		33,805
Net income attributable to PepsiCo		1,143		1,430
Cash dividends declared common		(762)		(744)
Cash dividends declared RSUs		(5)		(2)
Other				7
Balance, end of period		37,466		34,496
<b>Accumulated Other Comprehensive Loss</b>				
Balance, beginning of year		(3,630)		(3,794)
Currency translation adjustment		617		120
Cash flow hedges, net of tax:				

Edgar Filing: PEPSICO INC - Form 10-Q

Net derivative gains/(losses)	<b>8</b>		(48)	
Reclassification of net losses to net income	<b>4</b>		18	
Reclassification of pension and retiree medical (gains)/losses to net income, net of tax	<b>(3)</b>		136	
Unrealized losses on securities, net of tax	<b>(13)</b>		(1)	
Other	<b>(18)</b>			
Balance, end of period	<b>(3,035)</b>		(3,569)	
<b>Repurchased Common Stock</b>				
Balance, beginning of year	<b>(284)</b>	<b>(16,745)</b>	(217)	(13,383)
Share repurchases	<b>(7)</b>	<b>(413)</b>	(14)	(940)
Stock option exercises	<b>5</b>	<b>296</b>	7	434
Other	<b>2</b>	<b>89</b>	(15)	107
Balance, end of period	<b>(284)</b>	<b>(16,773)</b>	(239)	(13,782)
<b>Total Common Shareholders Equity</b>		<b>22,096</b>		21,686
<b>Noncontrolling Interests</b>				
Balance, beginning of year		<b>312</b>		638
Net income attributable to noncontrolling interests		<b>1</b>		4
Contributions from/(distributions to) noncontrolling interests, net		<b>1,348</b>		(352)
Currency translation adjustment		<b>28</b>		(15)
Balance, end of period		<b>1,689</b>		275
<b>Total Equity</b>		<b>\$ 23,674</b>		\$ 21,856

(a) Includes total tax benefits of \$13 million in 2011 and \$18 million in 2010. See accompanying notes to the condensed consolidated financial statements.

**Table of Contents**

PEPSICO, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENT  
 OF COMPREHENSIVE INCOME  
 (in millions, unaudited)

	12 Weeks Ended	
	3/19/11	3/20/10
Net Income	<b>\$ 1,144</b>	\$ 1,434
Other Comprehensive Income		
Currency translation adjustment	<b>645</b>	105
Cash flow hedges, net of tax:		
Net derivative gains/(losses)	<b>8</b>	(48)
Reclassification of net losses to net income	<b>4</b>	18
Reclassification of pension and retiree medical (gains)/losses to net income, net of tax	<b>(3)</b>	136
Unrealized losses on securities, net of tax	<b>(13)</b>	(1)
Other	<b>(18)</b>	
	<b>623</b>	210
Comprehensive Income	<b>1,767</b>	1,644
Comprehensive (income)/loss attributable to noncontrolling interests	<b>(29)</b>	11
<b>Comprehensive Income Attributable to PepsiCo</b>	<b>\$ 1,738</b>	\$ 1,655

See accompanying notes to the condensed consolidated financial statements.

---

**Table of Contents**

PEPSICO, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

**Basis of Presentation and Our Divisions**

***Basis of Presentation***

Our Condensed Consolidated Balance Sheet as of March 19, 2011 and the Condensed Consolidated Statements of Income, Cash Flows, Equity and Comprehensive Income for the 12 weeks ended March 19, 2011 and March 20, 2010 have not been audited. These statements have been prepared on a basis that is substantially consistent with the accounting principles applied in our Annual Report on Form 10-K for the fiscal year ended December 25, 2010 and in our Current Report on Form 8-K dated March 31, 2011. In our opinion, these financial statements include all normal and recurring adjustments necessary for a fair presentation. The results for the 12 weeks are not necessarily indicative of the results expected for the full year.

While the majority of our results are reported on a period basis, most of our international operations report on a monthly calendar basis for which the months of January and February are reflected in our first quarter results.

On February 26, 2010, we completed our acquisitions of PBG and PAS. The results of the acquired companies in the U.S. and Canada are reflected in our condensed consolidated results as of the acquisition date, and the international results of the acquired companies have been reported as of the beginning of our second quarter of 2010, consistent with our monthly international reporting calendar. Prior to our acquisitions of PBG and PAS, we recorded our share of equity income or loss from the acquired companies in bottling equity income in our income statement. Additionally, in the first quarter of 2010, in connection with our acquisitions of PBG and PAS, we recorded a gain on our previously held equity interests of \$958 million, comprising \$735 million which was non-taxable and recorded in bottling equity income and \$223 million related to the reversal of deferred tax liabilities associated with these previously held equity interests. Our share of income or loss from noncontrolled affiliates is reflected as a component of selling, general and administrative expenses. See also *Acquisitions* and *Items Affecting Comparability* in Management's Discussion and Analysis of Financial Condition and Results of Operations.

In the first quarter of 2011, Quaker Foods North America (QFNA) changed its method of accounting for certain U.S. inventories from the last-in, first-out (LIFO) method to the average cost method. This change is considered preferable by management as we believe that the average cost method of accounting for all U.S. foods inventories will improve our financial reporting by better matching revenues and expenses and better reflecting the current value of inventory. In addition, the change from the LIFO method to the average cost method will enhance the comparability of QFNA's financial results with our other food businesses, as well as with peer companies where the average cost method is widely used. The impact of this change on consolidated net income in the first quarter of 2011 was approximately \$9 million (or less than a penny per share). Prior periods were not restated as the impact of the change on previously issued financial statements was not considered material.

Our significant interim accounting policies include the recognition of a pro rata share of certain estimated annual sales incentives, and certain advertising and marketing costs, generally in proportion to revenue, and the recognition of income taxes using an estimated annual effective tax rate. Raw materials, direct labor and plant overhead, as well as purchasing and receiving costs, costs directly related to production planning, inspection costs and raw material handling facilities, are included in cost of sales. The costs of moving, storing and delivering finished product are

included in selling, general and administrative expenses.



**Table of Contents**

The following information is unaudited. Tabular dollars are in millions, except per share amounts. All per share amounts reflect common per share amounts, assume dilution unless otherwise noted, and are based on unrounded amounts. Certain reclassifications were made to the prior year's amounts to conform to the 2011 presentation. This report should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended December 25, 2010 and our Current Report on Form 8-K dated March 31, 2011, in which we reclassified historical segment information on a basis consistent with our current segment reporting structure.

***Our Divisions***

We are organized into four business units, as follows:

1. PepsiCo Americas Foods (PAF), which includes Frito-Lay North America (FLNA), Quaker Foods North America (QFNA) and all of our Latin American food and snack businesses (LAF), including our Sabritas and Gamesa businesses in Mexico;
2. PepsiCo Americas Beverages (PAB), which includes PepsiCo Beverages Americas and Pepsi Beverages Company;
3. PepsiCo Europe, which includes all beverage, food and snack businesses in Europe; and
4. PepsiCo Asia, Middle East and Africa (AMEA), which includes all beverage, food and snack businesses in AMEA.

Our four business units comprise six reportable segments (also referred to as divisions), as follows:

FLNA,

QFNA,

LAF,

PAB,

Europe, and

AMEA.



**Table of Contents**

	12 Weeks Ended			
	Net Revenue		Operating Profit	
	3/19/11	3/20/10	3/19/11	3/20/10
FLNA	\$ 2,904	\$ 2,864	\$ 774	\$ 728
QFNA	640	683	214	195
LAF	1,108	983	171	145
PAB	4,531	2,765	558	73
Europe	1,626	1,044	63	118
AMEA	1,128	1,029	146	155
Total division	11,937	9,368	1,926	1,414
Corporate Unallocated				
Net impact of mark-to-market on commodity hedges			31	46
Merger and integration costs			(42)	(88)
Venezuela currency devaluation				(129)
Asset write-off				(145)
Foundation contribution				(100)
Other			(189)	(158)
	\$ 11,937	\$ 9,368	\$ 1,726	\$ 840

	Total Assets	
	3/19/11	12/25/10
FLNA	\$ 6,072	\$ 6,027
QFNA	1,204	1,217
LAF	4,041	4,053
PAB	31,981	31,622
Europe <sup>(a)</sup>	19,824	13,032
AMEA	5,629	5,569
Total division	68,751	61,520
Corporate <sup>(b)</sup>	4,091	6,394
Investments in bottling affiliates	243	239
	\$ 73,085	\$ 68,153

<sup>(a)</sup> Change in 2011 relates primarily to our acquisition of WBD.

<sup>(b)</sup> Corporate assets consist principally of cash and cash equivalents, short-term investments, derivative instruments and property, plant and equipment.

**Table of Contents****Acquisitions*****PBG and PAS***

On February 26, 2010, we acquired PBG and PAS to create a more fully integrated supply chain and go-to-market business model, improving the effectiveness and efficiency of the distribution of our brands and enhancing our revenue growth. The total purchase price was approximately \$12.6 billion, which included \$8.3 billion of cash and equity and the fair value of our previously held equity interests in PBG and PAS of \$4.3 billion. The acquisitions were accounted for as business combinations, and, accordingly, the identifiable assets acquired and liabilities assumed were recorded at their estimated fair values at the date of acquisition. Our fair market valuations of the identifiable assets acquired and liabilities assumed have been completed and the final valuations did not materially differ from those fair values reported as of December 25, 2010.

The following table presents unaudited consolidated pro forma financial information as if the closing of our acquisitions of PBG and PAS had occurred on December 27, 2009 for purposes of the financial information presented for the 12 weeks ended March 20, 2010.

	(unaudited) 12 Weeks Ended 3/20/10
Net Revenue	\$ 11,112
Net Income Attributable to PepsiCo	\$ 966
Net Income Attributable to PepsiCo per Common Share Diluted	\$ 0.58

The unaudited consolidated pro forma financial information was prepared in accordance with the acquisition method of accounting under existing standards, and the regulations of the U.S. Securities and Exchange Commission, and is not necessarily indicative of the results of operations that would have occurred if our acquisitions of PBG and PAS had been completed on the date indicated, nor is it indicative of the future operating results of PepsiCo.

The historical unaudited consolidated financial information has been adjusted to give effect to pro forma events that are (1) directly attributable to the acquisitions, (2) factually supportable, and (3) expected to have a continuing impact on the combined results of PepsiCo, PBG and PAS.

The unaudited pro forma results have been adjusted with respect to certain aspects of our acquisitions of PBG and PAS to reflect:

the consummation of the acquisitions;

consolidation of PBG and PAS which are now owned 100% by PepsiCo and the corresponding gain resulting from the remeasurement of our previously held equity interests in PBG and PAS;

the elimination of related party transactions between PepsiCo and PBG, and PepsiCo and PAS;

changes in assets and liabilities to record their acquisition date fair values and changes in certain expenses resulting therefrom; and

---

**Table of Contents**

additional indebtedness, including, but not limited to, debt issuance costs and interest expense, incurred in connection with the acquisitions.

The unaudited pro forma results do not reflect future events that may occur after the acquisitions, including, but not limited to, the anticipated realization of ongoing savings from operating synergies in subsequent periods. They also do not give effect to certain one-time charges we expect to incur in connection with the acquisitions, including, but not limited to, charges that are expected to achieve ongoing cost savings and synergies.

***WBD***

On February 3, 2011, we completed the previously announced acquisition of ordinary shares, American Depositary Shares (ADSs) and Global Depositary Shares (GDSs) of WBD, a company incorporated in the Russian Federation, which represented in the aggregate approximately 66% of WBD's outstanding ordinary shares, pursuant to the purchase agreement dated December 1, 2010 between PepsiCo and certain selling shareholders of WBD for approximately \$3.8 billion. The acquisition increased our total ownership of WBD to approximately 77%. The total consideration transferred was approximately \$5.8 billion, which included the \$3.8 billion of cash (or \$2.4 billion, net of cash and cash equivalents acquired), the fair value of our previously held equity interest in WBD of \$0.7 billion and the fair value of the remaining noncontrolling interests in WBD of \$1.3 billion. The preliminary estimates of the fair value of the identifiable assets acquired and liabilities assumed in WBD as of the acquisition date include goodwill and other intangible assets of \$4.8 billion; property, plant and equipment of \$1.2 billion; debt obligations of \$1.1 billion; and other net assets of \$0.9 billion, all of which are recorded in our Europe segment. The preliminary estimates of the fair value of identifiable assets acquired and liabilities assumed are subject to revisions, which may result in adjustments to the preliminary values discussed above as valuations are finalized. We expect to finalize these amounts as soon as possible but no later than by the end of 2011.

Under the guidance on accounting for business combinations, merger and integration costs are not included as components of consideration transferred but are accounted for as expenses in the period in which the costs are incurred. See *Merger and Integration Charges* for details on the expenses incurred during 2011.

On March 10, 2011, we commenced our previously announced tender offers in Russia and the United States for all outstanding ordinary shares and ADSs of WBD for 3,883.70 Russian rubles per ordinary share and 970.925 Russian rubles per ADS. The Russian offer is being made to all holders of ordinary shares and the U.S. offer is being made to all holders of ADSs. The U.S. offer price is equal to the Russian offer share price after adjustment for the four-to-one ratio of ADSs to shares. The U.S. offer price will be converted to U.S. dollars at the spot market conversion rates available to the ADS depository during the conversion period and paid to tendering ADS holders using the weighted average of the conversion rates, less certain fees under the ADS depository agreement and applicable taxes, if any. The Russian offer will expire on May 19, 2011 and the U.S. offer is scheduled to expire on May 16, 2011.

**Table of Contents****Intangible Assets**

	<b>3/19/11</b>	12/25/10
<b><i>Amortizable intangible assets, net</i></b>		
Acquired franchise rights	<b>\$ 968</b>	\$ 949
Reacquired franchise rights	<b>110</b>	110
Brands	<b>1,526</b>	1,463
Other identifiable intangibles	<b>1,142</b>	747
	<b>3,746</b>	3,269
Accumulated amortization	<b>(1,269)</b>	(1,244)
	<b>\$ 2,477</b>	\$ 2,025

**Table of Contents**

The change in the book value of nonamortizable intangible assets is as follows:

	Balance 12/25/10	Acquisitions	Translation and Other	Balance 3/19/11
<b>FLNA</b>				
Goodwill	\$ 313	\$	\$ 4	\$ 317
Brands	31		1	32
	344		5	349
<b>QFNA</b>				
Goodwill	175			175
<b>LAF</b>				
Goodwill	497		1	498
Brands	143		1	144
	640		2	642
<b>PAB</b>				
Goodwill	9,946	24	9	9,979
Reacquired franchise rights	7,283	20	26	7,329
Acquired franchise rights	1,565		2	1,567
Brands	182	8	1	191
Other	10			10
	18,986	52	38	19,076
<b>Europe<sup>(a)</sup></b>				
Goodwill	3,040	978	150	4,168
Reacquired franchise rights	793		32	825
Acquired franchise rights	227		9	236
Brands	1,380	3,400	134	4,914
	5,440	4,378	325	10,143
<b>AMEA</b>				
Goodwill	690		(3)	687
Brands	169		1	170
	859		(2)	857
Total goodwill	14,661	1,002	161	15,824
Total reacquired franchise rights	8,076	20	58	8,154



Edgar Filing: PEPSICO INC - Form 10-Q

Total acquired franchise rights	1,792		11	<b>1,803</b>
Total brands	1,905	3,408	138	<b>5,451</b>
Total other	10			<b>10</b>
	\$ 26,444	\$ 4,430	\$ 368	<b>\$ 31,242</b>

<sup>(a)</sup> Net increases in 2011 relate primarily to our acquisition of WBD.

**Table of Contents****Stock-Based Compensation**

For the 12 weeks ended March 19, 2011, we recognized stock-based compensation expense of \$79 million (\$72 million recorded as stock-based compensation expense and \$7 million included in merger and integration charges). For the 12 weeks ended March 20, 2010, we recognized stock-based compensation expense of \$74 million (\$47 million recorded as stock-based compensation expense and \$27 million included in merger and integration charges).

For the 12 weeks ended March 19, 2011, we granted 6.4 million stock options and 5.1 million RSUs at a weighted-average grant price of \$63.75, under the terms of our 2007 Long-Term Incentive Plan. We did not grant any stock options or RSUs in the 12 weeks ended March 20, 2010, as our annual equity award was delayed until the second quarter in the prior year, in connection with our acquisitions of PBG and PAS.

Our weighted-average Black-Scholes fair value assumptions are as follows:

	12 Weeks Ended	
	3/19/11	3/20/10
Expected life	<b>6 yrs.</b>	4 yrs.
Risk free interest rate	<b>2.6%</b>	1.6%
Expected volatility <sup>(a)</sup>	<b>16%</b>	18%
Expected dividend yield	<b>2.9%</b>	2.8%

<sup>(a)</sup> Reflects movements in our stock price over the most recent historical period equivalent to the expected life.

**Table of Contents****Pension and Retiree Medical Benefits**

The components of net periodic benefit cost for pension and retiree medical plans are as follows:

	12 Weeks Ended					
	Pension				Retiree Medical	
	3/19/11	3/20/10	3/19/11	3/20/10	3/19/11	3/20/10
	U.S.		International			
Service cost	\$ 82	\$ 61	\$ 17	\$ 14	\$ 12	\$ 12
Interest cost	126	98	21	18	20	20
Expected return on plan assets	(162)	(125)	(24)	(22)	(3)	
Amortization of prior service cost/(benefit)	3	3			(7)	(4)
Amortization of experience loss	33	25	7	4	3	1
	82	62	21	14	25	29
Settlement/Curtailment (gain)/loss	(9)					
Special termination benefits	10	8			1	
Total expense	\$ 83	\$ 70	\$ 21	\$ 14	\$ 26	\$ 29

**Income Taxes**

A rollforward of our reserves for all federal, state and foreign tax jurisdictions, is as follows:

	3/19/11	12/25/10
Balance, beginning of year	\$ 2,022	\$ 1,731
Additions for tax positions related to the current year	41	204
Additions for tax positions from prior years		517
Reductions for tax positions from prior years	(29)	(391)
Settlement payments	(87)	(30)
Statute of limitations expiration	(4)	(7)
Translation and other	1	(2)
Balance, end of period	\$ 1,944	\$ 2,022

**Table of Contents****Net Income Attributable to PepsiCo per Common Share**

The computations of basic and diluted net income attributable to PepsiCo per common share are as follows:

	12 Weeks Ended			
	3/19/11		3/20/10	
	Income	Shares <sup>(a)</sup>	Income	Shares <sup>(a)</sup>
Net income attributable to PepsiCo	\$ 1,143		\$ 1,430	
Preferred shares:				
Dividends				
Redemption premium	(2)		(1)	
Net income available for PepsiCo common shareholders	\$ 1,141	1,583	\$ 1,429	1,582
Basic net income attributable to PepsiCo per common share	\$ 0.72		\$ 0.90	
Net income available for PepsiCo common shareholders	\$ 1,141	1,583	\$ 1,429	1,582
Dilutive securities:				
Stock options and RSUs <sup>(b)</sup>		21		23
ESOP convertible preferred stock	2	1	1	1
Diluted	\$ 1,143	1,605	\$ 1,430	1,606
Diluted net income attributable to PepsiCo per common share	\$ 0.71		\$ 0.89	

<sup>(a)</sup> Weighted-average common shares outstanding (in millions).

<sup>(b)</sup> Options to purchase 31.3 million shares in 2011 and 20.7 million shares in 2010 were not included in the calculation of earnings per share because these options were out-of-the-money. Out-of-the-money options had an average exercise price of \$66.85 in 2011 and \$67.02 in 2010.

**Merger and Integration Charges**

In the 12 weeks ended March 19, 2011, we incurred merger and integration charges of \$55 million (\$49 million after-tax or \$0.03 per share) related to our acquisitions of PBG, PAS and WBD, including \$21 million recorded in the PAB segment, \$42 million recorded in corporate unallocated expenses and a credit of \$8 million recorded in the Europe segment, primarily reflecting a gain on our previously held equity interest in WBD. All of these net charges were recorded in selling, general and administrative expenses. These charges also include closing costs and advisory fees related to our acquisition of WBD. Substantially all cash payments related to the above charges are expected to be paid by the end of 2011.

In the 12 weeks ended March 20, 2010, we incurred merger and integration charges of \$312 million related to our acquisitions of PBG and PAS, including \$193 million recorded in the PAB segment, \$1 million recorded in the Europe segment, \$88 million recorded in corporate unallocated expenses and \$30 million recorded in interest expense. All of these charges, other than the interest expense portion, were recorded in selling, general and administrative expenses. These charges also include closing costs, one-time financing costs and advisory fees related to our acquisitions of PBG and PAS. In addition, we recorded \$9 million of charges, representing our share of the respective merger costs of PBG and PAS, in bottling equity income. Substantially all cash payments related to the above charges are expected to be paid by the end of 2011. In total, these charges had an after-tax impact of \$261 million or \$0.16 per share.

**Table of Contents**

A summary of our merger and integration activity in 2011 is as follows:

	Severance and Other Employee Costs		Other Costs	Total
Liability as of December 25, 2010	\$	179	\$ 25	\$ 204
2011 merger and integration charges		8	47	55
Cash payments		(43)	(74)	(117)
Non-cash charges		(20)	17	(3)
Liability as of March 19, 2011	\$	124	\$ 15	\$ 139

**Financial Instruments**

We are exposed to market risks arising from adverse changes in:

commodity prices, affecting the cost of our raw materials and energy,

foreign exchange risks, and

interest rates.

In the normal course of business, we manage these risks through a variety of strategies, including the use of derivatives. Certain derivatives are designated as either cash flow or fair value hedges and qualify for hedge accounting treatment, while others do not qualify and are marked to market through earnings. Ineffectiveness of our hedges is not material. We do not use derivative instruments for trading or speculative purposes. We perform assessments of our counterparty credit risk regularly, including a review of credit ratings, credit default swap rates and potential nonperformance of the counterparty. Based on our most recent assessment of our counterparty credit risk, we consider this risk to be low. In addition, we enter into derivative contracts with a variety of financial institutions that we believe are creditworthy in order to reduce our concentration of credit risk and generally settle with these financial institutions on a net basis.

**Commodity Prices**

We are subject to commodity price risk because our ability to recover increased costs through higher pricing may be limited in the competitive environment in which we operate. This risk is managed through the use of fixed-price purchase orders, pricing agreements, geographic diversity and derivatives. We use derivatives, with terms of no more than three years, to economically hedge price fluctuations related to a portion of our anticipated commodity purchases, primarily for natural gas, diesel fuel and aluminum. For those derivatives that qualify for hedge accounting, any ineffectiveness is recorded immediately in corporate unallocated expenses. We classify both the earnings and cash flow impact from these derivatives consistent with the underlying hedged item. During the next 12 months, we expect

to reclassify net gains of \$34 million related to these hedges from accumulated other comprehensive loss into net income. Derivatives used to hedge commodity price risk that do not qualify for hedge accounting are marked to market each period and reflected in our income statement.

Our open commodity derivative contracts that qualify for hedge accounting had a face value of \$573 million as of March 19, 2011 and \$582 million as of March 20, 2010. These contracts resulted in net unrealized gains of \$73 million as of March 19, 2011 and \$72 million as of March 20, 2010.

## **Table of Contents**

Our open commodity derivative contracts that do not qualify for hedge accounting had a face value of \$300 million as of March 19, 2011 and \$221 million as of March 20, 2010. These contracts resulted in net gains of \$58 million as of March 19, 2011 and \$20 million as of March 20, 2010.

### ***Foreign Exchange***

Financial statements of foreign subsidiaries are translated into U.S. dollars using period-end exchange rates for assets and liabilities and weighted-average exchange rates for revenues and expenses. Adjustments resulting from translating net assets are reported as a separate component of accumulated other comprehensive loss within common shareholders equity as currency translation adjustment.

We may enter into derivatives, primarily forward contracts with terms of no more than two years, to manage our exposure to foreign currency transaction risk. Exchange rate gains or losses related to foreign currency transactions are recognized as transaction gains or losses in our income statement as incurred.

Our foreign currency derivatives had a total face value of \$2.3 billion as of March 19, 2011 and \$1.4 billion as of March 20, 2010. The contracts that qualify for hedge accounting resulted in net unrealized losses of \$34 million as of March 19, 2011 and \$29 million as of March 20, 2010. During the next 12 months, we expect to reclassify net losses of \$30 million related to these hedges from accumulated other comprehensive loss into net income. The contracts that do not qualify for hedge accounting resulted in net losses of \$5 million as of both March 19, 2011 and March 20, 2010. All losses and gains were offset by changes in the underlying hedged items, resulting in no net material impact on earnings.

### ***Interest Rates***

We centrally manage our debt and investment portfolios considering investment opportunities and risks, tax consequences and overall financing strategies. We use various interest rate derivative instruments including, but not limited to, interest rate swaps, cross currency interest rate swaps, Treasury locks and swap locks to manage our overall interest expense and foreign exchange risk. These instruments effectively change the interest rate and currency of specific debt issuances. Certain of our fixed rate indebtedness has been swapped to floating rates. The notional amount, interest payment and maturity date of the interest rate and cross-currency swaps match the principal, interest payment and maturity date of the related debt. Our Treasury locks and swap locks are entered into to protect against unfavorable interest rate changes relating to forecasted debt transactions.

The notional amounts of the interest rate derivative instruments outstanding as of March 19, 2011 and March 20, 2010 were \$9.23 billion and \$8.35 billion, respectively. For those interest rate derivative instruments that qualify for cash flow hedge accounting, any ineffectiveness is recorded immediately. We classify both the earnings and cash flow impact from these interest rate derivative instruments consistent with the underlying hedged item. During the next 12 months, we expect to reclassify net losses of \$13 million related to these hedges from accumulated other comprehensive loss into net income.

As of March 19, 2011, approximately 44% of total debt, after the impact of the related interest rate derivative instruments, was exposed to variable rates, compared to 43% as of December 25, 2010.



**Table of Contents****Fair Value Measurements**

The fair values of our financial assets and liabilities as of March 19, 2011 and March 20, 2010 are categorized as follows:

	2011		2010	
	Assets <sup>(a)</sup>	Liabilities <sup>(a)</sup>	Assets <sup>(a)</sup>	Liabilities <sup>(a)</sup>
Available-for-sale securities <sup>(b)</sup>	\$ 70		\$ 69	
Short-term investments index funds <sup>(c)</sup>	\$ 177		\$ 123	
Deferred compensation <sup>(d)</sup>		\$ 553		\$ 572
<b>Derivatives designated as hedging instruments:</b>				
Forward exchange contracts <sup>(e)</sup>	\$ 4	\$ 38	\$ 10	\$ 39
Interest rate derivatives <sup>(f)</sup>	296	16	207	12
Commodity contracts other <sup>(g)</sup>	89	1	112	5
Commodity contracts future <sup>(h)</sup>	1	16		35
	\$ 390	\$ 71	\$ 329	\$ 91
<b>Derivatives not designated as hedging instruments:</b>				
Forward exchange contracts <sup>(e)</sup>	\$ 6	\$ 11	\$ 2	\$ 7
Interest rate derivatives <sup>(f)</sup>	14	52		42
Commodity contracts other <sup>(g)</sup>	59	1	12	30
Commodity contracts future <sup>(h)</sup>				2
Prepaid forward contracts <sup>(i)</sup>	43		64	
	\$ 122	\$ 64	\$ 78	\$ 81
<b>Total derivatives at fair value</b>	<b>\$ 512</b>	<b>\$ 135</b>	<b>\$ 407</b>	<b>\$ 172</b>
<b>Total</b>	<b>\$ 759</b>	<b>\$ 688</b>	<b>\$ 599</b>	<b>\$ 744</b>

(a) Financial assets are classified on our balance sheet within other assets, with the exception of short-term investments. Financial liabilities are classified on our balance sheet within other current liabilities and other liabilities. Unless specifically indicated, all financial assets and liabilities are categorized as Level 2 assets or liabilities.

(b) Based on the price of common stock. Categorized as a Level 1 asset.

(c) Based on price changes in index funds used to manage a portion of market risk arising from our deferred compensation liability. Categorized as a Level 1 asset.

- (d) Based on the fair value of investments corresponding to employees' investment elections. As of March 19, 2011 and March 20, 2010, \$63 million and \$124 million, respectively, are categorized as Level 1 liabilities. The remaining balances are categorized as Level 2 liabilities.
- (e) Based on observable market transactions of spot and forward rates.
- (f) Based on LIBOR and recently reported transactions in the marketplace.
- (g) Based on recently reported transactions in the marketplace, primarily swap arrangements.
- (h) Based on average prices on futures exchanges. Categorized as a Level 1 asset or liability.
- (i) Based primarily on the price of our common stock.  
The fair value of our debt obligations as of March 19, 2011 was \$28.9 billion, based upon prices of similar instruments in the marketplace.

**Table of Contents**

The effective portion of the pre-tax (gains)/losses on our derivative instruments are categorized in the tables below.

	Fair Value/Non-designated Hedges		12 Weeks Ended			
			Cash Flow Hedges		Losses/(Gains) Reclassified from Accumulated Other Comprehensive Loss into Income Statement <sup>(b)</sup>	
	(Gains)/Losses Recognized in Income Statement <sup>(a)</sup>		Losses/(Gains) Recognized in Accumulated Other Comprehensive Loss			
	3/19/11	3/20/10	3/19/11	3/20/10	3/19/11	3/20/10
Forward exchange contracts	\$ (1)	\$ 6	\$ 25	\$ 13	\$ 5	\$ 11
Interest rate derivatives	(22)	10	(6)	48	3	
Prepaid forward contracts	2	(18)				
Commodity contracts	(39)	(46)	(40)	(12)	(6)	16
<b>Total</b>	<b>\$ (60)</b>	<b>\$ (48)</b>	<b>\$ (21)</b>	<b>\$ 49</b>	<b>\$ 2</b>	<b>\$ 27</b>

(a) Interest rate gains/losses are included in interest expense in our income statement. All other gains/losses are included in corporate unallocated expenses.

(b) Interest rate losses are included in interest expense in our income statement. All other gains/losses are included in cost of sales in our income statement.

**Table of Contents**

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

**FINANCIAL REVIEW**

*Our discussion and analysis is an integral part of understanding our financial results. Also refer to Basis of Presentation and Our Divisions in the Notes to the Condensed Consolidated Financial Statements. Tabular dollars are in millions, except per share amounts. All per share amounts reflect common per share amounts, assume dilution unless otherwise noted and are based on unrounded amounts. Percentage changes are based on unrounded amounts.*

**Our Critical Accounting Policies**

***Sales Incentives and Advertising and Marketing Costs***

We offer sales incentives and discounts through various programs to customers and consumers. These incentives are accounted for as a reduction of revenue. Certain sales incentives are recognized at the time of sale while other incentives, such as bottler funding and customer volume rebates, are recognized during the year incurred, generally in proportion to revenue, based on annual targets. Anticipated payments are estimated based on historical experience with similar programs and require management judgment with respect to estimating customer participation and performance levels. Differences between estimated expense and actual incentive costs are normally insignificant and are recognized in earnings in the period such differences are determined. In addition, certain advertising and marketing costs are also recognized during the year incurred, generally in proportion to revenue.

***Income Taxes***

In determining our quarterly provision for income taxes, we use an estimated annual effective tax rate which is based on our expected annual income, statutory tax rates and tax planning opportunities available to us in the various jurisdictions in which we operate. Subsequent recognition, derecognition and measurement of a tax position taken in a previous period are separately recognized in the quarter in which they occur.

**Our Business Risks**

*This Quarterly Report on Form 10-Q contains statements reflecting our views about our future performance that constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the Reform Act). Statements that constitute forward-looking statements within the meaning of the Reform Act are generally identified through the inclusion of words such as believe, expect, intend, estimate, project, anticipate, will and variations of such words and other similar expressions. All statements addressing our future operating performance, and statements addressing events and developments that we expect or anticipate will occur in the future, are forward-looking statements within the meaning of the Reform Act. These forward-looking statements are based on currently available information, operating plans and projections about future events and trends. They inherently involve risks and uncertainties that could cause actual results to differ materially from those predicted in any such forward-looking statements. Investors are cautioned not to place undue reliance on any such forward-looking statements, which speak only as of the date they are made. We undertake no obligation to update any*

*forward-looking statement, whether as a result of new information, future events or otherwise.*

**Table of Contents**

Our operations outside of the United States generated approximately 40% of our net revenue in the 12 weeks ended March 19, 2011. As a result, we are exposed to foreign currency risks, including unforeseen economic changes and political unrest. During the 12 weeks ended March 19, 2011, favorable foreign currency increased net revenue growth by 1 percentage point, primarily due to appreciation of the Mexican peso, Canadian dollar and Brazilian real, partially offset by depreciation of the euro. Currency declines against the U.S. dollar which are not offset could adversely impact our future results.

We expect to be able to reduce the impact of volatility in our raw material and energy costs through our hedging strategies and ongoing sourcing initiatives.

See *Financial Instruments* in the Notes to the Condensed Consolidated Financial Statements for further discussion of our derivative instruments, including their fair values as of March 19, 2011 and March 20, 2010. Cautionary statements included in Item 1A. Risk Factors in our Annual Report on Form 10-K for the fiscal year ended December 25, 2010 and in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations. Our Business Risks included in Exhibit 99.1 to our Current Report on Form 8-K dated March 31, 2011, should be considered when evaluating our trends and future results.

**Table of Contents****Results of Operations Consolidated Review****Items Affecting Comparability**

Our reported financial results are impacted by the following items in each of the following periods:

	12 Weeks Ended	
	3/19/11	3/20/10
<b>Operating profit</b>		
Mark-to-market net gains	\$ 31	\$ 46
Merger and integration charges	\$ (55)	\$ (282)
Inventory fair value adjustments	\$ (34)	\$ (281)
Venezuela currency devaluation	\$	\$ (120)
Asset write-off	\$	\$ (145)
Foundation contribution	\$	\$ (100)
<b>Bottling equity income</b>		
Gain on previously held equity interests	\$	\$ 735
Merger and integration charges	\$	\$ (9)
<b>Interest expense</b>		
Merger and integration charges	\$	\$ (30)
<b>Net income attributable to PepsiCo</b>		
Mark-to-market net gains	\$ 19	\$ 29
Gain on previously held equity interests	\$	\$ 958
Merger and integration charges	\$ (49)	\$ (261)
Inventory fair value adjustments	\$ (21)	\$ (240)
Venezuela currency devaluation	\$	\$ (120)
Asset write-off	\$	\$ (92)
Foundation contribution	\$	\$ (64)
<b>Net income attributable to PepsiCo per common share diluted</b>		
Mark-to-market net gains	\$ 0.01	\$ 0.02
Gain on previously held equity interests	\$	\$ 0.60
Merger and integration charges	\$ (0.03)	\$ (0.16)
Inventory fair value adjustments	\$ (0.01)	\$ (0.15)
Venezuela currency devaluation	\$	\$ (0.07)
Asset write-off	\$	\$ (0.06)
Foundation contribution	\$	\$ (0.04)
<b>Mark-to-Market Net Impact</b>		

We centrally manage commodity derivatives on behalf of our divisions. These commodity derivatives include energy, fruit, aluminum and other raw materials. Certain of these commodity derivatives do not qualify for hedge accounting treatment and are marked to market with the resulting gains and losses recognized in corporate unallocated expenses. These gains and losses are subsequently reflected in division results when the divisions take delivery of the underlying commodity. Therefore, the divisions realize the economic effects of the derivative without experiencing any resulting mark-to-market volatility which remains in corporate unallocated expenses.





## **Table of Contents**

In the 12 weeks ended March 19, 2011, we recognized \$31 million (\$19 million after-tax or \$0.01 per share) of mark-to-market net gains on commodity hedges in corporate unallocated expenses.

In the 12 weeks ended March 20, 2010, we recognized \$46 million (\$29 million after-tax or \$0.02 per share) of mark-to-market net gains on commodity hedges in corporate unallocated expenses.

## **Gain on Previously Held Equity Interests**

In the 12 weeks ended March 20, 2010, in connection with our acquisitions of PBG and PAS, we recorded a gain on our previously held equity interests of \$958 million (\$0.60 per share), comprising \$735 million which is non-taxable and recorded in bottling equity income and \$223 million related to the reversal of deferred tax liabilities associated with these previously held equity interests.

## **Merger and Integration Charges**

In the 12 weeks ended March 19, 2011, we incurred merger and integration charges of \$55 million (\$49 million after-tax or \$0.03 per share) related to our acquisitions of PBG, PAS and WBD, including \$21 million recorded in the PAB segment, \$42 million recorded in corporate unallocated expenses and a credit of \$8 million recorded in the Europe segment, primarily reflecting a gain on our previously held equity interest in WBD. These charges also include closing costs and advisory fees related to our acquisition of WBD.

In the 12 weeks ended March 20, 2010, we incurred merger and integration charges of \$312 million related to our acquisitions of PBG and PAS, including \$193 million recorded in the PAB segment, \$1 million recorded in the Europe segment, \$88 million recorded in corporate unallocated expenses and \$30 million recorded in interest expense. These charges also include closing costs, one-time financing costs and advisory fees related to our acquisitions of PBG and PAS. In addition, we recorded \$9 million of charges, representing our share of the respective merger costs of PBG and PAS, in bottling equity income. In total, these charges had an after-tax impact of \$261 million or \$0.16 per share.

## **Inventory Fair Value Adjustments**

In the 12 weeks ended March 19, 2011, we recorded \$34 million (\$21 million after-tax or \$0.01 per share) of incremental costs in cost of sales related to fair value adjustments to the acquired inventory included in WBD's balance sheet at the acquisition date and other related hedging contracts included in PBG's and PAS's balance sheets at the acquisition date.

In the 12 weeks ended March 20, 2010, we recorded \$281 million (\$240 million after-tax or \$0.15 per share) of incremental costs in cost of sales related to fair value adjustments to the acquired inventory and other related hedging contracts included in PBG's and PAS's balance sheets at the acquisition date.

## **Venezuela Currency Devaluation**

As of the beginning of our 2010 fiscal year, we recorded a one-time \$120 million net charge related to our change to hyperinflationary accounting for our Venezuelan businesses and the related devaluation of the bolivar. \$129 million of this net charge was recorded in corporate unallocated expenses, with the balance (income of \$9 million) recorded in our PAB segment. In total, this net charge had an after-tax impact of \$120 million or \$0.07 per share.



## **Table of Contents**

### **Asset Write-Off**

In the 12 weeks ended March 20, 2010, we recorded a \$145 million charge (\$92 million after-tax or \$0.06 per share) related to a change in scope of one release in our ongoing migration to SAP software. This change was driven, in part, by a review of our North America systems strategy following our acquisitions of PBG and PAS. This change does not impact our overall commitment to continue our implementation of SAP across our global operations over the next few years.

### **Foundation Contribution**

In the 12 weeks ended March 20, 2010, we made a \$100 million (\$64 million after-tax or \$0.04 per share) contribution to The PepsiCo Foundation, Inc., in order to fund charitable and social programs over the next several years. This contribution was recorded in corporate unallocated expenses.

### ***Non-GAAP Measures***

Certain measures contained in this Form 10-Q are financial measures that are adjusted for items affecting comparability (see *Items Affecting Comparability* for a detailed list and description of each of these items), as well as, in certain instances, adjusted for foreign currency. These measures are not in accordance with U.S. Generally Accepted Accounting Principles (GAAP). Items adjusted for currency assume foreign currency exchange rates used for translation based on the rates in effect for the comparable prior-year period. We believe investors should consider these non-GAAP measures in evaluating our results as they are more indicative of our ongoing performance and with how management evaluates our operational results and trends. These measures are not, and should not be viewed as, a substitute for U.S. GAAP reporting measures. See also *Management Operating Cash Flow*.

### ***Volume***

Since our divisions each use different measures of physical unit volume, a common servings metric is necessary to reflect our consolidated physical unit volume. For the 12 weeks ended March 19, 2011, total servings increased 9%, as worldwide snacks increased 3% and worldwide beverages increased 12%.

We discuss volume for our beverage businesses on a bottler case sales (BCS) basis in which all beverage volume is converted to an 8-ounce-case metric. Most of our beverage volume is sold by our company-owned and franchise-owned bottlers, and that portion is based on our bottlers' sales to retailers and independent distributors. The remainder of our volume is based on our direct shipments to retailers and independent distributors. We report our international beverage volume on a monthly basis. Our first quarter includes beverage volume outside of North America for January and February. Concentrate shipments and equivalents (CSE) represent our physical beverage volume shipments to independent bottlers, retailers and independent distributors, and is the measure upon which our revenue is based.

**Table of Contents****Consolidated Results****Total Net Revenue and Operating Profit**

	12 Weeks Ended		
	3/19/11	3/20/10	Change
Total net revenue	\$ 11,937	\$ 9,368	27%
Operating profit			
FLNA	\$ 774	\$ 728	6%
QFNA	214	195	9%
LAF	171	145	17%
PAB	558	73	669%
Europe	63	118	(47)%
AMEA	146	155	(6)%
Corporate Unallocated			
Mark-to-market net gains	31	46	(33)%
Merger and integration charges	(42)	(88)	(52)%
Venezuela currency devaluation		(129)	n/m
Asset write-off		(145)	n/m
Foundation contribution		(100)	n/m
Other	(189)	(158)	19%
Total operating profit	\$ 1,726	\$ 840	105%
Total operating profit margin	14.5%	9.0%	5.5

*n/m = not meaningful*

See Results of Operations Division Review for a tabular presentation and discussion of key drivers of net revenue.

On a reported basis, total operating profit increased 105% and operating margin increased 5.5 percentage points. Operating profit performance was primarily driven by items affecting comparability (see Items Affecting Comparability), which contributed 102 percentage points to the total operating profit growth and 8.9 percentage points to the total operating margin increase. Operating profit performance also reflects the incremental operating results from our acquisitions of PBG and PAS.

**Table of Contents****Other Consolidated Results**

	3/19/11	12 Weeks Ended 3/20/10	Change
Bottling equity income	\$	\$ 709	\$ (709)
Interest expense, net	\$ (163)	\$ (148)	\$ (15)
Tax rate	26.8%	(2.3)%	
Net income attributable to PepsiCo	\$ 1,143	\$ 1,430	(20)%
Net income attributable to PepsiCo per common share diluted	\$ 0.71	\$ 0.89	(20)%
Mark-to-market net gains	(0.01)	(0.02)	
Gain on previously held equity interests		(0.60)	
Merger and integration charges	0.03	0.16	
Inventory fair value adjustments	0.01	0.15	
Venezuela currency devaluation		0.07	
Asset write-off		0.06	
Foundation contribution		0.04	
Net income attributable to PepsiCo per common share diluted, excluding above items*	\$ 0.74	\$ 0.76**	(2)%
Impact of foreign currency translation			(1)
Growth in net income attributable to PepsiCo per common share diluted, excluding above items, on a constant currency basis*			(3)%

\* See *Non-GAAP Measures*

\*\* Does not sum due to rounding

Bottling equity income decreased \$709 million, primarily reflecting the gain in the prior year on our previously held equity interests in connection with our acquisitions of PBG and PAS.

Net interest expense increased \$15 million, primarily reflecting higher average debt balances, partially offset by lower average rates on our debt balances as well as bridge and term financing costs in the prior year in connection with our acquisitions of PBG and PAS.

The reported tax rate was 26.8%, compared to a benefit of 2.3% in the prior year. The year-over-year change was driven primarily by the prior year non-taxable gain and reversal of deferred taxes attributable to our previously held equity interests in connection with our acquisitions of PBG and PAS.

Net income attributable to PepsiCo and net income attributable to PepsiCo per common share decreased 20%. Items affecting comparability (see [Items Affecting Comparability](#) ) decreased both net income attributable to PepsiCo and net income attributable to PepsiCo per common share by 18 percentage points.

**Table of Contents****Results of Operations Division Review**

The results and discussions below are based on how our Chief Executive Officer monitors the performance of our divisions. For additional information, see *Our Divisions* and *Merger and Integration Charges* in the Notes to the Condensed Consolidated Financial Statements and *Items Affecting Comparability*.

Furthermore, in the discussions of net revenue and operating profit below, *effective net pricing* reflects the year-over-year impact of discrete pricing actions, sales incentive activities and mix resulting from selling varying products in different package sizes and in different countries, and *net pricing* reflects the year-over-year combined impact of list price changes, weight changes per package, discounts and allowances. Additionally, *acquisitions*, except as otherwise noted, reflect all mergers and acquisitions activity, including the impact of acquisitions, divestitures and changes in ownership or control in consolidated subsidiaries and nonconsolidated equity investees.

**Net Revenue**

<b>12 Weeks Ended</b>	<b>FLNA</b>	<b>QFNA</b>	<b>LAF</b>	<b>PAB</b>	<b>Europe</b>	<b>AMEA</b>	<b>Total</b>
<b>March 19, 2011</b>	<b>\$ 2,904</b>	<b>\$ 640</b>	<b>\$ 1,108</b>	<b>\$ 4,531</b>	<b>\$ 1,626</b>	<b>\$ 1,128</b>	<b>\$ 11,937</b>
March 20, 2010	\$ 2,864	\$ 683	\$ 983	\$ 2,765	\$ 1,044	\$ 1,029	\$ 9,368
<i>% Impact of:</i>							
Volume <sup>(a)</sup>	1%	(8)%	2%	*	*	4%	*
Effective net pricing <sup>(b)</sup>		1	5	*	*		