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PEP - PepsiCo Inc at Consumer Analyst Group of New York Conference

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PRESENTATION

Bryan Spillane - *Bank of America Merrill Lynch - Conference Co-Chair*

Alright. We can make our way to our seats. We're ready for the afternoon to begin. And to kick-off this afternoon, we are joined by PepsiCo. Before we get started please join me in thanking Pepsi for their generous support this week by supplying us with beverages and snacks all week.

So the format of PepsiCo's presentation today, they're going to make a few brief remarks, CEO of North America, Al Carey, will make a few brief remarks. And then we're going to turn it over to really extended portion of Q&A. And then beyond that, we'll go back into the breakout room as well for continued Q&A. So with that aside Al, I'll turn it over to you.

Al Carey - *PepsiCo, Inc. - CEO of North America*

Thank you, Bryan. Good afternoon everybody. It's a pleasure to be here, and Bryan, thanks for the invite and the opportunity to speak today. And we'd like to do a little bit differently than we've done in the past. Instead of a long presentation and a short Q&A, I thought we'd just have a very brief three slides that kind of give you an idea on what's important in North America for PepsiCo and then we'll open it up to Q&A for an extended period of time where we could talk about what you'd like to talk about. So first, I'd like to introduce my teammates here on stage. First, we have Vivek Sankaran, who is an eight-year veteran of PepsiCo now, formally with McKinsey then ended up working in ran strategic planning for PepsiCo. Then came down to Frito and ran several operating jobs, ran the sales department and then ran sales for PepsiCo and now he's the President and Chief Operating Officer. So he runs Frito-Lay North America. And then we have Kirk Tanner, right to his right and Kirk started with the company 25 years ago in the sales organization. He has come up through the ranks at Frito, he ended up working in Europe for a while in our snack business, and to beverages and now he's running the North America beverage business.

So let me get started. I thought I'd give you three slides only and just tell you a little bit about -- here's -- I'll read this to you. So let me talk to you a little bit, in each of our operating divisions there are important priorities, but we have the three of us have three very important priorities that go across all of PepsiCo for North America.

The first one is the transforming of our portfolio. And what that means is high priority on innovative products and packages and making R&D investments in new products into the marketplace. Innovation, now you'll notice that 85% of it looks healthier and healthy, and to give you a couple of ideas on the left side of the chart, couple of the products that have been rolled out this year already are LIFEWTR, zero calorie, Tropicana probiotic, low-calorie carbonated soft drinks like IZZE and LEMON LEMON, new varieties of tea under the Lipton Tea house variety and then we actually made an acquisition of KeVita, which is a non-dairy probiotic and Kombucha, which is another healthy product and it fits in this portfolio of healthier products.

On the Frito side, we now have veggie, harvest chips, we have Smartfood delights, which is a low-calorie exceptional popcorn product that is doing extremely well in the marketplace. And then the Simply line of snack-food products, which are non-GMO, organic and clean-label products on the snack-foods, which is growing rapidly.



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And then finally, there is one up there, you can see Overnight Oats for Quaker oat meal, which will come out in the summer time. That's not the whole list, there is more to come, but that's really about introducing more products into the marketplace that are healthier and putting a focus on innovation.

I thought I'd show you just one slide up here about how do you market some of those healthier products. I'm using the example of the Super Bowl this year. So in the past we've mostly advertised our full sugar products on the Super Bowl with a big audience of 117 million. This year in the middle you can see our Mountain Dew Kickstart was the product that we ran on television through the playoff games. And Mountain Dew Kickstart has now achieved \$500 million revenue at retail and it also is 60% less sugar. So the theme was healthier products.

Then when we've got to the Super Bowl, on the bottom, you can see our ad that we ran on the Super Bowl and we ran it on the Grammys for LIFEWTR, and we thought it was a great ad. The sales of this product very early on are terrific, and again zero-calorie. And then finally, we had the Halftime Show with Lady Gaga and it was sponsored by that Pepsi Zero Sugar. So here's a normally very big marketing platform that was done all with healthier products, lower sugar or zero sugar.

And then finally on merchandising. We're now looking not just merchandising in-store but merchandising on vending machines and in coolers using this Hello Goodness theme. And where we've placed these Hello Goodness vending machines or coolers, the only products that are in there are the healthier better-for-your products and the takeaway on these products is terrific and we're good progress. So that's one of our important priorities. And the second one is about serving the customer. Now we take this very seriously in our organization in North America. We are approaching our largest customers as one PepsiCo and I believe it's starting to make some progress. And then we've just extended to our next 10 largest customers, so that we extend the PepsiCo approach that way as well. I believe it's starting to pay off.

This Kantar score that you see on the top is something that's been done for about 16 or 18 years. We have never been Number 1. This is something that's voted on by the customer. And this last go-around, we were Number 1 rank against all the other suppliers, which we felt pretty good about. Also this last year and the year before, we contributed the most growth to our retail partners of any vendor that supplies them. And in the last several months, we have been awarded Vendor of the Year with three of our very largest customers. So I think we're starting to pay off. But I can tell you that the theme we live by is being hungry and humble with our customers and serve them extremely well and we're starting to get our PepsiCo approach down pretty pat.

Also it's not just in the retail side, it's in foodservice. And we have one organization that is right now under Kirk Tanner, and we have one organization that runs all of PepsiCo products sold through the foodservice business. And you can see some of the coolers and the ways that we merchandise our products in those foodservice accounts.

Finally, the third in the Top 3 priorities is making our DSD system more efficient and effective. We think that we now have a very scaled business, Frito-Lay has done an exceptional job at working on this GES model which is taking inventory out of the system, it's moving complexity upstream, it's saving us a lot of money, but the route salesman that work in the field would say that this is an exceptional way to improve their job and allow them to sell more. Kirk will tell you a little bit later on about, he's doing a similar thing for GES on the beverage side.

And finally I'll just tell you very quickly about one, maybe the next time we're back together we'll talk more about it, but that is we have a couple of experimental markets where we put our chilled DSD products, in other words, juices, Kevita, Tropicana, Naked Juice, hummus and we put it on a bay of one of our Pepsi trucks. We've refrigerated one bay, we figured out how to do this and really have success in our Florida and in our Texas markets, and it's something we're likely to do more of. And it allows us to get deeper penetration into the small format, which we normally don't do with those chilled products.

So the top priority, transforming the portfolio. Second is serving our customer exceptionally well. And the third one is doubling down on our DSD business and making it more effective for the future.

So that's it on the presentation side. And Bryan, I thought I'd just go right into the Q&A, if that's okay. And we'll take questions from the audience.



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QUESTIONS AND ANSWERS

Bryan Spillane - *Bank of America Merrill Lynch - Conference Co-Chair*

Dara.

Dara Mohsenian - *Morgan Stanley & Co. LLC - Analyst*

Thanks. So Al, you highlighted the effectiveness of the DSD system and the GES is better enabled you to extract value from the system. At the same time, one of your competitors has announced they're moving away from DSD. So I was hoping you could just take a step back and from a top-down perspective, as you look at the North American business, what are the advantages of the DSD system, how you're better kind of enabling it to drive value going forward?

Al Carey - *PepsiCo, Inc. - CEO of North America*

Yes. I've been around the DSD business for a very long time. We do have a business's warehouse delivered in Quaker, Tropicana and Gatorade, but my belief on DSD is there is nothing like it. We are able to get very specific. If you ever spend a day in the field with a good route salesman for Frito-Lay or for Pepsi, you'll see the relationships that have built at the store level that are unmatched. And when there is a problem with servicing a customer and let's say it's in a Wal-Mart Store and it's a Friday afternoon and they're running short on product, we will put a person out there in one second. They make a phone call and we are there for them. And as a result, we get a lot of jump balls at store level, we build a relationship with the store manager that's unequalled and it allows us to get better execution at the store level as well. Now on the refranchising side, I think that's part of what you're asking to, Coke is moving in that direction. They still have a DSD system, but I like the idea of owning our system, because as we find different ways of getting productivity like in this GES model, we can take those savings and put them back against brands and R&D and developing new products. We also -- it's easier to manage pricing with the large customers. I can't imagine -- we own 80% of our bottling system, it's already tricky enough, I can't imagine having more independent bottling partners and trying to agree on what a price will be with one big customer when they demand the price.

And the other thing I'd say is I really like the potential of doubling down on these Pepsi trucks that we've got. The possibility of using the excess capacity on those trucks to sell chilled product is really a good idea for us. I think it's going to pay dividends down the road.

Unidentified Audience Member

Two questions, first one for you, Al. And you touched on it a little bit in your remarks. There's a lot of notable consumer trends that are really accelerating I think in your space and so, if you could give us a little bit more color in terms of how your portfolio is evolving to address those. And then back in, I guess as a follow-up to Dara's question about DSD, Frito-Lay North America has the highest margins firstly for a DSD operator, but really even among the highest in the food industry. So is there a concern that margins are too high? And I remember this -- I'm old enough to remember this discussion when it was 20% margin. But are margins too high? Is there runway for margins to expand? Just how should we think about maybe margin expansion in that business going forward?

Al Carey - *PepsiCo, Inc. - CEO of North America*

So on the -- Kirk, I'm going to pass it to you in one second. I just wanted to say that as you look at these young consumers coming up the ranks, millennials and generations, the interest in healthy products is clear. And I don't think this obesity epidemic goes away anytime in the near future, and I think therefore we have to deliver products in the marketplace that fit those needs. So over the last several years, we've invested quite heavily in developing new products, most of them healthy. And I look at water, sport drinks, teas, coffee, low-calorie versions of Mountain Dew and it really does work.



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And I think that's where we're going to have to go even more aggressively than we're going to today. I think we almost need to double down and move even faster. Kirk, maybe you could talk a little bit about the beverage portfolio, because we are working hard on that.

Kirk Tanner - PepsiCo, Inc. - President & COO, North America Beverages

Yes, absolutely. I think if you think with the consumer trends that AI talked about in health and wellness, there's also this immediate consumption consumers on the go, and you see food service or food away from home growing faster than food and retail. So that's another trend, that's why you see us invest in foodservice from innovation standpoint, equipment standpoint and creating a better experience for consumers when they're on-the-go and away from home. But separately we are working really hard on the portfolio to meet those consumers where they are going. And we're building in three different ways. One, we're taking the broad portfolio that we have today, the powerful brands that we have. And AI talked a little bit about it, but things like taking Starbucks and your innovation is whole brew a premium experience for consumers. You take Pure Leaf and the success that we've had with Pure Leaf and innovate Tea House, this premium brewed tea in a glass bottle. That's a great experience for consumers.

With Naked Juice, we have cold-pressed. With Tropicana, we innovated on probiotics. On Gatorade, we innovated on G Organics and we have a sub-line coming out this year called [Flow]. In addition, we leverage brands like IZZE and we feel like we can extract more value out of IZZE by introducing kind of a next-generation CSD that has 60 calories per 12-ounce and is a great consumer experience.

In our brands like Mountain Dew and Pepsi, we continue to innovate off those platforms drive relevance. AI talked about it earlier, but Mountain Dew Kickstart is about \$500 million business and continues to grow and it delivers on like what the consumer expects, at the same time, it delivers 60 calories per 12 ounces. We continue to innovate off of Mountain Dew with the label series of premium, crafted Mountain Dew and this year we'll launch Mountain Dew Spiked lemonade. Not the spike that you had at the bar last night, but spiked with prickly pear juice. It's a terrific product.

And Pepsi 1893 a craft cola, to really get to the essence of cola. It's a premium experience for consumers. So we take our brands and we innovate off those brands. Also say we introduce new brands. LIFEWTR has been a huge success this year. It exceeded our expectations almost 70% ACV after three weeks. The velocities are terrific. I think you've experienced LIFEWTR, you've seen the display outside. And we are thrilled to death with the launch of LIFEWTR and the success we've seen so far.

In addition, AI mentioned LEMON LEMON, another product that we'll introduce this year that hits the sweet spot of consumer experience with the right amount of calories, 70 calories per 12 ounces. And last, I would say we look for opportunities like Kevita. Kevita is a sparkling probiotic that allows us to build our chilled premium portfolio, and it is a great partner to Naked and IZZE. And we look forward to building and growing that brand. So that's how we're thinking about meeting consumers where they're going.

AI Carey - PepsiCo, Inc. - CEO of North America

One other point, Brian, before Vivek talks about DSD is, with the theme that goes to all those products you just mentioned is single-serve products, small packages. I think it's a really important part. It's not only where the consumers are going on-the-go with smaller packages, the margins are terrific on single serve, they're good for the retailer and they are good for us and it makes us less dependent on these deep discounted take-home packages that sometimes drag down the profitability of the category.

Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

So Brian, I think you would agree with me, margins can never be too high, I think. Unless we either start losing the topline or start losing shares, neither of which is happening. And we don't start the year saying, hey, we are -- what we do to expand margins. What we do is we are always thinking about ways to get a better price per pound and are always thinking about ways to get better cost per pound, lower cost per pound. And on the price per pound, we have three things going for us. One is we spent a lot of money building up our brands. And that in itself allows us to take some pricing, certainly keep up with CPI.

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Then our innovation, in most of our innovation, we get a higher revenue per pound, and that's why we keep bringing a lot of innovation to the marketplace. And the third one is the mix is working in our favor, and by that I mean our single-serve mix and our multi-pack business is growing faster than anything else in our portfolio. And by definition that gets us a higher revenue per pound. So all those things are driving for higher net revenue per pound.

On the cost side, Derek, your question on GES, we don't think of GES as the person in the truck, it is a really integrated system -- DSD rather as a person in the truck. It begins with GES and we've talked about it before. We think there is runway past 2020 in GES and what we are realizing is that where we've implemented it, we are beating our old assumptions. So we thought that the radius would be x, now the radius is bigger than x of what GES can serve. We thought that cost per case would be x and cost per case is turning out to be low. So we keep funding and I think part of it is Frito's incredible ability to keep learning and improving on everything we do.

The second big bucket for us is the automation and this is not automation that you just pick up off the shelf from somewhere. Our engineering teams work hard at automating everything, so the multi-pack, which is pretty complex thing, if you think about it in a bag your 20 different items, we worked on that for years and now our multi-pack packaging lines are automated and it's home-grown automation. And so we continue to do that to get more productivity there.

We are enabling our front-line with technology makes them more efficient in the store, makes them more efficient getting to a store and we are improving our ordering capabilities with technology, get more out of every hour that we have there. And then we continue on our journey on what we call the Smart Spend. We don't stay in hotels like this. Both those dimensions help us tremendously in terms of keeping that margin growth.

Kirk Tanner - PepsiCo, Inc. - President & COO, North America Beverages

We're usually at Marriott Courtyard.

Unidentified Audience Member

So question on topline and one on margins. From a topline perspective, in fact assuming Frito-Lay continues on its path right now, I want to focus more on beverages for a moment. We talked about a lot of innovation, you listed a bunch of innovations both up there in the screen. But from a share perspective, shares are at best slightly up or really flat, right. So a lot of work that you're doing not really amounting to on share growth, so lot of cannibalization. Dispel me if that's wrong, if you can tell me about that. And then the way you're funding that partially is the margin question, \$1 billion of cost savings every year that we hear was tough to track from our perspective, but we hear that's 10% of your EBIT, every single year coming through flexibility. At some point, I guess there was more room, but at some point that has to slow. You can't cut equivalent to 10% of EBIT every year on a consistent basis going forward.

So how do you get the algorithm to work beyond just the next few years if the innovation, it's on the beverages is working, assuming Frito-Lay's was the same and your \$1 billion have to kind of slow down?

Kirk Tanner - PepsiCo, Inc. - President & COO, North America Beverages

So clearly the innovation pipeline is robust and it's tied to the transformation of the portfolio strategy that we're very committed to. And I would say there is a large incrementality to the innovation, but it continues to be a very competitive environment. So those that innovate usually grow, and we've been the beneficiary of growth through innovation, so we'll continue to do that.

But the long-term plan is just that it's really pretty simple. Innovation, supported by productivity and really we think about our business in building brands, driving innovation, focus on execution fueled by productivity. And that talked a lot about the GES system and driving productivity and efficient with DSD.



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On beverage side, we have the same commitment and we've learned a great deal as partners with Frito-Lay to drive and extract some of that that value so that we can put that value back into, again that cycle of building our brands, adding innovation and enhancing our execution. We still think there is room to grow across all three of those measures across the brands that we have, the innovation that we drive and then obviously we feel like our execution can still get better as we drive greater granularity down at the store level with our DSD system. But we see that as a long-term play.

Al Carey - PepsiCo, Inc. - CEO of North America

Ellie, in the share, I think it's, right now we're about even to slightly up, but just remember three or four years ago, we weren't gaining -- we were losing share, we were losing sales and the profit performance, it wasn't where we wanted it to. So we finally got this into balance. I think the long-term bet is if we keep investing in tea, coffee, sport drinks, water and some of these faster moving products over a long period of time, we will gain share.

Right now, it's a bit of a balance between staying in the CSD game, you have to be there because the volumes are high and also gaining on the new, what's called the new-age beverages, which in five years from now, I look at college campuses and I just give you one example, one story. Out on a college campus, asked the people on our marketplace which is the fastest selling product in the campus. Number 1, water. What's Number 2, Gatorade. What's Number 3, Lipton Tea. Number 4 is Starbucks. Number 5 is Mountain Dew. Number 6 is Pepsi.

So if you just fast forward, when these kids become 28, 29, 30, have their own families, that's what they're going to be buying. And I think when that time comes, we'll be in a much better share position if we keep investing in these kind products.

Unidentified Audience Member

And just a billion-dollar track record going forward from savings perspective, it has to be diminishing over time. So just a little bit more on that.

Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

Ellie, I'll tell you. In theory, you are right. At some point, we should hit the limits of physics on productivity. But I think technology keeps opening constraints that we believe we have today. I'll give you an example. I drive to work. On the other side, I see a Frito-Lay truck stuck in traffic, it just, it makes me mad, but the reality is in today's technology, that truck could have figured out that there was going to be traffic, then route it into a different store, brought them along. So we keep finding breakthroughs like that with each year that we felt there was a constraint and then something comes along that breaks that constraint. While I believe in the theory that there is a limit, I haven't seen it yet.

Unidentified Audience Member

Maybe just to put some numbers around those themes, on GES, can you just update us? I think on the Frito-Lay side, about 30% of the footprint has been converted over, just an update there. And the pacing of conversion as you talk about the runway to 2020? And then a similar some update on where we are analogous on the beverage side, Kirk?

And then second question, as we think about these premium occasions that you're going after, and I know it's hard to kind of make this line of demarcation in the portfolio, but can you give us some sense of how you would classify your portfolio in terms of the percentage that's premium healthy snacking, premium healthy beverage consumption, the rate of growth in that segment of the portfolio versus the core and then also the relative profitability of that growth, just so we can frame the future?

Al Carey - PepsiCo, Inc. - CEO of North America

Why don't you start with the portfolio?



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Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

On the GES question, you're right. We're about 30%. We continue to expand it. What we're finding is that where we -- there's two ways to think about it. One is investing capital in all our different sites where we converted to GES. And second is coverage of the marketplace. So we are finding ways to cover more of the marketplace with any initial investment in GES. So we're rethinking how best to spend that capital going forward. So that we can cover the marketplace in the most capital-efficient manner. So it's a slight re-think of what we might have said maybe five, six years ago, just that it's more efficient.

On the portfolio, we are affording share of the premium segment, in Frito, about 20% of the segment, 18% or so is what we'd call the premium better-for-you. So we under index on that. So we look at that and say that's a significant opportunity. It's also more the growing segment. So we feel good about the momentum there. Our premium business is growing, I'd say about 3x the rest of it. And so we've -- it's becoming a bigger part of our growth.

Kirk Tanner - PepsiCo, Inc. - President & COO, North America Beverages

Let me answer the GES question for the beverage side. We have a five-year roadmap to get there. The GES model in beverages is a little less cumbersome from an automation standpoint, and we have a clear path to do that over the next five years. We are about 15% into it right now, and continue to invest behind it and reap the rewards that we both enjoy.

Similar numbers on the beverage side from a premium standpoint, we continue to have a smaller portion in premium, but it is definitely high growth and products like Pure Leaf and Naked have definitely allowed us to see substantial growth and give us the runway to continue to drive that growth. At the same time innovating on our core business is still very important to us and premiumizing some of our products like Tea House and like some of the other products I mentioned before, definitely allow us to keep a solid ground on our core business and still allow us to enjoy growth on the premium side.

Al Carey - PepsiCo, Inc. - CEO of North America

About 48% of our business in beverages is CSDs and about 25% of my total business is CSD, to give you an idea of the mix.

Unidentified Audience Member

Just a broad question, and I apologize it maybe too broad. But if you just look at the productivity savings that Ellie mentioned 10% growth rate in operating profit, but you only guided the 8% local currency EPS growth every year and there you grow the topline 3% to 4% organically. I know there's some currency (inaudible) book. Why is the evergreen target 8% when every year you're 10% productivity?

Al Carey - PepsiCo, Inc. - CEO of North America

Yes, so Bill, the \$1 billion, if you look at as a percent of EBIT, but then you've got offsets to that, which is the natural rate of operating cost inflation as well as investments we're making in the business.

Unidentified Audience Member

Okay. But like if you don't have add the productivities, there'd be negative growth in the business? Do you know what I'm saying, like --?



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Al Carey - PepsiCo, Inc. - CEO of North America

Yes, for sure. If you look at the margins, and we don't talk about productivity x percent goes to the bottom line, but to the positive, you've got positive price mix, you've got productivity and then the offsets are going to be commodity inflation, operating cost inflation, investments and then you've got some negative margin mix depending on how quickly the developing and emerging markets are growing and some of that's also -- there is an investment element to the D&E markets.

But the net of all of that gets us to the 8% constant currency EPS growth. And if you look at what we've done since 2012, this model is working well, we are generating topline growth, we're getting a fair amount of margin expansion that's driving good earnings growth and good cash flow. So we think we've got a model that works.

Unidentified Audience Member

And then do you think we are on the other side of bell curve in terms of soda taxes and why you haven't seen similar taxes in some of the I guess like healthy snacks, because it seems like a lot of chatter has died down, but it still seems like people are still keen to kind of exact the pound of flesh.

Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

Is your question on snacks, or--?

Unidentified Audience Member

Snacks and beverages. We haven't seen anything on snacks.

Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

Yes, we haven't seen anything on snacks. But we are doing all the -- if you saw us report our new performance with purpose goals, the 2.0 taking salt out, fat out and we are going to continue down that path even though we haven't seen anything particular on snacks.

Unidentified Audience Member

How about on beverage side? It seems like the chatter has died down, but I'm just curious where you kind of think we are?

Kirk Tanner - PepsiCo, Inc. - President & COO, North America Beverages

The soda taxes are a problem. There are several markets that have implemented them. And it seems like they come into two categories, one is where you have real health concerns and we're working hard on our performance with purpose goals and making good progress on them and launching lots of new products in taking down sugar on the health side.

Then there is a group of cities and jurisdictions that are trying to close their budget gaps and it has nothing to do with health. We're working with the American Beverage Association. I'm on the board of that with the Coke and Dr. Pepper people and the other beverage people fighting these taxes because they are discriminatory and they don't seem to make sense, but that's -- we're doing that as an industry.



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Unidentified Audience Member

It looks like there is a rule of credible challenger in sports drinks, this is the first time, right? Another brand out there with good velocity and growing distributions. Can you talk a little bit about BODYARMOR? Could you talk a little bit about how you are thinking about that and for Gatorade beyond Flow and how you're defending?

Kirk Tanner - PepsiCo, Inc. - President & COO, North America Beverages

Absolutely. We treat all competitive activity very seriously, and Gatorade has been and continues to be a driving force with sports nutrition across an entire platform. We're reaching the athlete better than ever, being backed by science. We continue to innovate off the Gatorade platform and that's -- you saw us introduce G Organics end of last year. We'll continue to support that this year and we continue to build brands -- sub-line brands for Gatorade that allow a greater reach to consumers. And this year, we're launching Flow, which is a terrific sub-line. Last year we extended Frost, which reached over \$1 billion in revenue. So we are completely committed to driving the growth on Gatorade with the athlete through formidable experiences with the athlete. We reach over 7 million students each year and that's growing. And the competitive intensity certainly if that continues, we feel really good about where we're at with Gatorade, where we continue to drive the growth through the innovation and our support with A&M, we continue to lean into the growth in sports drinks. So we remain confident.

Al Carey - PepsiCo, Inc. - CEO of North America

We're approaching 80% share on Gatorade sport drinks. So we're going to attract competitors. Maybe you could talk about the custom products.

Kirk Tanner - PepsiCo, Inc. - President & COO, North America Beverages

Yes. In addition, again we do a lot of research with the athlete and part of that in the next generation is called GX and that is getting the formula right for the athlete. And working with each individual athlete and getting the formula that matches their sweat and really the output that they need in the form of electrolytes and carbohydrates. And that's a customized formula that athletes can get today and we're working with teams in the NFL and the NCAA to continue to build that science. But again, Gatorade is so passionate about the athlete that I'm confident we'll continue to innovate, ahead of the curve.

Unidentified Audience Member

So two questions for Vivek. So I guess, if you just kind of look at the macro snacking category, obviously, it's been a bright spot in the kind of the food category broadly. It seems like the growth rate has slowed a little bit. So just wondering if you can kind of share your perspective on what's happening to the broader category, what's the realistic growth rate for the category generally over the next couple of years.

And then as it relates the eCommerce, it seems like snacking is kind of pretty good category for eCommerce penetration to grow. So can you talk about what percentage of your snacking business go through eCommerce and what you're doing in terms of capability?

Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

First of all on the macro-snacks, you're right, Judy. The last -- I'd say, it seems like maybe eight to 10 weeks, it has been a bit of a slowdown. I will tell you that 13, just a week before Christmas was a monster week for food and beverage, and a monster week for snacks overall, bigger than anything in the past that week leading up to Christmas. So we think there was some shift in purchasing before the New Year that happened then. We've also seen -- there's been a lot less money in the marketplace, tax refunds with the delay to the [15th]. I think as of Feb 2, there was \$45 billion of less money in the marketplace. So, we think some of that is affecting consumption. So if we go back to, if you look at it steadily over the last two/three years, macro snacks has been around 2%, salty snacks has been around 3.5%, and there's no fundamental reason I've seen that it won't come back to that once we get past what I think are some both dynamics here and some lags that we're going through.



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So, I'm not worried about that. What I will tell you is that we are seeing, I'd say mid-to-high single-digit growth on consumption occasions, we track the panel on snacking and we continue to see that level of growth there. So I feel good about the category itself. eCommerce, we love it, actually we think of eCommerce both with the pure plays, think of the Amazons of the world. And then with the grocery click and collect. And in both those cases, we do very well, in fact it's equal to a higher share index in the basket that we see over there. Some parts of our portfolio play better than others in eCommerce. It's not a material share of the business yet, but it is an extremely fast growing part of our business and we feel very grounded in how we are doing well in it.

Unidentified Audience Member

My questions for you specifically on the challenges of leveraging the scale of having the beverage and snack business together, because it was noteworthy when you spoke to the second priority of serving the customers One PepsiCo, you made the comment it's starting to make some progress and starting to pay off. But I think it was five years ago if I'm not mistaken, there is a lot of scrutiny around the strategy, the company announced the findings of a strategic review and found that shareholders are better served by keeping the two businesses together. So maybe a little bit of historical context with the benefit of hindsight now and even today as you manage the two businesses together, some of the challenges in terms of leveraging the scale of both businesses. Thank you.

Al Carey - PepsiCo, Inc. - CEO of North America

Yes, sure. At one point, and I had been on both sides of the business so I can say this. When I was at Frito-Lay, the beverages were struggling a bit, and the ability for us to work together to drive the business was limited. I think since we've gotten the beverage business back on track, when you go see a customer at the senior levels, first of all when you are the largest supplier, it gives you a chance to have a seat at the table. And we've been very serious about making sure we have one leader on our top accounts. So when we go into see any of these big accounts, we cover Wal-Mart, Albertsons, we have one leader for PepsiCo and they drive the agenda and the divisions work with that person to make sure that we fit the needs of that customer. And Vivek ran the group before he had this job and I think he made a lot of progress.

The other thing that happened, which I think made a big difference was we consolidated digital marketing customer insights into one group and once we did that, I think that's the reason why our score went up on the Kantar rankings because we were bringing one set of insights to customers that was meaningful and we staffed that group appropriately, we put topnotch talent in there and I think the group is doing a very good job right now. That was one other thing that helped.

Also on the power of one side or the synergies one eCommerce group instead of trying to have each individual division do their own thing, we put that under one eCommerce. Foodservice is the same thing. And then as we start getting it outside of the customer side of things, we're looking at technology. So for example Frito-Lay invented a technology for their frontline route salesman that allows them to have a mini iPad that is so much better for ordering, forecasting and presenting to customers at store level.

We took that -- typically in the past, the beverage guys have to invent their own version of this. We just took the Frito-Lay version and we've rolled that out now to all of the front line salespeople, within the beverage business. And I think there is a couple of other ideas where synergies might work. We are beginning to work on them, the three of us right now. One is Frito-Lay does the best job of fleet management of anybody I've seen. They've moved forward on electric trucks, they have moved forward on lightweight sprinter vehicles that get high-gas mileage, not so on the beverage side. We're going to put those two together.

The other one is on I'd call it one transportation company. Could we do a better job on our over-the-road fleet and some of the transportation parts of our business doing it as one, I think there are some possibilities there that we've just started working on.



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Unidentified Audience Member

AI, also for you two questions pertaining to the scale you now have integrated so to speak, both from a beverage and snack perspective. One is, as you think about bolt-ons and the opportunity that is presented to you perhaps incrementally now that you are managing these businesses as you are, and the beverage business has the more stable trends, is your appetite for bolt-ons higher? How do you think about bolt-ons differently?

That's one question. And then the second question is if you think about the different channels you're selling in C stores versus large format, can you give us a little bit of a sense of where you think you're really making some progress, that significant leveraging these two businesses together and where the opportunity is really more of a white space opportunity, you really haven't made much progress and therefore, large format, you can go much further than you gone, say for example in C stores. So, just trying to get some channel comparison.

AI Carey - PepsiCo, Inc. - CEO of North America

Okay. So on bolt-ons, we definitely have an appetite for bolt-ons. And I give you one example where it worked well. So with the Kevita business, we watched that business for a while. It was very interesting. Looks like it had rapid growth, it was a new healthy category and we took a stake in that business and watched it over a couple years, and then we eventually got the business. And I think it ended being a win-win for the company and for us, but we're going to be very careful about what we pay for these deals. Some of the attractive smaller companies out there have multiple expectations that are quite high and we want to make this a profitable business down the road. But if you take a look at Kevita, there are many other very interesting smaller businesses out there that I think could be attractive for PepsiCo.

On the channel, maybe you guys could help me out on this, if I were to say one channel for leveraging our scale, there's opportunities in every single channel. I think one place we've done a great job at is the dollar channel. And I would say that one area for big opportunity is foodservice. And I think sometimes we still to look at -- when I was at Frito-Lay, I looked at the foodservice business like some ancillary little business, it's 10% or 11% of their mix. And on the beverages, now that we have this broader portfolio, it's more interesting than just selling cola. We have a real chance of changing the business in colleges, healthcare, business dining, those kinds of feeders that right, I think we're really small compared to where we could be.

Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

I'd just add that I think, if you set aside the channels we'd become really good at working together on holidays. And it's a material part of our business. So, six holidays times three weeks each, synchronizing things, developing programs that are truly integrated executing it at the same time in the stores. So, we're really terrific at that. I think we have opportunity on an everyday basis if we do the same kind of thing in large format. So if you look at it, we still think there's upside.

AI Carey - PepsiCo, Inc. - CEO of North America

So, one thing that helps is -- I have been on the Pepsi, started for Pepsi back and forth. Vivek has done both sides, Kirk has done both sides. So I looked at the Top 10 positions in North America for our management team among all of our businesses. Eight of the 10 has been on both sides of the business. And the three of us, we have one people plan, new succession plan for North America and we are really convinced that you have to have both sides of the business. What I found is that Frito-Lay is a precision, a machine at execution. And there's nobody like Frito-Lay and then when you move over to the Pepsi business, I remember when I came over I thought this is going to be easy, it's a little different when you have a big competitor bigger than you are and it teaches you the art of competition and also to be very diligent about looking at the marketplace and what's going on, and the combination of two is a great combination. But if you come with just one, it makes it tough. I was brought to my knees the first six months, I was in the beverage business, it is a tough go.



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Kirk Tanner - *PepsiCo, Inc. - President & COO, North America Beverages*

Let me just comment too on the foodservice business. I had the chance to run that for PepsiCo for three years. Again when you pull together your total portfolio, your offering, your customer base, access to, really a full access path to PepsiCo and I can tell you that makes a difference. And they lean in on the growth and when you show up with growth and you talk about growth with your customers, you are a stand out. In our commitments to outgrow our competition using the total portfolio of PepsiCo and resources of PepsiCo and foodservice is a great example of that, small format and then these customer teams that we have today, really drive the growth. And that is the mission. And it continues to work. And I would just echo the comments on talent, on building talent across our teams is essential something that we work on each day. We talked about it on a weekly basis about moving talent from our businesses one to the other.

Unidentified Audience Member

Judy's question earlier on eCommerce. What are you doing about it, winning that (inaudible) last week said, PepsiCo was representing about 18% of the growth in retail while representing just 10% of sales. So is it the same numbers do you see in eCommerce and what you're doing to run that if not to win in this channel. And the second question is more about, I know I've got in front of me the US crew here, but since like the US is rating in wholesale lenders, how this is replicable outside of the US, internationally, that great model?

Vivek Sankaran - *PepsiCo, Inc. - President & COO, Frito-Lay North America*

Let me talk to you about eCommerce. First, it's hard to get all the same numbers in eCommerce as we do from the retail side of the business. So it's hard for me to tell you what percent of the total growth we represent, et cetera on eCommerce. What we've done, we have created a group in, first, it's a global group responsible for eCommerce and there's a group within North America responsible for eCommerce. And we went and brought a lot of people from outside PepsiCo, we realized we didn't understand the space. And it's not so much the physical side of it, it's really about how do you win the screen and that's the skill set that we didn't have. And so we have a bunch of people that's all they think about at this point.

And then we have others within the businesses that are changing two, three things that are essential for eCommerce. One is speed of how we get things done. We can get a product out literally in five days for the eCommerce business. We try to do things like that, packaging, various et cetera.

And the second is the supply chain, making sure that what we're finding interestingly is that our existing distribution capability, because in the DSD and our products going to travel with, warehouses all over the country and manufacturing all over the country. So by definition we are quite distributed already. And so that's actually turning out really interesting advantage in eCommerce, because we just ship it to goods over DC want to from our closest location. So we feel good about all of the trajectory. Unfortunately I was not able to tell you the level of growth we represent on the total basis.

Al Carey - *PepsiCo, Inc. - CEO of North America*

My guess is we're not anywhere, we're not at 18% of the growth of ecommerce, that's not at all. But we need to do some work on packaging to be in more of ecommerce friendly packaging, which we're doing right now. We'll get there, but we're little behind on that.

Unidentified Audience Member

(inaudible) in US replicable outside of the US scale?

Al Carey - *PepsiCo, Inc. - CEO of North America*

We have a leader who's run the global eCommerce business and then --.



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Unidentified Audience Member

No, more broadly with GEs.

Al Carey - PepsiCo, Inc. - CEO of North America

I see what you are saying. Okay, we have global groups, one for nutrition, one for beverages and one for snacks. They are scouring the world for good ideas and they're also working with R&D on developing the future products so this is one example that came out of the GE group. The global groups identified premium water, something that we should do, and they actually came up with the idea, I'm quite sure that it was a very good idea taken the art of young developing artists and give them a chance to succeed by getting their art on the front package of these products and then every quarter this art is going to change. We have three into quarter one, we'll have three more. These were young artists that are budding artists. Now they're doing --. We met them at the Super Bowl. Their business has blossomed now. The next round is three young women artists are kind of go on here, and then we'll change this out every quarter.

It's a cool idea that came from a group of global people that work in our company and also a design group, which is our Global Design Group. It's in New York City and they will part. So I think the sharing of ideas around the world is a possibility for us. There are things going on in different parts of world I don't know anything about and if it wasn't for these, GEs, I would not get the opportunity to sell some of these products.

Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

Our model is boringly simple. We spend money on brands, we come out of the lot of innovation, we are maniacal about execution, and we're funded with productivity. And the role of these global groups is to take that the first two on brands and on innovation and make sure we get leverage on it globally.

Now, when it comes to the third bucket, on execution and productivity, we have other groups that also cut across horizontally. So when we are talking about a lot of the go-to-market ideas from we have to find a way to get or prevent a traffic routing as an example of any capability we develop, we've got those groups trying to make sure that it's applied all the DSD organization or operations across the company. So, we're trying to get that same degree of leverage and excellence in every part of the company.

Bryan Spillane - Bank of America Merrill Lynch - Conference Co-Chair

Can you take one more question?

Unidentified Audience Member

We spent the past day and half talking about the lack of sales growth, especially in the center store. You guys provide growth. So are you getting your fair share of space, if you see an opportunity for incremental space? And then as a part of that, is there an opportunity to expand a bit more on the snack side to get to consumption occasions, which you are not, if you can answer that?

Al Carey - PepsiCo, Inc. - CEO of North America

You're asking three sales guys if they think they should get more space?

Unidentified Audience Member

Yes.



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Al Carey - PepsiCo, Inc. - CEO of North America

When I think a couple of example, let's just take beverages for a second. If you go in there and just try to battle it out, give me a few more spacings, it's very boring for the retailer to have to deal with this. But if you can come in with new ideas for example, if you look at the non-card businesses and you look at the healthier drinks, the world is changing fast. This water business is on fire. It's probably going to grow double-digits this year. And the customers open to looking at insights that leads them to new merchandising strategies. I think there is a great opportunity to really recreate the beverage gondolas set and the way you merchandise beverages in the stores.

For example, we're going to go after, I'd call it the next generation CSDs, single-serve, lower calorie, smaller packages, so you're not held captive to these low-priced 12-packs. Customers are very interested in this. And they're interested in letting us experiment with new sets and rolling them out, because they realize the world is changing fast. One example, one very large customer believes in the single-serve business and they've now put in 60 to 84 foot single serve open-air coolers. And you can't believe the increase in their single-serve business and their overall beverage business from doing this and it pairs up with some of the meal solutions that they've got, but they're making 35% to 40% margin on all of these products instead of a 5% margin that you might sometimes see on these multi-packs.

It really makes a difference for the customer. Those kinds of ideas are working. That's how we'll get more space rather than the usual battle of we deserve to spacings versus our competitor, and it gets pretty old. Now on the snack side.

Vivek Sankaran - PepsiCo, Inc. - President & COO, Frito-Lay North America

We will get more space, because we continue to be the highest cash per square foot to just go with that raw metric, there is nothing better than our portfolio. The innovation we bring continues to help us get more space. For your second question, we went into the frozen section with Doritos loaded, some of you may have tried it, we launched that product last year. We've expanded that now into most almost all of retail. It's been an interesting learning for us, it actually works very well and so we're going to continue with that pipeline. So we try to get out of our space, if you think of our space as savory snacks, we try to get out of that carefully and slowly and deliberately where our brands can make a difference and we're having some good early wins in some of those areas.

Kirk Tanner - PepsiCo, Inc. - President & COO, North America Beverages

If you think about space in the store, it really comes down to what both Al and Vivek talked about, it comes down to performance, how you're performing with the space, how well you're performing on your current space and also your innovation pipeline. How are you going to bring new shoppers down the aisle, and the experience that the shopper has at the shelf at that moment of choice and with our DSD system, we have the ability to help customers own that moment of choice with great execution at the shelf. And those are the three things that we focus on. When Al talked about serving our customer, one of the things they need help with is center store excellence and that's what we're committed to and that's what generates the space. It's really the proof in performance, your innovation pipeline and your ability to execute at the shelf and we're committed to all three of those.

Bryan Spillane - Bank of America Merrill Lynch - Conference Co-Chair

Alright, I think with that -- first, join me in thanking PepsiCo for spending the time with us. We're going to move over to the breakout now. And we'll be over there in a few minutes. Thanks.



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