Good morning, and welcome to PepsiCo's First Quarter 2011 Earnings Conference Call. [Operator Instructions] Today's call is being recorded and will be archived at www.pepsico.com. It is now my pleasure to introduce Mr. Jamie Caulfield, Senior Vice President of Investor Relations. Mr. Caulfield, you may begin.

Jamie Caulfield

Thank you, operator. With me today are Indra Nooyi, PepsiCo's Chairman and CEO; and Hugh Johnston, PepsiCo's CFO. Indra will lead off today's call with a review of our overall performance and outlook, and then Hugh will cover the financials and operating results and the financial guidance in more detail. We'll then move on to Q&A, where we'll be joined by the CEOs of each of our businesses: John Compton from PepsiCo Americas Foods; Massimo d'Amore from PepsiCo Beverages Americas; Eric Foss from Pepsi Beverages Company; Zein Abdalla from PepsiCo Europe; and Saad Abdul-Latif from PepsiCo Asia, Middle East and Africa.

During today's call, unless otherwise noted, all references to net revenue growth are on a constant currency basis, and all references to division operating profit growth and EPS growth are on a core constant currency basis. I refer you to today's earnings release for more details.

Before we begin, please take note of our cautionary statements. This conference call includes forward-looking statements based on currently available information, operating plans and projections about future events and trends.

Our actual results could differ materially from those predicted in such forward-looking statements, but we undertake no obligation to update any such statements whether as a result of new information, future events or otherwise.

Please see our filings with the Securities and Exchange Commission, including our annual report on Form 10-K and subsequent reports on Form 10-Q and 8-K. And finally, you should refer to the Investors section of PepsiCo's website under the Investor Presentations tab to find disclosures and reconciliations of non-GAAP financial measures that may be used by management when discussing PepsiCo's financial results.

And now it's my pleasure to introduce Indra Nooyi.

Indra Nooyi

Thank you, Jamie, and good morning, everyone. We are quite pleased with our Q1 results. Top line growth was balanced and strong, and profitability was right on plan. We delivered organic volume growth of 3.5% in beverages. And excluding the foods volume, we delivered 4% in core salty-snacks.

We're especially encouraged by our growth in North America where core salty-snack volume growth at Frito-Lay was up 2.5%, and organic beverage volume growth was 2%. Internationally, we delivered volume and revenue growth in each of the geographies. International organic volume growth was 7% in core salty-snack and 5% in beverages. Global foods volume, which is included in our set of snacks volume report for external reporting, declined 4%, driven primarily by Quaker Foods North America while internationally, our foods volume grew 2%.

Despite inflationary pressures, we continue to invest in brand building in emerging markets, and we're beginning to see evidence that our recent investments are paying off.

Last year at about this time, we set out five key growth imperatives for PepsiCo that formed the backbone of our strategy, and I'd like to discuss this quarter's results in the context of these imperatives.

Our first imperative is to build and extend our macro snacks portfolio. Our reported worldwide snacks volume growth was 3%, and this included our foods volume also. Our underlying core salty-snacks volume grew more than 4% on an organic basis. Growth was well balanced, with strength in both developed and emerging markets. And we grew salty-snacks volume in each of our top 10 global markets.

Innovation was strong across the board, which resulted in incrementality, even in our more developed markets like North America and the United Kingdom.

In emerging markets, we're building per capita consumption and driving frequency, and that's led to strong organic growth in these markets. For example, we grow snacks volume 18% in India, 13% in China, 26% in Russia and 32% in Turkey.

Operating margins in global snacks improved about 100 basis points, with gains in almost every division. In some countries, we saw value and niche players pulse in and out of the market and take some share. We are careful not to overreact, choosing to judiciously trade off some share to protect profit in the short term. Our goal is to balance volume and profit growth. And across the world, our businesses are doing a pretty good job in this regard.

Our second imperative is to sustainably and profitably grow our beverage business worldwide. Our global organic beverage volume growth was 3.5%. CSDs grew 2% and non-carbonated beverages grew 8%. Every division grew organic volume, with emerging and developing markets continuing to show terrific results. India was up 20%, Russia was up 13%, Turkey was up 21% and China was up 4%, lapping 19% from 2010.

Developed markets also generated good growth, with North America organic volumes up 2%, and the U.K. up 7%. We hit the first anniversary of the bottler acquisitions in the first quarter, and the synergies are ahead of original estimates.

We have made the operational organization changes necessary to realize the cost synergies, and we're beginning to realize the revenue synergies now. For example, we moved small format Gatorade onto DSD at the beginning of this year, and we're beginning to make progress in growing our business at food service accounts.

We also focused on improving profitability in beverages but have to carefully address 2 issues: first, commodities are clearly a headwind; and second, we intend to continue to invest in brands and in building out our emerging markets infrastructure.

Inflation has disproportionately impacted our beverage businesses, and thus pressured our beverage margins somewhat, especially in EMEA and North America. Partially offsetting this, in North America, we achieved almost 2 points of price mix and intend to pursue higher price utilization for the remainder of the year to more fully offset the commodity cost pressures.

In EMEA, we'll also begin to see the impact of pricing actions that they're are taking as we move into the balance of the year.

I'm confident that we're making the right investments, which is being born out of the growth we're seeing, and we've got solid pricing plans in place for the year to balance volume and profit growth to deliver on our financial and operating commitments.

The third imperative we articulated is to unleash the power of Power of One. We're making good progress here. In North America, we've ramped up our Power of One activity. For example, in the first quarter, we executed cross division basketball teams merchandising in March, we accelerated local UDS account promotional activity, and we are continuing our pilots where we have Power of One merchandisers in selected large-format stores, and early results are quite promising.

And this summer, we're introducing the first ever PepsiCo coupon inserts to cross for 20 of our brands across snacks and beverages. And we continue to advance Power of One as a strategic volume and productivity driver in our international market, where Power of One is already highly developed. In this area, I believe overall, we're making progress. We believe there's a lot more potential to be realized.

Our fourth imperative is to build and expand our nutrition business, and here we are pleased with our progress so far. We are focusing our efforts in 2 areas, innovation and branding. And we're doing this to accelerate the growth of the nutrition segment of our snack and beverage portfolio. And to remind you, it's Quaker in grains, Tropicana/Naked and the many regional brands we own in fruits and vegetables, Wimm-Bill-Dann in value-added dairy and Gatorade in sports nutrition.

To do this, we took a group of about 100 R&D and marketing people and about a $50 million budget, and focused them against these segments and brands. This core group is responsible for building an innovation pipeline looking 12 to 24 months out and for maintaining the global brand architecture for our nutrition-oriented brands.

Output from this Global Nutrition Group will start to appear in store shelves sometime in 2012. However, in the first quarter of 2011, the revenue growth in the nutrition segments of our snacks and beverage portfolios outpaced the growth of our core Fun-For-You and Better-For-You businesses, giving us confidence that our focus on this opportunity is well played.

The fifth imperative is to ensure prudent, responsible financial management. In the first quarter, our financial results came in as we expected. Core division operating profit grew 5%, driven by solid volume and net revenue performance and synergies and despite inflationary pressures and continued investment spending. We had negative leverage below the operating profit line from higher year-over-year interest expense and a higher tax rate, resulting in the quarter EPS decline, again as we expected and communicated on our Q4 call.

Looking forward, commodity cost inflation will be a major factor for all companies in our sector in 2011. Through our hedging programs, we have good visibility into our cost outlook for the balance of the year. Our plans and targets have taken commodity inflation appropriately into account, and I'm confident we have the right pricing and productivity plans in place to deliver on our commitments, and Hugh will give you more detail on this.

Next, we are confident we are focused on the right five imperatives, and we're making good progress against them. But before I turn the call over to

Hugh, I want to touch on 3 topics that seem to be of interest to many of you.

First, how will we sustain performance at Frito-Lay in North America? Two, what actions are we taking to accelerate growth in North America beverages? And three, how are we thinking about capital allocation?

Let me turn to Frito-Lay North America first. As all of you know, this is a very powerful franchise with tremendous scale advantage. We saw a volume growth in the first quarter, and that translated to solid operating profit growth, with healthy gross margin expansion. As we look to the balance of the year, we expect top line growth to be driven by innovation.

We've talked a bit about the initiative around all natural, and it's off to a great start. Just as importantly, we have a strong lineup of core Fun-For-You innovation, with products like Ruffles' bold flavors, Taco and Pizza doritos and a line of Tapatio flavors, and we expect these products to do very well, especially in single-serve in the UDS channel.

We'd also drive growth and adjacencies under the Stacy's and Sabra brands, where we're expanding the lineup to new product introductions. So we expect Sabra and Stacy's to continue to drive highly incremental growth.

We'll begin to see input cost inflation in Frito as we move through the year, and we have solid pricing plans in place to cover it, supplemented by solid productivity programs.

So our expectations for Frito-Lay North America: to continue to be a steady profit growth driver.

Let me turn now to North American beverages, where our focus is on judiciously balancing volume and profit growth. We believe we are making the right kinds and appropriate level of investments to accelerate our long-term beverage growth in North America, and this includes a sizable increase in our advertising and marketing expense in Q1.

Gatorade is a great example of how we've created innovative platforms and established brand marketing programs that drive brand equity. We have the same focused on our other key beverage brands like Pepsi, Dew and Tropicana. We have seen brands score strengthened across the board. And volume trends improved, which gives us confidence that we're making the right investments.

Regarding profit growth in Pepsi Americas Beverages. Clearly commodities are a headwind, and our intention is to offset these costs with productivity and pricing. We achieved some positive price mix in the first quarter out ahead of the category, and intend to continue to employ pricing as well as mix to drive solid net price realization and profit growth.

We intend to price to cover input costs and to maintain brand support, so that we can compete in the business of innovation and brand equity.

The final topic I want to address before I hand off to Hugh is capital allocation. Clearly, the bottler acquisition and the Wimm-Bill-Dann acquisition are major commitments of capital. These transactions were carefully analyzed and considered before we committed to them. I'm confident that they are justified in their financial and strategic merits, and we are absolutely committed to delivering on these important investments.

We are now well positioned to generate strong organic growth and going forward, anticipate relatively low levels of capital investments deployed against occasional tuck-in acquisitions, alliances and joint ventures.

Our businesses will continue to generate attractive cash flow, and we'll reinvest capital in the business only when there's a clear compelling case for value creation. We have a strong record of an ongoing commitment to returning cash to shareholders through both dividends and share purchases.

With that, let me turn the call over to Hugh, and I look forward to taking your questions. Hugh?

Hugh Johnston

Great. Thanks, Indra, and good morning, everyone. I'll spend just a few minutes reviewing the financial performance before we open it up for Q&A. I know today is a busy one for many of you, with so many companies reporting, so I'll keep my comments relatively brief.

For the sake of clarity before we get to the financials, I want to call your attention to a couple of key items that affect the comparability of our results for last year. Our financials for the quarter impacted by the bottler acquisition into a much lesser extent, by our acquisition of a controlling stake in Wimm-Bill-Dann. With respect to the bottlers, we closed on the bottler acquisitions on February 26 last year. So in this year's first quarter, we have a full quarter of bottler results and net interest expense related to the transaction comparing to a short stub period of ownership in Q1 2010.

The bottler's operating profit in the first quarter is seasonally low and, as I mentioned on last quarter's call, the European operations of the bottlers historically operated at a loss in Q1. So we have 2 periods of low seasonal results in Q1, and we have 2 incremental periods of full interest expense, associated with the bottler acquisitions, which created a net negative impact for the quarter.

Regarding Wimm-Bill-Dann, given the timing of the closing on our 77% stake toward the end of the quarter, the impact of this transaction on our overall first quarter results is relatively small.

Information in the release this morning is meant to provide visibility into the fundamental performance of the business. Couple of points here. One, we've presented organic volume growth for PAB in Europe, the 2 divisions impacted by the bottler and Wimm-Bill-Dann acquisitions, which strips out the impact of the acquisitions for those divisions from our volume growth. Second, we've also provided the pro forma impact on net revenue as if the bottlers had been acquired on the first day of Q1 2010. And finally, we provided disclosures on the impact of Wimm-Bill-Dann on net revenue and operating profit growth rates.

For the first quarter, our core EPS was $0.74, which was in line with our expectations. Core EPS was driven by a 5% increase in pro forma net revenue, excluding the impact of Wimm-Bill-Dann and a 5% increase in our core division operating profit. The core division operating profit reflects solid volume gains, some net pricing, synergies from the bottler acquisitions and productivity, partially offset by higher commodity costs, continued investments in brand building and in emerging markets, and the seasonal losses associated with the operations of the acquired bottlers.

Let me highlight on a few items impacting profit performance in the quarter by each of our sectors.

PAF core operating profit results were up a strong 8%, with good operating margin expansion, led by gross margin expansion at FLNA. PAB core operating profit was up 9% with positive bottler operating profit overlap, volume, pricing and synergies, offset somewhat by inflation and continued brand investment. Europe was impacted by the inclusion of 2 months of bottler results, which historically operated at a loss as I noted earlier. Using last year's operating losses of proxy, this accounts for approximately 33 points of profit decline in Europe's Q1 results. And finally, in EMEA, core operating profit declined 6%. This is a relatively small profit quarter for EMEA, and the difference between down 6% and up double digits is about $25 million.

There were a number of factors that contributed to the decline, including investment spending, price lagging somewhat behind inflation and some temporary business interruption in the Middle East.

Commodity cost inflation is a major theme we are managing across the entirety of our business. In the first quarter, inflation impacted our beverage operations more dramatically than our snacks. We covered some but not all of the beverage commodity cost inflation with pricing.

On the snack side, commodity inflation was less pronounced, and we generally were able to cover inflation there.

Looking out over the balance of the year, commodities will continue to be a headwind. We expect inflation of approximately $1.4 billion to $1.6 billion on a base of $18 billion of commodity based inputs. As we explained on last quarter's call, our intention is to offset a portion of this inflation with pricing and productivity.

In a year as volatile as 2011, we're closely managing the pricing volume productivity equation to ensure we deliver on our financial commitments for the year. This was true in all of our divisions, but especially so in PAB. As we've said before, we intend to be a disciplined, well-run bottler. As a part of this, we seek to cover our commodity cost with pricing. Given the soft consumer environment, and as the industry goes through transition, pricing in the first half has not been what we would have liked or expected. But because of the ongoing commodity inflation pressures, as we exit the first half, we anticipate taking additional pricing in the form of rate increases on key packages. This will be necessary to drive acceptable operating profit growth, provide the room to continue to invest in innovation and marketing and to operate consistent with the principles of being a well-run bottler.

Turning to cash flow. In the quarter, we generated $78 million of management operating cash flow excluding the impacts of merger and integration payments and integration-related CapEx.

Our key working capital metrics of DII, DSO and DPO, are all within target, but year-on-year cash flow comparisons are impacted by the seasonality of the bottler cash flows.

Finally, let me update you on our earnings outlook for the year, which is consistent with what we've shared on the first quarter call. We expect core constant currency EPS growth of 7% to 8%, and estimate ForEx could be a 1 to 2 point translation benefit to our full year core EPS growth all on a 52-week basis.

Below the operating profit line, we anticipate negative leverage for the full year for the reasons we shared on the last call, namely: higher interest expense, $50 million of spending at the corporate level on our nutrition initiative, higher pension costs related to the amortization of PAS losses, and the non-controlling interest elimination related to the income of Wimm-Bill-

Dann. In addition, we expect our core tax rate to be approximately 27% for the full year essentially even with 2010.

On cash flow, we expect CapEx to be approximately $3.5 billion for the year, excluding bottler integration CapEx of about $150 million. We remain committed to returning cash to shareholders through dividends and share repurchases, and expect share repurchases of approximately $2.5 billion in 2011.

In the first quarter, we repurchased $361 million of shares. We expect the rate of repurchase to accelerate in the second half, following repayment of acquisition-related debt to achieve the full year target.

As you model out the balance of the year, please note 2 items: first, operating profit growth in the second quarter will be lower than in the second half driven by the timing of anticipated pricing actions; and second, we estimate our Q2 core tax rate will be 90 to 100 basis points above our full year estimated tax rate.

So to summarize the overall financial picture: first of our Q1 results came in line with our expectations; second, commodity inflation will be challenge for us and everyone else in our industry for the foreseeable future but we'll continue to prudently manage the business balancing volume pricing and productivity; and finally, we remain committed to our full year financial outlook

With that, Indra and I will be glad to take your questions.

Question-and-Answer Session

Operator

[Operator Instructions] Our first question is coming from Christine Farkas of Bank of America Merrill Lynch.

Christine Farkas - BofA Merrill Lynch

A couple of questions if I could. Hugh, just to clarify, the commodity exposure, the $1.4 billion to $1.6 billion, is still in line with what you've indicated in the prior quarter, yet we've seen some inflation since then. So I'm just wondering if your earlier guidance had incorporated some expected PET increased. Or why that level is still there? And then I had a question for John on Frito. I know that we have some easier comps. But I'm curious in the second quarter, how trends may have changed given higher gas prices?

Hugh Johnston

Christine, great. Let me just talk a little bit about the commodity piece. Obviously, our commodity's purchase is relatively large in complexity, $10 billion with no commodity accounting for even 10% of the total. We buy an awful lot of things. Many of them have moved up. Some have moved around and down. And as I've shared in the past, we also have a very active hedging program. The net of it is there really is no change to the overall guidance of $1.4 billion to $1.6 billion. That number will likely continue to move around inside the range a bit, because we do only cover about 80% of our commodities purchases. That's the extent to which we can hedge. But we're very comfortable with the number that we have previously communicated of $1.4 billion to $1.6 billion. So that's where we are on that. Then I'll kick it over to John for the second question.

John Compton

This is John. No, we haven't seen any material changes on higher fuel prices. As we've said in the quarter, we had 2.5% volume growth at Frito-Lay and that sequentially improved during the quarter. As Indra mentioned, we just completed the final conversion of the all natural launch, and that is just now being activated in the marketplace, and we've just recently rolled a whole line of Hispanic products underneath the Tapatio subbrand into the marketplace. So our expectation is that our volume growth will continue. We may see some channel shifting due to the higher prices, of gas prices, but we don't expect our volume growth to slow down.

Operator

Your next question comes from Dara Mohsenian of Morgan Stanley.

Dara Mohsenian - Morgan Stanley

Hugh, can you quantify how much leftover commodity costs pressure, you're expecting in 2012 if commodities stay where they are today given you're somewhat hedged this year? So what's leftover piece that's not fully captured in 2011 given the hedging?

Hugh Johnston

Yes. Dara, all I'd say at this point is in total, we had about 20% at any time in the subsequent 12 months open. In terms of the balance of this year, there are certain items that we can hedge. We won't get into the details of our quantities program. So I really just leave you with the guidance of $1.4 billion to $1.6 billion in total, and I think we're very comfortable managing within that range.

Dara Mohsenian - Morgan Stanley

Okay. And then can you also give us some sense for the level of investment in AMP in the quarter versus the prior year? You beat gross profit versus my modeling consensus, but SG&A was higher than we expected. So I'm just wondering if you can give us some granularity on the level of investment behind the business versus last year.

Hugh Johnston

Yes, Dara, from our perspective, probably the biggest investment that we talked about is the one that we've made in Global Nutrition Group, and we talked about that being $50 million for the year. In terms of the other pieces of investment, for competitive reasons, we really don't want to get into the details of what countries we're putting it in or where it's going into. We did share that we had our PAD advertising and marketing expense up meaningfully from last year, and that should give you some sense for it. The net of it is in terms of the investments that we're making, what you should know is we're managing that inside the 7% to 8% overall guidance that we've given, and we're comfortable managing our investments within that overall guidance.

Operator

Your next question comes from Bill Pecoriello of Consumer Edge Research.

William Pecoriello - Consumer Edge Research, LLC

The question on North America snack and beverage pricing, you talked a lot about balancing price mix and productivity. How are you thinking about on the Frito side, weighed out versus rate, watching the $0.99 price point in the C&G channel? And on the beverage side, are you indicating you'll take pricing before Labor Day? And you mentioned taking more mix benefit there as well?

Indra Nooyi

Eric?

John Compton

So Bill, it's John. Let me take the Frito-Lay portion first. I think going forward, you'll see us use more visual pricing and more trade promotion price point than weighed out that we've typically used in the past, and we will start to employ those in the second half of the year as we exit Q2.

Eric Foss

And Bill, it's Eric. On the beverage side again, as Hugh mentioned, what we're looking to do is to optimize really the trade-off between consumer value, volume and margins. And I think if you look at the point he made earlier around what do great bottlers do, I'd point you to a couple of success metrics that matter most. One is we are looking for price appreciation, which we demonstrated in Q3 of last year, Q4 last year, full year 2010 and again, in Q1 of this year. Second, you'd look for balance top line, which we feel very good about the 2% volume and the 2 points of pricing we got this year, about a point of that was rate and a point of that was mix. And then finally, balancing what happens share wise in the market, which again we feel good about where we are year-to-date and where we finished 2010. As we look at the go forward, it will be a combination of great mix management but we do plan to initiate more rate, and that rate will probably hit the marketplace sometime after the 4th of July.

William Pecoriello - Consumer Edge Research, LLC

And then both divisions delivered around that 2% or so volume growth as you're taking that rate balance a year. Is that a level of volume growth that you hope to maintain -- obviously, you're talking about balancing the price mix productivity but that kind of low single digit would be a picture of success for you?

Indra Nooyi

Bill, I think what we plan to do is take the pricing and manage volume and share within a corridor because we just have to make sure that we judiciously balance the two. So we've drawn up some corridors and we plan to manage our business within those corridors.

Operator

Your next question comes from John Faucher of JPMorgan.

John Faucher - JP Morgan Chase & Co

I'm going to continue to follow up on this pricing environment, which is over the last couple of days, it seems as though you guys are a little more, I don't know, blase about the pricing environment than I think we've heard from some of your competitors. So I guess I'm just wondering what you're seeing that they aren't seeing. And then, good to hear that the pricing will go up after the 4th of July. That's kind of what everyone has been saying. But will prices go up even if they do not take pricing up? Is this something where you lead, or you're going to have to see kind of what everyone does at this point?

Hugh Johnston

John, let me start on this first, and if I missed anything, John and Eric can feel free to jump in on it. I'm not sure I characterize this as blase on pricing. Obviously, in the environment we're in right now, we have to look at these things very carefully. That said, as we look at the way we manage the business, we do think the appropriate way to manage the business is as we see commodity inflation, we need to take pricing in order to cover that. And we're going to do that within corridors of volume and share that we find acceptable. And if anything, in terms of leading pricing, I'd actually argue, we have been leading pricing all along. That said, we really don't pay that much attention to competition on this stuff. As Eric has articulated in the past, and certainly John's articulated, we manage the business the way we think it needs to be managed the right way in terms of the pricing/volume dynamic. And what we're really saying is we intend to take rate increases in the back half of the year.

John Faucher - JP Morgan Chase & Co

Yes. Hugh, if I can jump in, I guess, obviously, blase was the wrong term but sort of unenthusiastic. We've heard people talk about the pricing environment being very rational and very positive, but it doesn't seem like you guys are quite that positive about it. Is that a fair statement? Particularly in beverages here.

Hugh Johnston

Yes. Here's what I'd say on that, John. We've talked about the fact that given the challenging consumer environment, we weren't going to take pricing to cover all of our inflation for the year. And in a normal year, we would expect to do that. What we're saying now is while we're still not going to take sufficient pricing to cover all of the inflation for the year. We are going to take more pricing in the balance of the year. And we think that's the right thing to do for the way that we manage the business, balancing the marketplace result with the financial result.

Eric Foss

I would just add, John, this is Eric, that we are far from blase, that we are very passionate and focused on making sure we get the right rate actions in the marketplace. And again, we took pricing post-Labor Day. We took pricing post-Super Bowl. And again, it's showing up in the numbers as you can see, as indicated by first quarter. And again, we intend to do that, as I've mentioned earlier, post-July 4. So we'll balance that against what's happening in terms of consumer value, as I said earlier, the competition in commodities, but I would tell you we are very focused and passionate about the price and specifically, rate in addition to great mix management, as we always have been.

Hugh Johnston

And John?

John Compton

At Frito-Lay, as you know, as inflation comes to the business, we will price it through. And to Bill's former question, there's multiple levers at Frito-Lay to pull. One of which is mix because, as you know, the margin differentials between potato chips and tortilla chips are very different. And so we'll use the mix, we'll use visual pricing and we'll use some trade promotion pricing, but our intent is to pass it through.

Hugh Johnston

And John, just to kind of close this topic off, I mean I mentioned in my opening comments that we're not satisfied with the pricing that we're getting. Given what we look at in terms of commodities, we think it's right to take more pricing, and that's what we're going to do.

Operator

Your next question comes from Judy Hong of Goldman Sachs.

Judy Hong - Goldman Sachs Group Inc.

Indra, I just wanted to maybe take a step back and sort of, from a big picture perspective, get your perspective on some of the puts and takes, both at the macrolevel and then at the company level today versus maybe six months ago. More specifically, we entered the year with a pretty tough consumer environment. Commodity obviously a pretty challenging situation. So from your perspective at the microlevel, what's gotten better? What's gotten worse? And then at the company level, you had a lot of initiatives to invest more into marketing and branding. Are there any categories or brands or countries that you're more pleased with and maybe some of the payoffs that you're getting from the reinvestments?

Indra Nooyi

Judy, that's a broad question. Let me try to hit the highlights. Clearly, we've come into this year with GDP in the developed markets improving some, unemployment rates coming down a bit, but then offset by the very high inflation we're seeing on commodities. So every one of these situations has a positive and a negative. The good news is that we are in the food and beverage space, and people have to eat and people have to drink. And therefore, we've become more of a staple than anything and so we get the first dibs on the consumer dollars that are going out. So that's the good news. In terms of the microenvironment, as we've said before, emerging markets continue to be very, very strong, but inflation is also very, very high in emerging markets. So we're trying to thread the needle and really figure out how much pricing we can take and still get the consumer to increase per capita consumption and frequency. And that's why even countries like EMEA, we have to think very hard about what amount of pricing we can pass through to the consumer, and the teams are working through those details. In the case of the developed markets, our categories are quite well developed in these markets. And here again, we are looking carefully by product, by package to see how we can get that additional price, some through visible pricing mix, some through price mix, some through some channel offerings. And so we're playing this game in a much more nuanced micro way to be able to get that consumer dollar in order to drive our top line and our margin performance. Do you want to add something, there?

Hugh Johnston

Yes. Just one other piece to talk a little bit about this question of commodities and pricing as well, because obviously we're getting a few questions on it. I think there maybe some questions around the aggregate level of commodity inflation relative to most CPGs, we had came out earlier, and I think with the higher level of commodity inflation than the vast majority of others. To that extend, obviously, we anticipated a lot of what's gone on in the markets over the last couple of months in terms of commodity inflation. As we talk about pricing in response to that, we're really talking about that both in the context of 2011 and starting to think ahead to 2012 as well. So as you hear us talking about our strategies for the back half of the year, we're not thinking in just calendars, but we're thinking sort of on a multi-quarter basis as to where we think we need to manage the business. That said, as Indra mentioned, we do really have to be quite nuanced about how we do pricing so that we can do so effectively. But given the aggregate level of inflation in the economy, we do think it's important for us to take pricing.

Indra Nooyi

Yes. And so Judy coming back to -- and I'm picking up where Hugh left off, this is a year where if you look across PepsiCo, we have a large portfolio. We have a natural hedge between beverages and snacks, emerging markets, developing markets, developed markets, different day parts, different cohort groups. So with this natural hedge in the portfolio, we can decide what levels to tweak in order to deliver on the financial commitments. But this is where -

- this is the time you need great execution ability and excellent management to be able to navigate through the many headwinds and tailwinds that we are facing. And I think we are blessed with an extraordinary management team. Let me talk about the investment levels. The other big lesson we've all learned is that through short-term volatility, you cannot back off investments you should be making to ensure the long-term health of the business. Branding investments, absolutely we have to make them, but we wanted to make sure we make the investments when we have the right programs, the right people, the right proposition. Just as we did for Gatorade, how we turned that business around, and now it's smoking. And so we are making the stepped-up investments, especially North American beverages and beverages globally. Our investments in the nutrition group. The nutrition categories are growing 2, 3x that of the other core Fun-for-You, Better-for-You categories. It's a gigantic opportunity, and we'd be remiss if we didn't make these investments, and we shouldn't be pulsing these investments. You've got to make sure it's steady. And so that's why we've put the investments behind on nutrition group, and made it to sealed [ph] lab so that they can come up with innovation and we can start bringing them to market, because we expect all of these will also turn around the commodity costs and the economic world that developed markets are going through will turn around. And so we intend to keep the investments going to ensure the long-term success of our company.

Operator

Your next question comes from Carlos LaBoy of Crédit Suisse.

Carlos LaBoy - Crédit Suisse AG

Indra, you've spoken of stepped-up brand marketing and marketing investment for North America and globally. Can you speak to the scope of the step-up, how it flows through the year? And can you comment on some of your thinking on the need and opportunity that encourages you to step up your brand marketing investment? Is it mostly nutrition related as you just mentioned? Is it all nutrition related or mostly nutrition related?

Indra Nooyi

Carlos, the biggest step-up in brand investments are behind our core beverages brand. And because Frito-Lay North America and all of our snacks business are getting quite a bit of brand investments already, they do increase their advertising spending. But the biggest step-up that we've planned for this year and going forward is in our core North American beverage businesses. So Massimo, do you want to talk a little bit about the nature and step out -- and we don't talk about the exact level, Carlos, that's competitively disadvantaging us, but go ahead and talk about where you're investing, Massimo.

Massimo d’Amore

As Indra said, the stepped-up investment in North American beverage, first and foremost, is on Pepsi. And as we have said, we have locked in the exclusive partnership with the X Factor property and all of that investment is incremental versus last year. From a quarter standpoint also, we were back from on Super Bowl as you know with Pepsi Max, which we did not do last year. So that's what makes a big difference for the first quarter. In terms of the other beverage brands we are supporting Sierra Mist at a higher level than we did last year. And finally, the support of Gatorade is growing proportionately with the growth of the business. And we continue to aggressively partner with the right sports properties for the long-term partnerships, especially for Gatorade and Pepsi.

Operator

Your next question comes from Kaumil Gajrawala of UBS.

Kaumil Gajrawala - UBS Investment Bank

So it looks like there's very solid volume growth at Frito, maybe not as much pricing as you had wanted but obviously, some solid margin expansion as well. Could you talk a bit about the drivers of the margin expansion, including if any of that was volume leverage?

Indra Nooyi

John?

John Compton

Of course. Kaumil, some of it is volume leverage, but we did have 2.5% volume growth that obviously helps to leverage the fixed costs. And as we've said back at the Investors Conference in March, we're ramping up our productivity levels at Frito-Lay, and that's starting to come through. We talked about automation projects that are taking place. We've talked about GES controlling now. We've talked about Lean Six Sigma all through in the organization, not just the manufacturing but all the way through the sales organization. So volume leverage, yes, and then solid productivity programs contributed to the margin expansion.

Kaumil Gajrawala - UBS Investment Bank

And if I could follow up on GES, it's been about a year since the Investor Day. I believe at that time, you had one plant. Is there any update that you could give us on that?

Hugh Johnston

We've rolled 2 additional markets. We continue to see positive results from the initial markets that we've rolled. We talked at the Investor Day about how 2012 would be a year to get the IT systems in place to further the national rollout, and that's what we're doing. We'll put in an SAP and financially, upgrade our Oracle systems and then we'll get back in 2013 to rolling GES.

Kaumil Gajrawala - UBS Investment Bank

Got it. And then if I can ask about Gatorade, I believe one of the issues in the middle part of the last decade was that it was perhaps growing too faster, maybe not growing with the right consumer. So once again growing, but it's growing quite quickly at about 20%. Is there any concerns that it's maybe growing too fast, or that it's not growing with the consumer you had intended?

Massimo d'Amore

Listen, first of all, we are really totally focused on the right target and the right location. The growth you're seeing in the first quarter is really driven by 2 factors. First, we launched the G Series in April 2010, so we are lapping a quarter where we had no G series last year. And second, a big change has been in the transfer of the go to market for small formats, for convenience and drugs, from warehouse to DSD, which has allowed us to really accelerate the growth in that channel. But if you look at the pricing data, you will see that we are really not chasing volume. We're actually very focused on the right target consumer and the right location. So we feel very confident that we are not going back to some of the issues we have had in the past.

Indra Nooyi

And Kaumil, having said that, it's important to note that long term, we're not looking for a 20% sustained growth at Gatorade. That would be crazy. So we're looking at growth in the G franchise in the sports nutrition arena, and that's why you're seeing expansion into bites. You're going to see a lot more innovation around the needs of the sports athletes from a food and beverage perspective before they get into a game location, during the game and after. And you'll see a lot of niche innovations, a lot of innovation that's going to get us more price realization. Will there be some social beverage occasion that come into G? Yes, but it's not going to be meaningful, and we're not going to chase it with trade promotions or dropping off pricing. That's the key difference today: innovation, price utilization and a lot of focus on the sports athlete. That's the way we're going with Gatorade.

Operator

Your next question comes from Caroline Levy of CLSA.

Caroline Levy - Credit Agricole Securities (USA) Inc.

I'd like to just talk a little bit about Quaker and Frito, it looks like you reclassified. And I'm just trying to get a sense of what volume growth would have been on the old measure, because it looks like the Quaker business had very weak volume but also, your margins were up a lot in Quaker, despite some top line pressures. So if you could talk a little bit about that. Are you going to reclassify last year, so that we can figure out what's the next 3 quarters look like for volumes?

Jamie Caulfield

Caroline, it's Jamie. We put out an 8-K about a month ago on that, and we restated last year -- obviously, the restatement of last year makes everything apples-to-apples with this year. It's not a big piece of the business. It was some of these snack-oriented Quaker products that go through warehouse, and it really doesn't affect the growth that you saw reported in this morning's financials. But I can take you through that if you like off-line.

Caroline Levy - Credit Agricole Securities (USA) Inc.

And the margin increase, how did you drive that under the current conditions at Quaker? And is it sustainable, really is the question?

John Compton

Carol, it's John. We had a one-time accounting benefit in Quaker in the quarter. If you were to strip that accounting benefit out, we still would have grown profits around 1% to 2% even on declining volumes. So we're trying to get the price realization back into the business. We are very focused on innovation long term to turn the business around. And the business that we've been primarily focused against, the core oatmeal business, did grow in the quarter. So that gave us some optimism going forward that, that part of the portfolio is turning. As you know, we owned Aunt Jemima, Rice-A-Roni and other businesses, that we're not as -- haven't been as focused again.

Caroline Levy - Credit Agricole Securities (USA) Inc.

So would you consider those core businesses? Or could we think about some divestitures over time in that area?

Hugh Johnston

Caroline, this is Hugh. From our perspective, they're all core businesses, and we think they're important to the aggregate of the franchise, so we don't anticipate any of that.

Caroline Levy - Credit Agricole Securities (USA) Inc.

And last question, could I just get a confirmation on price mix at Frito? With the moving parts, I'm having a hard time coming up with exactly what that was for the quarter, price mix, North America?

John Compton

Essentially, it was slightly negative because again, we didn't take pricing in the quarter. So revenue growth could have grown with pound growth. It didn't in part because of the mix. Going forward, as inflation comes to the business, obviously, as we've said, we intend to fully price that through.

Operator

Your next question comes from Ali Dibadj of Sanford Bernstein.

Ali Dibadj - Sanford C. Bernstein & Co., Inc.

A couple of questions. One is just a follow-up on price mix in particular. Historically, in the past couple of quarters, it feels like it was in general more half-and-half price mix. With the greater focus going forward on increased kind of rate pricing or list pricing, kind of sure pricing as I call it, do you expect that, I guess, the mix between price and mix to be more focused on price and mix going forward?

Hugh Johnston

Ali, this is Hugh. Obviously, business by business, dealing with price mix at a PepsiCo level is a bit of a challenge because of the complexity of it. But in general, as you think through the lines of business, I would be thinking a little bit more rate than just a straight balance between rate and mix going forward. And that's what we were indicating this morning.

Ali Dibadj - Sanford C. Bernstein & Co., Inc.

And then within mix, how much do you see it -- and again, obviously, it's different by segment, by business, but how much do you see it between kind of between channel mix versus within channel mix? So C&G, obviously on the one hand, but then within C&G from a price pack architecture perspective.

Hugh Johnston

I mean in general, it's going to be, I think, more between channels than it is within channels by package. But that's a very general statement and obviously, with a big complicated portfolio. But generally speaking, it's going to be more between channels.

Ali Dibadj - Sanford C. Bernstein & Co., Inc.

And the last question is just, if you could address kind of the concern I have been hearing for a while from investors, which is execution on a very enticing strategy, right, a strategy that I think makes sense to people. How do you philosophically incentivize folks all the way down the line about some of the more complex messages? And as you mentioned a couple of times so far in answering prior question, a complex company. So for example, Power of One, what does that actually mean to the Frito driver? What does that actually mean? How do they think about it, and how do you in fact incentivize that? As you're focused more and more on that, are you thinking about, or have you incentivized folks differently at that level? So execution of the broad umbrella, but incentivization all the way down the line is a philosophical question.

Indra Nooyi

Ali, I'm going to let John and Eric tell you exactly how they do it, but let me put it in a fairly simple way. To the driver, he's also a consumer, he needs a bag of Lays, he's thirsty, he needs to have a beverage. And so that's the simplest expression of Power of One because they live it every day. But beyond that, let me pass it to John and Eric to talk about how they actually incentivize their route salesmen.

Eric Foss

This is Eric. I think a couple of things on Power of One. Again, if you really think about what we're trying to do from the most senior levels down to the frontline is we think Power of One can do 3 things for us. It can accelerate growth; it can eliminate or enhance our selling and service advantage, particularly at the frontline which you're referencing; and it can help us reduce costs and become a more efficient operator. I think we've made a couple of moves: One, we do have an incentive structure at the senior level, where both the Frito and the beverage system is incented on a North America wide number. So that's a big change from where we've been historically. Second, we've harmonized our field structure so that the Frito-Lay structure and the beverage structure geographically are aligned. That has not been the case historically. And so I think those 2 things, plus a great example is, Sunday for the first time ever, as Indra mentioned in her comments, we will have a moments to say, "coupon drop." It is a very leverageable entity for our frontline to go build joint displays and to actually build that team selling effort at the frontline, I think, are great examples of how we're trying to implement Power of One from the most senior levels down through the frontline selling organization.

Indra Nooyi

But Eric, is it fair to say that snacks and beverages are a logical bundle, therefore, it's intuitively obvious that it should be pulled together.

Eric Foss

There's not 2 more compatible products if you look at it at the point of consumption for the consumer, so obviously, that makes it a very sellable proposition for our trade customers.

John Compton

And the only thing I would add to this is Eric and his team there had been a year now into integrating the businesses. First, he had to integrate PBG and PAF, PBG and PAS into NAB. And now as a frontline, Frito-Lay in the PBC teams coming together store-by-store activating because we're now giving them real programs to go activate. We are just beginning, I think, to realize that benefit.

Operator

Your next question comes from Mark Swartzberg of Stifel, Nicolaus.

Mark Swartzberg - Stifel, Nicolaus & Co., Inc.

I guess 2 questions. First, Indra, on the AMP, you talked in the past about Coke went through this reset period seven years ago. Is it fair to think that your reset period sort of began middle of last year and this year, or do you think it's a more extended period?

Indra Nooyi

Hugh, you want to?

Hugh Johnston

Yes, sure. Mark, it's Hugh. I think we've really been investing in that in beverages over the last couple of years. If you think back, it was really in 2008 when we started to redo the packaging. In 2009, we obviously carried that forward in a significant way and then obviously, brought the bottling organization and PepsiCo together. And then in addition to that, we've obviously been sort of working our way through the brands with Gatorade, and now we've been doing things with Tropicana and Pepsi. So I think it's fair to say, we've been doing this over the course of the last couple of years as opposed to just a year or so. And from what we see, it really is yielding results both in terms of the performance of the business from a volume standpoint, as well as from the brand equity scores, which we have seen strengthened across the vast majority of the portfolio. So I think we're a couple of years into it at this point.

Indra Nooyi

Yes. But Hugh, I think it's also safe to say that we are making these additional investments while delivering great earnings performance.

Hugh Johnston

That's correct.

Mark Swartzberg - Stifel, Nicolaus & Co., Inc.

I mean, obviously, you're going to be growing it past '11. But in terms of the notion of step functioning it, do you believe that you've step functioned it, you're done step-functioning at the end of this year?

Hugh Johnston

Yes. I think generally speaking, Mark, we're comfortable with the amount of money we have in the business, and we're comfortable that we can manage it within our guidance and within the portfolio.

Mark Swartzberg - Stifel, Nicolaus & Co., Inc.

Okay. Great. And then shifting over to the nutrition business, which is multi-geography, multi-division. Can you give us an update on how you're managing the communication, the planning on the tracking of performance for that business, which includes multiple managers in multiple regions?

Indra Nooyi

Mark, to tell you, the primacy of the P&L at Pepsico is the regions. So PAS, PAB, Europe and EMEA is the primacy of the P&L, and that's where all the execution metrics exist, and that's where they really worry about how you bring products to life in each of the channels with each of the customers. So that's the primacy of the P&L. If you look at any large multinational company, there's always a matrix. There's a regional organization and global segments, and primacy is usually with one or the other. In PepsiCo, it's for the region. But in the past, we've never had global segments that harmonized platform, harmonized brand architecture and really looked at how to leverage the power of the company. And in PepsiCo, in particular, we've remained regionally focused. We came to the realization that the Global Nutrition Group needed to be managed globally, purely from an innovation, brand architecture, platform development perspective, not from managing the day-to-day P&L. So the GNG group is responsible for helping generate top line growth and ensuring that it's top line growth with good gross margin. And then what they have is the regional representatives into GNG, where each region or big country cluster gives input to GNG on what they need for their regions so that the GNG platform development can be consistent with what the regions need. And again, this is not in 200 countries. We're focused on 15 countries, and that's what we are using as the first push to drive the GNG growth. And this sort of wiring started the day we formed GNG. And the Global Nutrition Group works with each of the sector heads in each of the regions to make sure that there's a constant dialogue between the 2 to make sure the innovation actually yields top line and bottom line results.

Operator

And our final question will be from Damian Witkowski of Gabelli.

Damian Witkowski - Gabelli & Company, Inc.

I wanted to dive into North America a little bit more, U.S. in particular, and get your thoughts on strength across different channels, not just in the first quarter but what you're seeing through today. And as the construction worker back, is it getting better in the C&G channel and such? And then even if you look at the U.S. across West Coast, East Coast in the Middle, and sort of, are you seeing a different pattern of recovery across those regions?

Indra Nooyi

John?

John Compton

Our C-store business has been improving, but remembering it's coming off of sort of a declining channel a couple of years ago, and it's rolling again. We really haven't -- the first question I think we had this morning was around the gas prices, we haven't seen any massive channel shifts so far. We really haven't seen major regional shifts. Although within markets, there are ups and downs. But in total, I don't see any major shifts taking place. Eric, have you seen any?

Eric Foss

No. I think if you look at our business, I mean and particularly in small formats, C&G, FoodService dollar, drug, all of those channels were strong in the quarter, and those are the channels that we tend to see impacted by the construction worker, et cetera. So I think our business in the small format channel, in particular, is very strong.

Damian Witkowski - Gabelli & Company, Inc.

So you're actually seeing traffic being positive in those -- in the C&G channel?

John Compton

Yes, we have seen traffic being positive.

Indra Nooyi

The net numbers we should look at is overall food and beverage in North America was up 2%, 2.5%. And within that, there's a lot of channel shifting going. Convenience stores are back in focus because people are using that to do fill-up shopping right now rather than going to a large retailer, because they don't have the money to go to large retailer and make whole purchases, they're using convenience stores to top up.

So let me just summarize our call today. Overall, we are pleased with our Q1 results because they came in line with our expectations, our top line was strong. Commodities inflation will continue to be a challenge for us and everyone in the industry for the foreseeable future, but we'll continue to prudently manage the business, balancing volume, pricing and productivity, and we remain committed to our full year financial outlook.

So with that, thank you for joining us.