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# PepsiCo, Inc. (PEP)

## Q3 2023 Earnings Call

# CORPORATE PARTICIPANTS

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*Senior Vice President - Investor Relations, PepsiCo, Inc.*

**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*

**Hugh F. Johnston**
*Vice Chairman & Chief Financial Officer, PepsiCo, Inc.*

# OTHER PARTICIPANTS

**Bryan D. Spillane**
*Analyst, BofA Securities*

**Lauren R. Lieberman**
*Analyst, Barclays Capital, Inc.*

**Andrea Teixeira**
*Analyst, JPMorgan Securities LLC*

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

**Peter Grom**
*Analyst, UBS Securities LLC*

**Nik Modi**
*Analyst, RBC Capital Markets LLC*

**Chris Carey**
*Analyst, Wells Fargo Securities LLC*

**Robert Ottenstein**
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**Filippo Falorni**
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**Brett Cooper**
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# MANAGEMENT DISCUSSION SECTION

**Operator**: Good morning, and welcome to PepsiCo's 2023 Third Quarter Earnings Question-and-Answer Session. Your lines have been placed on listen only until is your turn to question a question. Today's call is being recorded, and will be archived at www.pepsico.com.

It is now my pleasure to introduce Mr. Ravi Pamnani, Senior Vice President of Investor Relations. Mr. Pamnani, you may begin.

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## Ravi Pamnani

*Senior Vice President - Investor Relations, PepsiCo, Inc.*

Thank you, operator, good morning everyone. I hope everyone has had a chance this morning to review our press release and prepared remarks, both of which are available on our website.

Before we begin, please take note of our cautionary statement. We may make forward-looking statements on today's call, including about our business plans, guidance and outlook. Forward-looking statements inherently involve risks and uncertainties and only reflect our view as of today, October 10th, and we are under no obligation to update.

When discussing our results, we refer to non-GAAP measures which exclude certain items from reported results. Please refer to our third quarter 2023 earnings release and third quarter 2023 Form 10-Q available on pepsico.com for definitions and reconciliations of non-GAAP measures and additional information regarding our results, including a discussion of factors that could cause actual results to materially differ from forward-looking statements.

Joining me today are PepsiCo's Chairman and CEO, Ramon Laguarta; and PepsiCo's Vice Chairman and CFO, Hugh Johnston. We ask that you please limit yourself to one question. And with that I will turn it over to the operator for the first question.

# QUESTION AND ANSWER SECTION

**Operator**: Thank you. [Operator Instructions] . Our first question comes from Bryan Spillane with Bank of America. Your line is open.

**Bryan D. Spillane**
*Analyst, BofA Securities*

Q

Thanks, operator. Good morning, everyone.

**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*

A

Good morning, Bryan.

**Bryan D. Spillane**
*Analyst, BofA Securities*

Q

So my question is just around volume. There's been a lot of focus on that topic not just for Pepsi but just, I think, more broadly. So I know in the prepared remarks there's some commentary about a shift to small packs. But maybe, Ramon, if you could touch on what was happening specifically volumetrically for PBNA in the quarter and then kind of relative to what your outlook was for volumes coming out of 2Q just how that might have evolved as the quarter progressed.

**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*

A

Yeah, good morning, Bryan. Let me step back beyond PBNA to the broader company. We're seeing sequential volume improvement, if you take the last few quarters. So globally we're improving our volume. But more philosophically how we're thinking about, how we're managing the company, there's two big variables that we're trying to optimize. One is consumer interaction with our brands, and the proxy we're using for that is units or specific purchasing act. And then the other one is obviously margin for the overall business. And those are the two variables that we're maximizing.

In both cases, units are growing much faster than volume, and we're seeing that. You mentioned consumers moving to smaller packs. We're also in a way facilitating that through our pricing and mix strategy. And then we're obviously optimizing margin that as you saw it was a good improvement in our margin across the company and the particular businesses that you referred to. So that's how we're thinking about volume and margin.

When it comes to PBNA, we've been a bit more aggressive than in the other businesses with regards to volume optimization, and we've made some decisions especially around take-home water that we were able to prune some promotions that were not profitable for the business. And that has almost a 2.5 points of volume impact.

So that's how we're managing volume. It's clearly an important variable for us, but for efficiency in the plans and some others, but unit transaction and consumer interaction with the brands are the metric that we're trying to maximize as we're making these trade-offs between volume, net revenue and margin expansion.

**Operator**: Thank you. One moment for our next question. Our next question comes from Lauren Lieberman with Barclays. Your line is open.

**Lauren R. Lieberman**
*Analyst, Barclays Capital, Inc.*
Q

Great. Thanks. Good morning. Carrying on Bryan's question, but taking it a little bit further out into 2024, and it was great to get kind of some preliminary perspective on next year so early, but I was also curious how you're thinking about that balancing volume and price mix as we go into next year because price mix has continued to outperform and so just kind of thinking about that more forward look as well. Thanks.

**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*
A

Yeah, Lauren. We'll give you more details obviously in February when it comes to the actual composition of some of our key metrics. But what I will tell you at this point as we've obviously seen all the commercial plans from the different markets and our innovation plans and our productivity plans and our cost trends, that there will be still a higher inflation in our businesses and therefore there will be higher price mix versus not the last couple of years, but if you think about the historical price mix that we had in the past, I think 2024 will have a bit more elevated price mix in the equation than in the previous years. Hugh?

**Hugh F. Johnston**
*Vice Chairman & Chief Financial Officer, PepsiCo, Inc.*
A

Yeah. So right. To add a finer point to Ramon's comments, Lauren, if you think of pre-pandemic inflation being kind of in that 2% to 3% range, inflation is going to be elevated relative to that, and our pricing will be roughly in line with inflation. So that should at least give you a rough sense as to how things might shake out.

**Operator**: Thank you. One moment for our next question. Our next question comes from Andrea Teixeira with JPMorgan. Your line is open.

**Andrea Teixeira**
*Analyst, JPMorgan Securities LLC*
Q

Thank you. Good morning. So going back to your comments about volumes in PBNA. Was that specific to the quarter? Or should we still see about this 2.5% headwind to volumes you included and potentially into the first half of 2024? And if you can also comment on the volumes in Latin America. How should we be thinking towards the end of the year and potentially into 2024? Thank you.

**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*
A

Yeah, Andrea, so with regards to PBNA, we continue to optimize the portfolio. So we should be probably thinking about a couple more quarters where we'll continue to see volume decisions that again we're trying to maximize units and transactions, and we're trying to continue to optimize the margin of the business. And you saw that this quarter and balance of the year, we feel very good about the margin expansion in PBNA.

Now, when it comes to LatAm, there – it's mostly our snack business what you see there in our numbers. And we've been making again decisions around affordability making sure that our brands continue to be within affordable price points to consumers that we know that this possible income is limited and they make decisions a lot based on price points. So we've been reducing size, portion size of our products and making sure that we're still very affordable. And that has a repercussion on, has an impact on the actual volume. But again the transactions are much healthier, and that's the metric that we use to assess the health of the business with regards to consumer along with brand equity and some other metrics that we use obviously to understand full consumer picture.

So we'll continue to make optimizations, Andrea, as we need to absorb inflation and make sure that our brands remain a choice for consumers that are clearly more limited in their disposable income.

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**Operator**: Thank you. One moment for our next question. Our next question comes from Dara Mohsenian with Morgan Stanley. Your line is open.

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

Q

Hey, guys. Good morning. Could you just discuss the motivation behind the decision regarding guidance for 2024 a bit earlier than is typical? What do you think your level of visibility is at this point versus typical year? And as you look out, maybe what are some of the areas that give you confidence and what might be some of the areas where there's more uncertainty particularly given the volatile consumer environment here? Thanks.

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**Hugh F. Johnston**
*Vice Chairman & Chief Financial Officer, PepsiCo, Inc.*

A

Yeah. Hi, Dara. I can answer that one. I think in general, as we build the plans, we're focused on a couple of things. Number one is obviously the level of commodity inflation, and you know we buy forward at about nine months. So that's roughly in line with the past.

Number two is the balance of the PepsiCo cost structure. And as we've talked about the last couple of quarters, we've put even higher focus than we've had in the past on driving productivity and driving out unnecessary cost using the tools that we've discussed, the investments in digitalization, the investments in global business services, the investments in driving out overlaps within the organization. Because that work has been going on for a longer period of time, I think that gave us earlier line of sight into what we would expect our cost outcome to be for next year.

And then number three, we're in a good spot in many of the developed markets in terms of our commercial plans. We do joint business planning with our customers and we're probably in line to maybe even a little ahead of where we've been historically with all of that. So given the information was available to us a little bit earlier and given there was undoubtedly questions in the investment community on what 2024 look like given the evolving pricing and inflationary environment, we thought it was prudent to at least give some indication of what guidance would look like in 2024. So that's what drove the decision.

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**Operator**: Thank you. One moment for our next question. Our next question comes from Peter Grom with UBS. Your line is open.

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**Peter Grom**
*Analyst, UBS Securities LLC*

Q

Thanks, operator, and good morning, everyone. So I actually wanted to follow-up on Dara's question there, but just more in the context of your actual performance versus your initial expectations historically, because it's really been a while since organic revenue growth has actually fallen short of your initial outlook. So can you maybe just characterize your confidence in the 2024 outlook at this stage and really whether or not you've embedded enough conservatism just given what remains a pretty choppy backdrop for the consumer? Thanks.

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**Hugh F. Johnston**
*Vice Chairman & Chief Financial Officer, PepsiCo, Inc.*

A

Sure. Happy to address that. We obviously have a long history here of meeting or exceeding expectations both our internal expectations as well as the guidance including this quarter where we beat revenue and we beat EPS. In fact, we've now met or beat consensus for 55 straight quarters. So we tend to be I think appropriately conservative in the way that we communicate to you all. So from that perspective, I think you can go into 2024 with a similar expectation that we should at least achieve the numbers that we've laid out for you.

**Operator**: Thank you. One moment for our next question. Our next question comes from Nik Modi with RBC Capital Markets. Your line is open.

**Nik Modi**
*Analyst, RBC Capital Markets LLC*

Q

Thank you. Good morning, everyone. Hugh, I was hoping maybe you can just provide some of the macro underpinnings that kind of go into your 2024 viewpoints at this point, just would love to kind of get your state of the union on the consumer, the economy and kind of how you guys are thinking that'll shape up as you go through 2024. Thanks.

**Hugh F. Johnston**
*Vice Chairman & Chief Financial Officer, PepsiCo, Inc.*

A

Sure. Why don't I start and then, Ramon, obviously you're super deep on the consumer as well. But I'm happy to start on this one. Number one, I do think that we see the consumer right now being more selective. And you see it in a variety of ways, right? You see some trade down in terms of channels of trade that they're purchasing products in. You see some orientation toward value.

At the same time, the things that I usually look at with the consumer to detect whether there's high stress, we see good results in. Number one is the convenience store channel. Typically when gas prices are up and consumer incomes are stressed, you see revenue in those channels under stress as well. For Q3, we saw revenue up 5% in beverages and 8% in foods in the convenience channel. Number two is foodservice, that's also typically a leading indicator. That's still growing double digits.

So I think we've gone into the year with an approach that says, given all that I laid out during Dara's question, we expect the consumer to continue to be cautious and to the degree that they are worse than that, we've got cost plans in place that we would use to mitigate whatever challenges we face. But we think our revenue outlook accommodates an increasingly cautious consumer next year.

**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*

A

Yeah, and the other thing I would say is that all the long-term structural tailwinds of our categories will continue. If you think about urbanization, demographic shifts, lifestyles, et cetera, that have been driving our snacking categories, our beverage category, they move from package to package, all those things will continue, and they drive a lot of our confidence in our categories. Then obviously we have almost completed by now our innovation plans, our commercial plans. I think we got better at affordability and premiumization of our portfolios. So we think our share of market will be good next year as well. So that's what's driving our kind of confidence for next year.

**Operator**: Thank you. One moment for our next question. Our next question comes from Bonnie Herzog with Goldman Sachs. Your line is open. Again, Bonnie Herzog, your line is open. If you have a question, go ahead and ask it. It looks like they didn't have a question. Do you want me to go ahead and move on to the next person?

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**Ravi Pamnani**
*Senior Vice President - Investor Relations, PepsiCo, Inc.*

A

Yes, please.

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**Operator**: Okay. Sure thing. One moment. Our next question comes from Chris Carey with Wells Fargo. Your line is open.

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**Chris Carey**
*Analyst, Wells Fargo Securities LLC*

Q

Hi. Good morning.

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**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*

A

Morning, Chris.

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**Chris Carey**
*Analyst, Wells Fargo Securities LLC*

Q

The inflation got a bit worse quarter-over-quarter in the PBNA segment specifically whereas in the rest of the segment the trend is for continued easing. Can you just comment on some of the puts and takes that you're seeing from a commodity inflation standpoint in this segment particularly in how the beverage side is driving the inflation expectations going into next year relative to food? I'm really tweaking to Hugh's comments on above average inflation next year and just given what we see from commodities, in general, I'm trying to parse out where exactly that outlook is coming from. So thanks so much.

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**Hugh F. Johnston**
*Vice Chairman & Chief Financial Officer, PepsiCo, Inc.*

A

Yeah, good morning, Chris. Chris, we don't get into by commodity levels of dissecting the numbers and guidance. That's something that historically we haven't done. As you know, the beverage segment is a little more packaging exposed than foods is just by virtue of the nature of the products. But I'd rather not go any further than that to get into the specifics of individual commodities for competitive reasons.

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**Operator**: Thank you. One moment for our next question. Our next question comes from Robert Ottenstein with Evercore ISI. Your line is open.

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**Robert Ottenstein**
*Analyst, Evercore ISI*

Q

Great. Thank you very much. Just want to shift a little bit more kind of to the long-term. And I was just wondering if you can kind of give us a sense of the vision, your vision for the business, the beverage business and the food business in the US in light of your large investment in Instacart, what you're trying to accomplish there, and other kind of strategic moves you're doing on the digital side and all the underlying work that you're doing in terms of automation and productivity. Just kind of what do you see the business looking like in the future and how does Instacart play into it? Thank you.

**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*
A

Yeah, good question. Obviously as you were saying, we continue to drive the transformation of the business with automation at the center of it and digitalization as well. With digitalization, we're trying to obviously give much more precision to our decision-making across everything we do from how we talk to consumers, how we invest in our pricing with our customers and how we run our end-to-end operation from agro to the consumers, how we run our routing and everything, and all these activities that we do to generate value for our consumers.

That is an investment we've been making over time, and that still is the priority of the company to make the company more precise and intelligent and empower our front line to make better decisions all the time with the best information possible real time and ideally forward information. So that is a continuous investment.

Now, when it comes to Instacart, there is a commercial relationship trying to enhance the capabilities of our DSD system with the shoppers that they have in store, and that is a continuous focus. I think DSD continues to be a competitive advantage, and I think we can enhance that capability with supporting activities from the Instacart shoppers, and that commercial relation led to a very minor investment in Instacart and just to reinforce the commitment to the commercial relationship, it's – there's nothing more than that in terms of a strategic long-term intentionality with that investment.

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**Operator**: Thank you. One moment for our next question. Our next question comes from Steven Powers with Deutsche Bank. Your line is open.

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**Steve Powers**
*Analyst, Deutsche Bank Securities, Inc.*
Q

Hey, thanks. Two questions if I could. One just following up on the 2024 outlook, given the visibility you have on costs and the commercial planning at this point, should we be expecting a relatively even performance and cadence of growth both top and bottom line throughout the year? Or is there reason to see that growth weighted first half versus second half?

And then I did want to ask on Gatorade because the improvement we saw this quarter sequentially volumetrically did occur, it just didn't occur at quite the level of improvement that we were expecting from a shipment perspective. I think we went from down high-single-digits in the second quarter to down mid in the third. So I just would love some perspective on how you view that business performing. Thank you.

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**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*
A

Good. Listen, we will not go into more details on 2024. We'll cover that in February in due time. When it comes to Gatorade, we're very pleased with the [ph] G2 DSD (00:21:56) or the movement of [ph] Gatorade 2 the DSD (00:21:58) platform over the summer. We're seeing sequential improvement in the performance of the brand, better performance in August than we saw early in the summer, et cetera, inventory on this play and number of secondary locations, et cetera. So that move is working.

On the velocity of the brand, we also saw that the brand is improving its velocity. It is true that the emergence of Prime in the category took some share from Gatorade less than other brands in the category or less proportionally to the size of the brand. But I would say Prime impacted Gatorade in a way in some transactions during the peak of the season. We're seeing the size of Prime in the category getting smaller as we go into the fall which gives us very good optimism that, with the new infrastructure we have with our DSD business, some of the innovation with

GFit, Gatorlyte, G Zero, our powders and tablets that are being very well received by consumers, that we're going to have a very good 2024 for Gatorade. So we have a stronger foundation to go into next year with potentially weaker competition. But obviously I don't know what their plans are.

**Operator**: Thank you. One moment for our next question. Our next question comes from Filippo Falorni with Citi. Your line is open.

**Filippo Falorni**
*Analyst, Citigroup Global Markets, Inc.*

Q

Hey. Good morning, everyone. So clearly there's been a lot of concern in the market around the adoption of GLP-1 drugs in the US and potential impact on your business. So maybe can you comment a bit on what you've seen so far, based on your consumer studies both on the beverage and food side, and how you're thinking that can evolve over the next couple of years [audio gap] (00:24:08) change in consumer behaviors? And then from a Pepsi specific standpoint, what changes can you make to adapt your portfolio to these new consumer preferences that could emerge if the adoption is greater than that? Thank you.

**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*

A

Thank you, Filippo. Good question. Listen, obviously we're looking at this along with many other positive and negative potential risks for our business and our category. So far, the impact is negligible in our business. Overall, if you take global consumption, there's obviously a lot of question marks with regards to this – obviously, the drugs when it comes to medical testing or scalability of the usage of this or what is the impact really on consumer choices. So a lot of question marks.

We continue to believe that all these structural positive trends that we had to our categories remain. And I mentioned and referred to that earlier in the conversation. So we're seeing urbanization as a big driver of adoption of our categories. We're seeing middle-class development. We're seeing lifestyle and people snacking to eat, so meals becoming more mini meals and much more unstructured during the day, being a big driver of our categories both beverages and snacks. So we're seeing a lot of tailwinds that will continue to drive our categories. Of course, we're observing the growth of these new drugs and its potential impact.

The other thing we're looking at is our strategy sound when it comes to portfolio transformation, and everything we've been doing for the last five, six years when it comes to reducing sodium, reducing fat, reducing sugar, reducing the portions of our products, adding some new cooking methods to our snacks, those are all very positive trends that will help us deal with the portfolio if needed in the future. We'll continue to do it, obviously. It's one of our key strategic pillars.

So again negligible impact today. A lot of these structural trends that are in our category I think remain very solid and even we see them accelerating. And our portfolio strategy we think is very solid when it comes to a potential protection against some of these future developments 5, 10 years from now.

**Operator**: Thank you. Our last question comes from Brett Cooper with Consumer Edge. One moment.

**Brett Cooper**
*Analyst, Consumer Edge Research LLC*

Q

Good morning. A question for you on the North American beverage business. You've said in the past your goal is to hold share in that business. When you begin to add things like Celsius as an organic business, I would just love to hear how you assess the beverage performance and [ph] consumers need a (00:27:08) hold with the owned portfolio or just do distributed brand as a component to hold share? Thanks.

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**Ramon L. Laguarta**
*Chairman & Chief Executive Officer, PepsiCo, Inc.*

A

Sorry. We missed a little bit of the question, but hopefully we got what you were trying to ask. Celsius obviously is part of our energy drink strategy. We said we had multiple pillars, and our ability to distribute in our system some third-party brands is part of that strategy. Obviously Celsius continues to grow. We've doubled the distribution and the presence in store of the brand in the last year or so, especially in the convenience channel which is a key channel for energy consumption. That participation of Celsius in our track makes our full system more efficient. It makes our salesmen more relevant in the store. It makes our cooler more a go-to cooler in the store.

And those are all positives that eventually have a halo effect as well in the rest of our portfolio. So I don't know if I'm answering the question because really we couldn't really hear it very well. But I guess you get a sense of the importance of Celsius in our energy strategy and the value we get from both the actual monetization of that distribution but also the halo it has in the rest of the portfolio.

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## Ramon L. Laguarta
*Chairman & Chief Executive Officer, PepsiCo, Inc.*

Okay. So thank you very much for your questions and for joining us today and especially thank you for the confidence that you've placed in us with your investment. We hope you all stay safe and healthy. Thank you very much.

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**Operator**: Ladies and gentlemen, this does conclude today's presentation. You may now disconnect. And have a wonderful day.