Consumer Analyst Group of New York Conference

Company Participants

- Hugh F. Johnston, Vice Chairman, Executive VP & CFO
- Ramon Luis Laguarta, Chairman, President & CEO

Other Participants

- Ali Dibadj, SVP and Senior Analyst, Sanford C. Bernstein & Co., LLC., Research Division
- Andrea Faria Teixeira, MD, JP Morgan Chase & Co, Research Division
- Brett Young Cooper, Senior Analyst of Beverages & Managing Partner, Consumer Edge Research, LLC
- Bryan Douglass Spillane, MD of Equity Research, BofA Merrill Lynch, Research Division
- Judy Eunjoo Hong, MD, Senior Analyst & Co, Goldman Sachs Group Inc., Research Division
- Robert Edward Ottenstein, Senior MD & Head of Global Beverages Research, Evercore ISI Institutional Equities, Research Division
- William Bates Chappell, MD, SunTrust Robinson Humphrey, Inc., Research Division

Presentation

Bryan Douglass Spillane {BIO 2147799 <GO>}

So we're ready for next presentation from PepsiCo. So we're very excited to have PepsiCo back at CAGNY again this year. Joining us today for the first time as Chairman and CEO is Ramon Laguarta; along with Vice Chairman and CFO, Hugh Johnston; and VP of Investor Relations, Jamie Caulfield.

Ramon, I'll turn it over to you.

Ramon Luis Laguarta {BIO 18967774 <GO>}

Right. Good afternoon, everybody. Do I sound okay? Good. Thanks. Thanks, Bryan, for your introduction. And thanks for hosting all of us, Hugh and Jamie, myself, today. It's a pleasure to be in this beautiful place. For a Mediterranean guy, to be in the sun is something invaluable. So thanks for taking me out of New York down to the sun. And thanks for this terrific event.

I must admit, for those of you who listen to the call on Friday, this might be a little bit repetitive. And you guys might be probably tired of this faster, stronger and better concept. But we will repeat it again. For those of you that were not on the call, hopefully this is a good use of your time as you think about the next chapter for PepsiCo.

Let me spend a couple of minutes on the process itself, how we got to this new chapter. Because it was a good process for the management team. It got us all together and it got us into a future vision that was very exciting for all of us. We spent -- about 30, 35 people. So it was not only the top of the pyramid, it was a group of senior leaders from the company, over four months, different sessions, talking about our performance historically and then trying to go after areas of dissatisfaction with our performance. But also trying to align ourselves, what inspires us, what really motivates us and what is the potential of our company? So the chapter you will see is the aligned input or output of those sessions. And really, a common purpose for what is the top management of the company overall.

There were 2 areas that, although we were quite happy with our historical performance, as you will see, there were 2 areas that we said were not really capturing the full potential of PepsiCo. And one was we're not gaining market share consistently across the world. We have a lot of good pockets of great performance. But we're not gaining share consistently. And second, we thought that the speed of transformation of our capabilities, our cost, was not fast enough. So those 2 were the 2 areas of dissatisfaction. And that's what we want to call ourselves in this mission of taking PepsiCo from being in a very good place to being in a great place.

And before I go into the detail, otherwise Jamie will kill me, please read the safe harbor statement, or you can find it in our -- in pepsico.com.

This chart summarizes the next chapter. So let me just spend a couple of minutes on this chart. The key idea is we think we can deliver a balanced, sustainable financial performance. And therefore, good value for all of you as investors in PepsiCo, by having a growth model that's based on an accelerated top line expansion with the right levels of reinvestment so that we can transform ourselves over time and sustain that performance.

And there are strategies around becoming faster, around becoming stronger, around becoming better that are distinct from the past. And I'm trying to summarize. And there are strategies around accelerated investments. So how we're going to be investing in the business; about becoming a much more centric -- consumer-centric company; the way we're organized; the way we think about our costs; the way we think about our investment in capabilities, with very intentional areas where we want to invest; and also the way we think about our purpose and how we integrate that into our strategy. So let me unpack all of this in a couple of minutes.

Before that, I think what differentiates us from many other companies is we start from a position of strength. We start from a very strong foundation. And this is not only because we play in very attractive categories that grow very fast. They are large. So if you think about our beverages category, it's almost $1 trillion globally and is growing almost at 4%. The same with micro snacks. Micro snacks is almost $800 million globally and growing even faster than beverages. So we compete in very strong categories, complementary, a lot of common occasions between our 2 categories. We have -- within those categories, we have very strong, leading brands. And we have a very good product portfolio, as I'll show you later, that helps us cover a lot of these spaces in those categories. And we can evolve the portfolio with our brands into new spaces that get generated with new consumer needs.

We have a strong geographical footprint. We have a lot of positions of strength in many countries around the world, both in developed and developing markets, from which we can accelerate our growth.

In terms of the capabilities. We have strong, relevant capabilities in top line growth, also in productivity, that we can scale across the globe.

Then we have, I think a differentiated culture that is centered around growth and a very (good) talent in many parts of the world. I think that will become a competitive advantage going forward.

With that, we've been delivering, I think good performance over the last few years. So if you think of from 2012 to today, we've been delivering almost a 4%, 3.8% top line growth. Although it's true that the last two years, we've been probably lagging a little bit behind what we think is the potential of the company. We've been expanding our core operating margins. We've been delivering 9% EPS year-after-year. And we have been increasing our ROIC. And obviously, returning dividends and share repurchases. So a pretty good financial performance. But as I said, 2 things that leave us dissatisfied is our marketplace performance; and it's the way we're transforming ourselves, the speed of transformation of our (inaudible) to remain competitive and within the marketplace.

So with that, let me go into the priorities that will set this next chapter of PepsiCo. The first one is about becoming faster. And this, of course, is the #1 priority for us, is accelerating, increasing the speed of growth of our top line. And with 2 things: becoming more consumer-centric in our innovation, the way we think about the different consumer spaces in our categories; but also taking a higher investment, higher-growth posture against the opportunities that we have in the marketplace.

So 3 things here. First, we're going to play our portfolio against all the different multiple vectors in our categories, I'll show you later; and then investing in both our large U.S. businesses and our international business for future expansion.

Before I go into the portfolio, there's a growth model that applies to both our snacks and our beverages category. It's been proven for us over many years. And all our commercial initiatives will be centered around this growth model. And this is a, what we call, the 4 key benefits that our consumers are looking for in our categories.

Number one is variety. And variety is very important in both snacks and beverages. Those are 2 (relative) to our categories. I mean, the majority of consumers. And you probably (yourself) yourself, snack several times a day, drink several times a day. And you guys choose different brands, both in snacks and beverages, for different parts of the day. (Having) a repertoire of brands and products that cover multiple demand spaces, be it in the morning, at night, during the day, different satiation needs in the different occasions for snacks or different functionality in beverages, it is critical to really capture all the occasions.

The other important piece for us is ubiquity. Ubiquity means -- we're an impulse category. So the ability to be everywhere where you have the need for a snack or our beverages creates a lot of value for you as a consumer and for us as a manufacturer. So for us, investing in this capability of being everywhere is a must-do.

The third one is creating brands that obviously hook the consumer, creates higher loyalty, creates that emotional link with our products.

And the fourth one is value. And value in developing market is clearly about affordability and price points. In developed markets, it's also affordability. But it's more about what are the benefits that go with the product so that we have a full consumer experience.

So everything you will see in our business. And we'll talk in the future, is around giving the consumer those 4 key benefits on a consistent way and on an advantaged way.

Now our portfolios and how we think of our portfolios. You see, this is a -- I think a great portfolio. Broad. It covers all the spaces from indulgent to nutritious. It covers different price points. It covers individual consumptions, social consumption. The way we think about this portfolio, obviously, we will keep evolving the portfolio in all the different vectors. We want to maximize the coverage that we have, all the different occasions of micro snacks. But we think about the portfolio in a way that we want to make sure that our global brands, our core brands are funded, they are healthy, they keep being modernized, they stay relevant to the customer every other time. Then we add to those big, global brands; big, core brands, some smaller brands that will become bigger in the future but -- that will give us the growth. But clearly, without our core brands healthy and growing, the whole portfolio doesn't work.

As you think about snacks, obviously, the big idea for us is taking this (beautiful portfolio) around the world. I must (say) we're not there right now. And that is a huge opportunity per se. But the other idea is as you think consumers moving more towards convenience and on-the-go, we will try to expand ourselves into occasions that are closer to mini meals, very close to street foods in developing markets. And that will be a huge area of growth for us going forward.

You think about our beverage portfolio similarly. We have -- we cover indulgent occasions. We cover nutritious occasions. We cover (personal). We cover hydration. We cover a lot of different locations. We have beautiful brands. And we have solutions for many different need states. As you think of ourselves in the future, we will be innovating across all the different spaces. Again, we want to make sure our core brands stay healthy, well-funded, they grow. Then we will obviously invest in new spaces that will define the category for the future.

Also, you should think of ourselves investing quite a lot in creating a beyond-the-bottle space, what we call beyond the bottle. I mean SodaStream is a great example of how we're thinking about new spaces of consumption that do not require a bottle and still allow the consumer to personalize their consumption. And we eliminate the need for a bottle and plastic and everything else. So that's from the portfolio point of view.

In terms of the geographical priorities. We want to -- we had -- in this meeting we had with our people, we saw that there were growth opportunities everywhere. And including our beautiful U.S. business. And so if you think about the way we want to invest, we want to fortify North America. North America is a huge part of our business. It's healthy. It's growing. We want to make sure that those businesses are well invested.

If we start with Frito, to me, is one of probably the best consumer companies in the world, very well run, excellent management, excellent brands, great infrastructure. But still huge opportunities. And I mentioned in the call on Friday, we're only 19% of micro snacks. You think micro snacks, we're only 19%. So there's 80% of occasions that we don't capture in -- with Frito-Lay in the U.S. You see channel opportunities, geographical opportunities. So we think this is a business that, well-funded, will capture much more growth. And obviously, we have huge return on investments on this business. So we plan to invest in our manufacturing capacity. We plan to invest in our brands. We plan to invest in our go-to-market and enable Frito-Lay to continue this journey and also accelerate their market share performance.

The same applies to NAB. NAB, we know we have been underperforming the market for the last couple of years. Our goal is to get the business back into growing with the market. We know we have the brands to do it. We will -- and we started last year repurposing some of our A&M against our (bigger brands), taking money away from our smaller brands so we have a more holistic growth model.

We are investing in go-to-market. We think that we have opportunities to get more (capillar), at the same time, improving the way we service our large customers. We want to make sure that we have a cost-competitive and very flexible supply chain and also that we have an organizational model that allows us to service big, global customers but also be very locally relevant. And that's the recent announcement you saw on NAB. We're trying to have an organization that is able to be a bit more flexible in its pricing, in its understanding of the local routing and local opportunities. And I think we will generate additional performance because of that.

Internationally, you think about snacks, this is a great opportunity for us globally. I mean we have strong positions in many markets, in developed markets, in a lot of the developing markets. We have a very clear playbook on how to develop the category, how to build per caps of our business and how to build strong market positions, both with our potato chips. But some with our other products. So we will replicate the models that we have in Mexico, we have in Turkey, we have in Russia, we have in many markets around the world. We're going to try to replicate them globally. And obviously, the big dream for developed markets is to have the portfolio that I just showed you for Frito-Lay in all the developed markets. So if you go to Australia, you go to Western Europe, that would be our dream, to have that portfolio in those markets. And it's only a question of execution and discipline on the execution.

When you go to beverages, there we have different market positions in different parts of the world. We're going to have a much more nuanced approach to beverages, investing more where we have the right to succeed, where we are leaders or we have strong battleground positions; and then being more smart about where we invest, how do we invest when we have a smaller market share. So again, I think I covered this, where we're going to make investment. We're going to make investments in manufacturing capacity, digitizing the business, supply chain, go-to-market and A&M. Yes.

The second pillar of our strategy. And to me, is most important, is how do we become stronger? And the word stronger to me is -- this gets to the operating machine of the company. This really gets into the how do we operate in a way that we are leaner, that we're more agile, that we're more focused, that we're more -- we're operating with more precision? So it's how do we get our supply chain, our go-to-market, our insights, our marketing to be much more precise, agile? And that is a journey that, if we do it right, I'm sure we'll do it right, will give us the sustainability of the accelerated model. So that -- this is what keeps the model sustaining itself and allowing for us to become more competitive every day versus our competitors in the marketplace.

There are 3 things that we put here. One is elevating cost to a much more strategic role in the company. So we want to make sure that cost and cost management and cost transformation get a lot of management time. And we have -- as I show you, we have a playbook. We have some very clear principles. And we're going to transform holistically our cost structure on an ongoing basis, adopting technology, adopting data in a way that allows us to execute with more efficiency, at the same time, be more effective.

Then we're going to be very intentional on where we invest those savings. There are a few things that will make us really perform much better in the marketplace. And those are the capabilities we really want to be best in class. And they will give us the superior performance. I'll talk to you about it. These are capabilities in the areas of consumer, customer and an end-to-end supply chain, which is going to be a big accelerator.

And the third point is all this will not happen if we don't have the right talent, a differentiated culture that is focused on high performance and an organization that allows us to be very locally relevant, winning every geography. But at the same time, be connected as a company in what could make a difference globally. So let me unfold that a bit better.

In terms of cost. We're going to work on 4 areas -- 4 big areas of cost. Obviously, redesigning work so that we create better jobs. And at the same time, reduce labor costs, right. So we're seeing that some of our positions, our jobs, our current jobs, will not be sustainable in the future. People don't want to do them anymore. We need to rethink them. So we're rethinking the way we operate in our warehouses, some of our sell-in, even some of our back-office roles, we need to really side them with technology in a way that will create better jobs for our employees. And in that, there will be a lot of, I think, efficiency. And then we'll do the work in a better way. Obviously, reducing nonlabor cost. Increasing the ROI of the commercial investments. And by that, I mean trade, space management cost and obviously A&M, getting into a much more rigorous way of understanding the return on those investments. Then increasing the utilization of assets, be it warehouses, be it vans, be it factories, be it our offices.

And we -- as a group, we created a set of cost principles that we're going to apply across the company. And those principles are not rocket science. But I think they give us a very clear expected behavior from all of us. And this is -- the first one is very relevant, which is local affordability first. We want to be competitive in every market around the world. And clearly, developed market costs cannot apply to developing markets. And so we need to think locally as we think about being competitive in every single market around the world. There are things like multifunctional collaboration. We think the next generation of value will be created by functions collaborating on an end-to-end of any process versus the very vertical functional optimization. And you will see one example as I talk about end-to-end supply chain, that (inaudible) is about the supply chain, factories, the go-to-market and marketing working together to unlock value.

And so there is a few principles that I think are very important. This one on not all capabilities and costs are equal is a very important one. We tend to invest in many, many things in our company. Making sure that we're very intentional on which capabilities will make the difference is a very important metric.

So we will -- as we apply those principles, we will change our operating models. And you saw the announcement in NAB this week. And we just changed also our operating model in the Asia, in AMENA region, trying to be much delayered and faster, agile. We will look at global business services as a way to service the company in a much more intentional way. We'll look at go to market. And for example, what I mean by this is if you think about, for example, our Mexico business, we are -- by applying technology to that business. We used to call on, I don't know, 22 stores per day on a normal route. By applying technology, we're able to increase that to 25 per day, reduce the number of hours that our employees work to the concept of making the work and the jobs more better for our employees. And at the same time, we're able to execute with much more precision, creating closed loops of executional management that we didn't have before. So clearly, a win of efficiency, be much more effective and ways that we will win in the marketplace. These are all the areas where we will be attacking.

In terms of where we want to reinvest and which are the things that we believe will make us a better company if we're best-in-class. And there are 5 of them. There's what we call consumer intimacy. You could call it consumer-ing or understanding consumers. I'll try to unfold that a bit more detail.

Building indispensable brands. Clearly, that has changed, how you used to build brands and how you build brands today. And so we need to adapt ourselves to the new reality.

How do you have top innovation that is based on science and is based on design? So we're good at that. We want to become really best in class.

The fourth one is very critical. As the consumers are moving into multichannels or omnichannels, we need to be able to service them in all these channels without friction. And that is a capability that we're building. We're good in e-commerce. We're good in DSDs. I'm not sure we're good in putting it all together. So that's the idea.

Then end-to-end supply chain. As we look at the future and we're able to disaggregate demand and understand consumers with much more detail, our ability to service that complexity will depend on having a very flexible supply chain. So it doesn't work if you understand your consumers in a very granular level and you're unable to service that because you have very rigid supply chain. So having end-to-end supply chain agility, being able to service your consumers in very different channels and with the complexity of the portfolio that we'll have in the future is a key capability.

Let me tell you about consumer intimacy just to get a sense of what we mean. And we'll talk more because, clearly, that's an area where you should know we're investing the money. And hopefully, we get returns from it.

So building consumer intimacy. This is the journey, for example, for the U.S. business. So we want to do 6 things. The first one is, obviously, understanding the consumer in a much more granular way. We used to understand consumers in groups of millions, cohorts or those big words. Now we're trying to understand at the household or individual level with multiple sources of data. Once you have that information, you can then go into personalized communication. This is an area that we're doing a lot. But we will do much more. Now we're maybe creating 20 messages for 100 audiences. In the future, we'll be creating 1,000 messages for 1 million audiences, this kind of magnitude of complexity in our communication. Clearly, having a machine that understands the return on your investments, to the point of commercial investment optimization that allows us to understand much more real-time, what is the best way to invest our money to get the best return for sales.

Then the last one is very critical, which is okay, eventually, we want to get to a place where we can have almost personalized pricing or personalized pricing for a group of consumers so we maximize the value creation for each consumption occasion. So that is the type of capability we're investing on.

The same one I was talking about end-to-end value chain and how do we unlock this, this cannot be unlocked by marketing working in silo and sales working in silo and the manufacturing and warehousing guys working in silo. This is the new way of unlocking value for companies, which is multi-functions working together with the same set of information against the same principles. And these were -- by us understanding consumers in a very granular way, being able to leverage our DSD to cover much more than just retail outlets that we go today, go supply in e-commerce and supply many other channels. And then have the flexibility of our infrastructure, manufacturing infrastructure, to supply that complexity is going to be a big accelerator of growth for us. And to tell you the truth, we're not even 6% of the journey here. So that's a big opportunity for us to do much better as we think about the future.

Okay. I think that's all. I covered that. But clearly, we would not be able to realize all this without changing our leadership behaviors, changing the way we're organized in a way that is much more empowering our local markets, our local organizations, to be closer to the consumer, have local portfolios, have local go-to-market systems, have local A&M. And that is going to give us, I think, a bigger return. But at the same time, we need to connect the company. We need to connect it because is a global scale and we can bring a lot of value as a global company to our local operations. So that's the complexity of how we want to get organized.

The same with the culture, their behaviors around being faster, being more agile, act as owners, that we want to make sure that every one of our associates lives those values. And that will be, I think, a competitive advantage for PepsiCo going forward.

And the last point is very important to me. And it's very important to all of our associates, which is we want to be a better company, a company that really makes an impact in the planet, makes an impact in the communities we service, make an impact with our own associates. And we're going to double down on this. We're going to double down on how do we become a better citizen. But we want do it in a way that we integrate it with our commercial strategies.

So for example, the SodaStream acquisition is a clear example of how we want to connect our commercial strategy with our purpose. So SodaStream allows us to improve the use of -- or reduce the use of plastics. Okay, to me, the way of we grow and also we help the planet. So we want to do more of those and make sure that purpose becomes integrated with the way we're going to accelerate the company. There's 4 areas where we want to make a difference: Making a sustainable agriculture; reduce the water consumption. But make actually positive water impact; creating a circular packaging economy; and then obviously, continue the improvement of our products, reducing salt, reducing fat and reducing sugar.

So those are the kind of the long-term strategies that will feed our long-term value creation. We talked on Friday about our guidance for '19. Three key numbers here. We want to grow 4%, at least 4%. We want to grow 4% as we -- and then obviously, in future years, we'll get better, we'll grow 4.5%, 5%. But this year is a 4% year. We want to invest back in our business in a way that it helps our acceleration, it helps our transformation.

We guide a minus 1% constant currency EPS. There are some factors that Hugh and Jamie talked -- took you the other day, which is we're going to have -- we'll have an increase of our tax rate of about 2 points going into next year. We're lapping some one-offs last year in terms of strategic asset sales or refranchise. Then the rest is investments in the business to make sure that we really deliver on our commitments for an accelerated growth. We're increasing our CapEx as well in a way that, especially in the next two years, we can -- this is a lot of capacity, a lot of manufacturing capacity and system capacity.

Okay. And with that, a final slide. We're convinced as a team. As I told you, it was an aligned process of the management, the whole management team. We're convinced that there -- PepsiCo is a growth company. We're very lucky of the categories where we operate. We're very good, strong in those categories. That, I think, allows us to promise that we can be a faster-growth company, a company that creates more value by being a fastest-growth company. And with that, a balanced finance performance, expanding our margins every year 20 to 30 basis points and then being a high single-digit EPS, consistent financial delivery.

With that, I think we'll take questions. So we have 20 minutes.

Questions And Answers

Q - Bryan Douglass Spillane {BIO 2147799 <GO>}

Okay. And let's start with Andrea Teixeira.

Q - Andrea Faria Teixeira {BIO 1941397 <GO>}

So Andrea Teixeira from JP Morgan. I wanted to just double click on NAB. Obviously, you've given some sort of a bridge of a recovery. And you have said that even within the fiscal '19, we should be expecting some stabilization of market share. So if you can elaborate more on how the plan that you have built into this guidance can lead us to (believe). And if you can also elaborate in terms of how much money will be invested back within NAB.

A - Ramon Luis Laguarta {BIO 18967774 <GO>}

Yes. And I will not go into specifics, obviously, for competitive reasons. But what I'd like you to take away is that we started this year already investing in NAB on a serious way. It was an A&M-focused investment against our core brands. We're seeing a good response on some of our core brands, especially Pepsi. Pepsi is growing nicely. And so we're back to growth. There are some other brands that need a bit more fuel. But the way we're investing this year is more also on go-to-market. You saw the changes we're making in our organizational structure that would allow us to be much more locally relevant and faster. So you should think of NAB as a multiple-dimension investment, both in growth but also in capabilities and in organizational executional power.

Q - Bryan Douglass Spillane {BIO 2147799 <GO>}

Bill Chappell?

Q - William Bates Chappell {BIO 1737315 <GO>}

Bill Chappell from SunTrust. Maybe if you could step back, understand the kind of 4-month process. But in your opinion, kind of how did you get there? Especially from NAB of kind of falling a little bit behind? And was this a process of you're taking over, we need to turn the page and look at everything once again? Or was it we have a real problem we need to address? And just help me kind of understand the process of how the company got to this state.

A - Ramon Luis Laguarta {BIO 18967774 <GO>}

I think it's -- I mean you've seen the performance over the last six years. It's a pretty good performance, right? But as we got together as a group, we said, "Okay. Are we happy with our performance?" And we said, after a really long -- this was, I think, how many, 4 sessions or 5 sessions of two days. We said, "I think we can aspire to more." I think we wanted to have -- as a group, we were dissatisfied with a couple of areas, which I mentioned, especially the share of market performance, not only NAB. I think there's opportunities in other markets. So we said, "No. We want to aspire to be. And we can be, a company that gains market share consistently across all the markets," and that's what we want to be.

So I wouldn't focus on NAB per se. I think as a company, you should think of we're operating beautiful categories that are on trend, that are growing 4%, that are massive globally, they're aspirational for many people around the world. They serve a lot of -- we serve a lot of needs that are unmet. So we think that we -- in those categories, we operate from positions strength in many of those markets. So why not investing?

And we went through the rigorous process of understanding opportunities and then say, "Okay, what if we first take discretionary funds that we have today in the business and we apply them to those opportunities?" Okay, yes, we can grow faster. And second, are there still opportunities that are unmet? And we said, "Yes." Then we said, "Why not? Well let's go and invest more to accelerate the business," and set for ourselves what is, I think a much more aspirational mission, which is we want to be a (growth) company. We want to be top-tier growth company. And we want to have a growth model for all of you, as investors, where we deliver balanced financial performance that focus on being a very, very good market performing company. That was the process.

It's really -- it's not a new book for PepsiCo. It's actually a new chapter for us. It's a new chapter that flows very nicely from the foundation we've created over so many years and being in categories that grow, (building) strong positions. And now it's more of a -- we know where we can invest. And we know that to maintain that acceleration, we need to transform ourselves. So that's what I'm saying. Being faster is important. And I think we can do it. But being stronger is what's going to make us faster over the long term. So our ability to transform ourselves, build real capabilities that are differentiated, look at our costs in a very aggressively and think, "Are there better ways to do things that are more efficient, effective?" That's the charcoal that is going to make us a better-performing company sustainably. So that's how I would life for you guys to think about PepsiCo in the future.

Q - Bryan Douglass Spillane {BIO 2147799 <GO>}

Okay. Ali Dibadj?

Q - Ali Dibadj {BIO 15328592 <GO>}

So in that process, in the 4, 5 meetings in the 4, five months that you went through, how did you get comfortable about the ROI to get to what sounds pretty ambitious, given what we've heard all week, the 4% to 6% in particular top line growth, the high single-digit EPS growth? And I ask that in the context of 2 things. One is the nutritious versus indulgent spectrum that you -- actually it's up there, actually that (was the) equivalent of the spectrum. So I'm not sure that nut mix is that big of a category for you. But beverages, I haven't had in a while. So I don't know how big of a category that is for you. And I think the cooler in the back is Coke products, actually, outside. So those are really small categories. And they're growing quick. So in that context, number one, how do you get to 4% to 6%? And number two is, everything that we've heard from the food companies this whole week is that they're not food companies, they're snacks companies. So I'll almost re-ask the question I asked last year at this time, which is how does that impact your view on Frito-Lay in terms of getting that same growth targets? So again, I'll just try to get to that one.

A - Hugh F. Johnston {BIO 15089105 <GO>}

Yes. A couple of things, Ali. I'd begin with the fact that we really started investing in the business kind of second half of '17 and into '18. If you recall, we talked a lot about that with North America Beverages. And we saw responsiveness to those investments, some of which was incremental investment which we funded from elsewhere in the P&L; some of which was shifting resources from products that, frankly, we launched and didn't do as well, the Lemon Lemons of the world and things like that. But it was the response that we saw to the advertising in particular that encouraged us to do more. Now truth be told, as we were investing in some of the smaller products, our competitor was investing primarily behind CSDs. And we needed to do some things there to be more competitive as well. All of this is not news, we've discussed all this in the past. So that gave us some level of confidence.

We also -- as we started to put a bit more money behind Frito-Lay, we saw remarkable responsiveness there as well. It was clear that the business could use more investment not because it was coming from a position of weakness. But rather quite the opposite, a position of strength with -- combined with more investment would result in what we felt were going to be much better outcomes for that business over time, certainly in the U.S. and then internationally as well. Our snacking position internationally, obviously, is quite large. Our market shares are quite good. The opportunity there, we've talked about in the past, is per-capita consumption development. And we do that through a combination of basically the model that Ramon showed earlier. So I think it was the -- some of the experience that we had, along with what we know are good structural and category advantages that led us to the conclusion, we think we can do this and earn a really good return for investors over time.

A - Ramon Luis Laguarta {BIO 18967774 <GO>}

Yes. And Ali, to your point on snacks and the competition there. Obviously, the fact that everybody's trying to go into snacking tells you that there's tailwinds to that category in terms of people are going to unstructured meals. And obviously, they are snacking more and more every day. So that's -- from a concept, that's, I think we all understand. We have very strong positions. So I mean it's hard to -- when you peel the layers of advantage that we have in that snack business, from the farming all the way to the execution at point of sale, the brands we have, we have pretty high chances of capturing that growth. So we want to make sure that our -- all our units are well funded, that they have the muscle to compete when those other players come into the market.

And our experience is that the more we are in the category, the more we're investing in each one in our brands, in our innovation, that drives the category. That drives more space in the store. It drives more consumer GRPs on the categories. So it's normally positive. So we're looking at this as a, first, these are good categories; second, we feel comfortable that with the right level of investment and capabilities we have, we can win in those categories; and third, we like the fact that there's multiple players developing categories. If you think about any developing market, like I don't know, Turkey or Pakistan or whatever, the per caps is less than a kilo, less than a kilo per person. If you think about our developed markets, U.K. or here or Canada, we're talking about 10 kilos-plus. Imagine the opportunity we have. And we cannot do it on ourselves. It's great to have multiple players trying to develop that category. So it's good news for us in terms of, yes, these could be high-growth territories for us. So we're ready for competing. We respect everybody. I mean we like competition, actually. If anything, sometimes our snacks people become a bit arrogant because they have 70% share in some categories. So we want our people to be motivated and be challenged and to give their best. And I think competing is a very good way for us to be a better-performing business. So that's how we're thinking about it. And I don't want to sound arrogant in a way. But I want to make sure that you guys understand that we feel good about our snacks business, our ability to capture share and to keep developing the categories.

Q - Bryan Douglass Spillane {BIO 2147799 <GO>}

We've had 2 very patient hands over here, Robert Ottenstein and Brett, please?

Q - Robert Edward Ottenstein {BIO 1498660 <GO>}

Great. So in the past, it's been challenging. And it's -- look, it's difficult to do. But it's been challenging for you to balance some focus on the brand health of the larger, more important brands. And at the same time, nurture and grow smaller, faster-growing brands. So is the answer to that just more investment in general? Because it's a little bit what I'm hearing. Or are there other things that you're doing to improve the execution? Maybe changes in the incentive system, changing in the network, in which you can do better, have a better balance doing that?

A - Ramon Luis Laguarta {BIO 18967774 <GO>}

I think it's a combination of all of them. I think the fact that we're putting more investments in the business tells you that, yes, we think that there is a more sustained way -- sustainable way to invest both in the growth of our core brands and investing in our smaller brands. The funding for those investments will come, I think, from many areas. One is repurposing money from other parts. And that's the process we did, repurposing money from the discretionary funds into a better funding model for our core and smaller brands. Second and very important, the process that I was talking about is getting stronger by really elevating cost to a much more strategic role in the way we manage the company. We will be able to generate the right amount of savings that we'll be reinvesting both in capabilities and in our brands. And I think that's how you should think about it. The third element is not irrelevant, is this one I was talking about, about a higher return on investment on our commercial investments. That is a very important piece of the improvement of the company and how, by taking trade, A&M, space management and some of the other growth drivers and making sure that we're a bit more scientific in the way we allocate money to drive growth, I think that's going to help us as well. So it is all the above. And we feel comfortable that we will have a much more balanced growth between our core and in our smaller brands going forward.

Q - Bryan Douglass Spillane {BIO 2147799 <GO>}

Okay. So Brett Cooper, then we're going to come to Judy Hong, please.

Q - Brett Young Cooper {BIO 17398526 <GO>}

Two questions. And I think it was in 2012, we went through a rebase. We've rebased today. So what gets put in place in the future to avoid that happening, whether it be 5, 6, seven years down the road? Then just wondering philosophically, how you address, like, you need more brands in a world where the consumer is more fragmented, your competitors are smaller so forth and so on?

A - Hugh F. Johnston {BIO 15089105 <GO>}

Yes. In terms of your first question, Brett, 2012 was, I think fairly different from where we are right now. In 2012, we were really re-basing, I think, from more of a position of weakness. Advertising and marketing had gotten down to about 5.2% of sales. During and perhaps just a bit after the financial crisis, the organization was pushing to make targets that were challenging in that economic and consumer environment. Contrast that with today, where the company really has been performing pretty strongly now for 5 or six years. This is much more around realizing, I think, a set of excellent opportunities that present themselves because of our categories, because of the structural advantages that we have in place and because the leadership team is highly execution-focused on both delivering financial results and consistently gaining market share, which means the revenue growth rates will be higher. That higher level of revenue growth will lead you to a sustainable level of financial performance, which should basically put us in a position where we can reinvest in the future while delivering around our long-term financial targets.

Q - Bryan Douglass Spillane {BIO 2147799 <GO>}

We have Judy, yes, please.

Q - Judy Eunjoo Hong {BIO 22723741 <GO>}

Judy Hong from Goldman Sachs. So one is just a quick clarification, Ramon, just your aspiration on market share gains in NAB. Is there a distinction in terms of focusing on gaining within a segment? So gaining share in sports drinks, CSDs versus the broader non-alcoholic ready-to-drink category? Then my broader question is just in terms of your decision to keep the North American bottling assets in-house. How much of that is because you don't want the disruption while the business is trying to improve its market share performance versus you fundamentally see an advantage of keeping that business and sort of enabling you to be faster as you kind of think about that business going forward?

A - Ramon Luis Laguarta {BIO 18967774 <GO>}

Yes. On the NAB question, I think we talked Friday. I think we believe that this is a business that we'll make great by working on 4 things, right. One is having very strong brands that are well funded and cover all these spaces. And I think that is a question of resources, innovation and marketing versus franchising, not refranchising. The second one is by, we want to make sure that we service our customers, the large national customers, with the best service possible across the country. Then we're able to cover the small up and down the street and smaller (brands) with the same level of high service and precision. And I think there, for the large customers always, I think we have an advantaged model being an integrated. And so we have one piece of innovation, we can roll it out across the whole country. We can respond to any sort of promotion. We can give better service overall. So for the large customers, there's no doubt in my mind that having an integrated model is better. For the smaller customers, what we're trying to do is, with this new organization, is make sure that we have the local servicing also better understood. So I don't think it is anything to do with the refranchising model, it's having an organization that can react to the local opportunities in a much more agile way. So that's how we're approaching it now. The third piece is having a very flexible and very efficient supply chain. And to me, our integrated model is also a way to have much, much better utilization of assets across the whole country. The fourth one has to be with culture. Has to do with culture and high-performance culture. And there, you would say, "Okay, sometimes, smaller companies act much more as owners than large companies." So it's a process of how do we, along with the organizational change, we create a culture of ownership, we create a culture of agility and quick decision making, which I think we can do. We have it in Frito, we can do it in NAB.

We have in many countries around the world. So that's how we're thinking about the success factors. Then when you say, "Okay. Are we better off in a refranchise model or an integrated model?" we say, "Listen, I think we're better off as we are." Then, again, when you add the complexity of a potential refranchising, you say, "It doesn't work at all." So that's how the thought process is right now. And we're comfortable with this decision. We're actually pretty, pretty confident. And we're seeing the market...

Q - Bryan Douglass Spillane {BIO 2147799 <GO>}

Okay. With that, please join us in thanking PepsiCo for the presentation. We'll move on to the breakout.