Good morning and welcome to PepsiCo's Second Quarter 2015 Earnings Conference Call. Your lines have been placed on listen-only until the question-and-answer session. [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 and good morning. Joining me on the call today are Indra Nooyi, PepsiCo's Chairman and CEO; and Hugh Johnston, PepsiCo's CFO. We'll lead off the call this morning with prepared remarks, and then turn to Q&A.

As we begin the call, it's important to note the following. We will make forward-looking statements on this call. Any forward-looking statement inherently involves risks and uncertainties that could cause our actual results to differ materially from current predictions and expectations. Information on such risks can be found in today's earnings release and our most recent Form 10-K and subsequent SEC filings. In addition, we will discuss results using non-GAAP measures and you can find the GAAP to non-GAAP reconciliations on our web site under the Investors section in the Events and Presentations tab.

Beginning with the third quarter of 2015, PepsiCo will realign certain of its reportable segments as you saw in this morning's press release. And within the next 30 days, PepsiCo expects to provide reclassified summary segment reporting for 2013 and 2014 and the first two quarters of 2015 to reflect the company's new structure.

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

Indra Nooyi

Thank you, Jamie, and good morning everyone. We are very pleased with our performance in the quarter. Organic revenue grew 5.1%, with Global Snacks up 8% and Global Beverages up 2%. Core gross margin improved 115 basis points. Core constant currency operating profit grew 8% and core constant currency EPS grew 11%.

Based on the strength of the quarter, our overall first half results and our outlook for the remainder of the year, we are increasing our full year of core constant currency 2015 EPS growth outlook to 8%.

Our businesses are performing well, both in the top line and bottom line. PepsiCo America's beverages had an outstanding quarter. 3% organic revenue growth translated to 10% core currency operating profit growth.

Frito-Lay North America delivered another quarter of very strong results, with organic revenue up 3% and core constant currency operating profit up 7%. And our developing and emerging markets delivered 11% organic growth in the quarter, revenue growth, despite the ongoing volatility in many regions of the world.

Looking across some of our key D&E markets, our businesses continue to prove resilient. Turkey and Saudi Arabia achieved double digit organic revenue growth. China, Egypt and the Philippines achieved high single digit organic revenue growth and Mexico achieved mid-single digit organic revenue growth.

Now I assume you have had a chance to read the release this morning. So rather than go through the numbers in detail by segment or country, what we will do in this call and going forward is to give you an update and provide a bit more detail on each of our big initiatives to drive performance, namely innovation supported by sensible brand management, flawless execution, self-sustaining productivity, prudent capital allocation, and talent renewal in management. But today we will focus primarily on innovation and touch briefly on the others. And on future calls, we will highlight one of each of the other initiatives.

So let me begin with innovation. Our innovation success today is the result of significant investments in and changes to our innovation research and development capabilities and processes that began about eight years ago. At that time, we were in an extremely decentralized organization, operating as a loose confederation of geographic business units, with each largely driving its own development agenda and establishing their own processes. Development is focused largely on product line extension, and that structure, while effective in its time, led to less efficient use of resources with redundant projects often being undertaken in different parts of the world and suboptimal resource allocation to the most promising ideas.

As a result, much of our innovation lacked staying power. In part, this had to do with the quality of our innovation, but it also had to do with our inability to appropriately incubate innovation in the marketplace. And to address these opportunities, we undertook a major transformation to improve our R&D function and innovation capabilities. Specifically, we established global category groups charged with coordinating global innovation. This resulted in a more focused innovation agenda, a greater emphasis on development platforms, rather than product line extensions only, and more efficient allocation of development resources, as we have significantly reduced redundant efforts through better coordination.

Two, we globally adopted the proprietary Demand Moments framework, originally developed at Frito-Lay North America. The framework focuses on the triggers of consumption by examining consumer needs based on the context of the occasion. This created much stronger linkage between consumer and shopper insights in the R&D functions, and has led to our innovation being more incremental to top line growth.

Three, we implemented a common discipline-staged gear process to gain better visibility into multiyear pipeline of R&D projects, to allocate resources to the most promising ideas and new platforms, and to ensure a better balance of refresh, reframe and breakthrough innovation.

Four, to facilitate more rapid lift and shift of our more successful innovation launches from one market to another. We provided our businesses with better visibility into new products and their performance around the globe.

Five, we increased our investment in R&D starting in 2008. In fact, from 2011 to 2014 alone, our investment in R&D has increased almost 40%.

Next, more recently, we established a design capability, capped at world class design talent. Increasingly, they are involving design in the early stages of innovation, taking into account the entire purchase to consumption cycle, to create truly memorable experiences for our consumers.

And lastly, we are using reverse engineering, leveraging our learnings and developing in emerging markets, to yield the benefits of thinking more holistically about low cost design of new products, packaging and equipment, without sacrificing quality.

We are pleased with the progress we have made across all these fronts and the tangible results we see. Innovation as a percentage of total revenue reached 9% in 2014, an improvement of over 150 basis points compared to two years ago.

Three, PepsiCo products received the 2015 Nielsen Breakthrough Innovation Awards. This award recognizes the most successful and enduring new CPG products launched in the U.S. in 2013. PepsiCo was the only company to receive multiple awards this year. And over the past three years, we have introduced a number of new products that have achieved or are on pace to achieve more than $100 million each in annual retail sales, including Tostitos Cantina, Mountain Dew Kickstart, Doritos-Cheetos fun multipack mix, and Gatorade Fierce Blue Cherry and Frost Glacier Cherry.

More recently, we are successfully using premium innovation within key categories to capture more price realization, to relaunch Caleb's Kola and launched DEWshine, a craft premium soda inspired by Mountain Dew's brand roots in the backwoods of Tennessee.

We are also innovating in packaging, capitalizing on the success of our consumer engaging, Lay's Do Us A Flavor campaign. We launched Lay's Summer Days campaign, encouraging fans to create custom digital packs of Lay's potato chips, featuring photos of your favorite summer moments to share with friends and family on social media.

Adding excitement to this experience, 10,000 lucky fans will receive a real life customized bag of Lay's Classic Potato Chips, featuring the photo they digitally submitted, offering consumers personalized packaging for the first time in the brand's history.

We are also capitalizing on consumer health and wellness demand. As consumers are embracing almond milk and other plant-based proteins as an alternative to traditional dairy milk, Naked Juice has launched two new nut milks, Berry Almond Nut Milk and Peachy Almond Nut Milk. And in Quaker Foods North America, our new Quick Cook Steel Cut innovation has propelled us to the number one market position in the on-trend and growing Steel Cut Oatmeal segment by making preparation much more convenient.

Channel focus innovation is advancing our food service business. We are launching a new line of craft soft drinks called Stubborn Soda in fountain this summer. The Stubborn lineup includes unique and contemporary takes on traditional craft flavors. Flavors include Black Cherry Tarragon, Lemon Berry Acai, Agave Vanilla Cream, and Pineapple Cream. They contain no high fructose corn syrup and are made with fair trade certified cane sugar and natural flavors. And of course we have continued to refresh and reframe our key brands to maintain a high level of consumer engagement and excitement.

Now innovation has also contributed to good market share performance in the second quarter in the United States, and I believe our results are impressive. We held LRB value share, while delivering strong net price realizations. We gained value share across important subcategories, including sports drinks and ready-to-drink tea. Gatorade share of sports drinks surpassed 80%. Mountain Dew gained 40 basis points of value share within the CSD category in Q2. in fact, if you add Kickstart, DEWshine and Baja and Sangrita Blast together, it represents more than two points of CSD value share in the most recent four week period, placing our recent Mountain Dew innovation by itself as a fourth largest flavored CSD behind base Mountain Dew, Dr. Pepper and Sprite.

In Q2, we grew retail sales in measured channels in the U.S. For regular colas and Mountain Dew within CSD, for Gatorade, Lipton Tea and Naked Juice within our non-carb portfolio. And at Frito-Lay we have a value share in savory snacks, and in Quaker Foods, we gained value share in key categories, hot and ready-to-eat cereals, while expanding gross margin and stepping up advertising and marketing at the same time.

And our innovation is driving growth for our retail partners as well. In the second quarter, PepsiCo was once again the largest contributor to U.S. retail sales growth among all food and beverage manufacturers, with over $400 million of retail sales growth in all major channels. This was more than two times the next largest contributor to growth, and represented more growth than the next 14 largest manufacturers combined. Notably, North American beverages was a key driver of U.S. retail sales growth within PepsiCo, and the largest contributor to U.S. retail sales growth on a standalone basis.

Our intention is to continue to invest in innovation, build upon our already strong capability base and further sharpen our holistic innovation process to drive greater growth for our customers, create compelling products for our consumers and ultimately, increase the contribution of new products to our total revenue. So that's the story on innovation.

Turning now to execution; we have ramped up our execution focus across the value chain from seed to shelf. We have established clear consistent performance metrics to track and benchmark the effectiveness and efficiency of every one of our core value driving activities, from safety to manufacturing utilization to transport efficiency to promotional display execution.

You know, execution is a never ending journey, as there will always be an opportunity to raise the game of the below average performance, be it at manufacturing lines [ph] or DSD routes. But we are seeing solid execution and steady improvement across the enterprise, and this is translating to good market based performance and financial results.

Turning now to productivity and disciplined capital allocation. As you know, we have a goal of delivering $5 billion in productivity savings over five years from 2015 to 2019, which is approximately $1 billion per year. Our current program follows a similarly aggressive three-year $3 billion program that we successfully concluded in 2014, and overall our productivity initiatives are driving meaningful results.

Over the three years ending in 2014, despite adverse ForEx, we've realized a $1 billion of annual productivity savings, net revenue per employee is up 10% and EBIT per employee is up 9%. And since 2012, gross margins have consistently expanded. Similarly, our capital allocation discipline is yielding meaningful results. From year end 2011 to the second quarter of 2015, net CapEx as a percentage of net revenue has improved from 4.9% to 4.1% on a rolling four quarter basis, and this 80 basis point reduction equates to approximately $500 million in incremental annual free cash flow. And since 2012, through the second quarter of 2015, core net ROIC has improved by 310 basis points to 18.4% on a rolling four quarter basis.

And finally, people renewal and development; this is an area that I and the board spend a lot of time on. Our focus is twofold here; making sure we have the right leaders in place today, and that we are developing the next two generations of leadership for the company. And as all of you know, good talent management does not happen in short burst. It requires taking a long term view and very detailed analytical planning.

As a core of our people renewal and management plan, we have to focus on the 200 critical leadership roles in our company. These are the roles that are most important to our success, and that provides the greatest experiential development for our executives. For each of these roles, we have developed a pipeline that ensures that we have at least one immediate successive candidate; two people in a one to three year timeframe; and then another three people ready, four to six years out.

As a result of this process, we are deliberately developing top talent, by giving them multiple category, geography and job experiences and ensuring we have well developed succession plan.

The other priority we have is ensuring that we have the right balance of home grown talent, that we augment our talent pool from time to time, with exceptional executives that we recruit from outside the company, and I believe our plans are working. When we have had executive transitions, both planned and unplanned, they have been smooth and well coordinated. And as we look at our current leadership, you will find that executive have had very broad critical experiences within PepsiCo over many years across functions geographies and categories, people like Tom Greco, Al Carey, Sanjeev Chadha, Ramon Laguarta and Hugh Johnston. And folks that we brought into PepsiCo later in their careers to augment our skill base and stretch our thinking. People like Mehmood Khan, Laxman Narsimhan, and Tony West.

And we are grooming our next generation of leadership, by giving them critical experiences. People like Mike Spano, who runs our China operations; or Eugene Willemsen and Brian Newman, whose promotions we announced last night.

So to conclude, we are pleased with our financial performance for the first half of 2015, and with the progress we have made across our valued driving initiatives. Clearly, there are a number of macro challenges around the world, but we believe we have the right strategies and programs in place, to enable us to continue to navigate successfully through the current environment. The construction of our product and geographic portfolios enable us to continue to deliver strong results. In part, because our balanced portfolio creates a natural hedge against the global macro and political volatility that has become the new normal. And all of this bolsters our confidence in our ability to continue to achieve our financial target.

So with that, let me turn the call over to Hugh.

Hugh Johnston

Great, thank you, Indra and good morning everyone. Turning directly to guidance; as Indra mentioned, based on the strength of our first half results and our outlook for the remainder of the year, we have increased our full year core constant currency EPS growth target to 8% from 7% previously. Our other targets remain unchanged.

For the full year 2015, we continue to expect mid-single digit organic revenue growth, core operating margin expansion as organic top line growth, and productivity, should offset negative geographic mix and commodity inflation, which incorporates the impact of transaction related foreign exchange headwinds, and approximately $1 billion of productivity settings.

Below the division operating line, we continue to expect corporate costs to be lower, a core tax rate of approximately 25%, and a reduced share count. We expect foreign exchange translation to negatively impact net revenue and core earnings per share growth by approximately nine and 11 percentage points respectively, based on current market consensus rates. Our outlook for the year assumes translation of our VIM [ph] as well the results, at the SICAD rate of 12.8 bolivars per U.S. dollar. Should circumstances dictate use of a higher rate, this would also negatively impact our U.S. dollar results. Taking our 2014 core EPS of $4.63 and applying our guidance in current market consensus of foreign exchange impact, implies 2015 core EPS of approximately $4.49.

As you model up the third quarter, I'd ask you to consider the following; foreign exchange translation should have an approximate 11 point unfavorable impact on the third quarter net revenue growth and approximately 12 point unfavorable impact on third quarter core EPS growth, based on current market consensus rates. And we expect the profit decline in QFNA, as we left last year's gain on the sale of the cereal business.

Below the division Operating Profit line, net interest expense is expected to continue to increase in the third quarter versus last year, driven by higher interest rates and net debt balances, and our tax rate in the third quarter is expected to be higher than the third quarter of 2014.

From a cash flow perspective, we continue to expect full year free cash flow of more than $7 billion. We expect our capital allocation discipline to continue to drive core ROIC improvement. This is building on the steady progress we have made in ROIC, with core net ROIC up 310 basis points from 2012 to 18.4% through the second quarter of 2015 on a rolling four quarter basis. And consistent with prior outlook, we expect to return between approximately $8.5 billion and $9 billion to shareholders in 2015, through both dividends and share repurchases.

As a reminder, our previously announced 7% dividend per share increase, commenced with the June payment. Our annualized dividend is now $2.81, an approximate 60% payout ratio based on 2014 core EPS. This represents the 43rd consecutive year of annual dividend increases and our annualized dividends per share have grown at 10% compound annual rate over the past 10 years.

So to summarize; our core constant currency earnings per share outlook for 2015 has improved from our last call, and free cash flow, disciplined capital allocation and returning cash to our shareholders remain top priorities for the company.

With that operator, we will take the first question.

Question-and-Answer Session

Operator

[Operator Instructions]. Your first question comes from the line of John Faucher of JP Morgan.

John Faucher

Thanks. Good morning.

Indra Nooyi

Good morning John.

John Faucher

Good morning Indra. Two quick questions here; one, can you just give us a little bit of the rationale in terms of the merger at the Latin American Food and Beverage businesses? I just sort of -- the regions -- need to manage the regions? And then secondly, can you talk a little bit about the Frito volume, which was a little bit light relative to trends? Anything in particular going on there? Thanks.

Indra Nooyi

Let me talk a bit about the Latin American merger. We have seen success in Europe and AMEA with all of the power of one management of those regions. We are able to get more productivity takeout costs, and especially with volatile economies, we have to get more and more agile and more creative about how to take out costs. And its not just costs within our system, John; I think even with our bottling partners, there is an opportunity to cooperate and figure out how not to duplicate efforts between the two companies. And we are seeing those initiatives pay off in AMEA and Europe, and we decided now is the time to do it in Latin America.

We are in the middle of a major productivity program in Latin American Foods, and integrating Latin American beverages with foods, gives us that much more of a cost base to work with.

Lastly, given the volatility of those economies there, I think it's very important to really become a lean mean machine there, in order to take the sales and reinvest it to grow the top line. So that's Latin America.

Second is on the Frito volume. Again, we watched the Frito performance very carefully as does Tom Greco and the Frito team. In our potato chip business, we were going through a revenue management program, and that revenue management program is actually yielding good revenue growth, and improving topline growth and profitability for our retailers. And one of the results of the revenue management program is that, it is going to impact volume, because the price-backed [ph] architecture shifts some of the volume to certain bag sizes, which impacts volume in the short term. But over the long term, it’s the right thing for the business. So I'd let it play out through the balance of the year, then look at our results in 2016.

Operator

Our next question comes from the line of Bryan Spillane of Bank of America.

Bryan Spillane

Hi, good morning everyone.

Indra Nooyi

Good morning Bryan.

Bryan Spillane

Just two quick ones; first, in terms of exchange rate, Hugh, you mentioned Venezuela; and if you were to move to the SIMADI rate, what would the impact for that be on the year, and how will that affect the guidance that you have given for currencies?

Indra Nooyi

I mean, Hugh is going to take that.

Hugh Johnston

Yeah. Happy to do that, Bryan. As you all know, we have provided pretty extensive disclosures in our 10-Qs and 10-K on the question. In the Q that we intend to file after today's market close and consistent with past Qs, you will see that Venezuela represents approximately 2% of our revenue and operating profit. We also have net monetary assets of approximately $335 million, and non-monetary assets of approximately $725 million.

Now, if we were to take all of that and go to SIMADI, Venezuela would then represent 0% or very slightly above 0% of our revenue and operating profits. So it's roughly a 2% hit on both revenue and operating profit. We have a charge of approximately $325 million related to the net monetary assets. It will also likely lead to an impairment of our non-monetary assets.

Now the one thing for investors to consider on this is, from an economic standpoint, this really would not represent a big impact on PepsiCo, given that Venezuela is largely a self-sufficient, self-funding operation. We are not putting any capital to speak of in the country, and we have not been able to redeploy any of our Venezuela cash outside of Venezuela. So from the perspective of cash flow and cash management, it would not have a meaningful impact on cash returns.

Bryan Spillane

So that 2% effect on operating income though would be above and beyond the guidance that you have given this morning, in terms of the 11% currency hit to EPS for the year, is that right?

Hugh Johnston

That's correct. Right now, what we are assuming for the balance of year on Venezuela is 12.8, because that was the recent SICAD option, which was a pretty robust option. But if we did make the move to SIMADI, the impact would be that much more significant.

Bryan Spillane

Okay. And then just one other question I guess, thinking about the back half of the year. Just seems like, the first half has come in better than expected, and with organic sales at mid-single digits, it seems like there has just been a better operating leverage here, or again, the currency neutral operating profit has been better. So in the second half, why -- just some higher level thoughts in terms of why that doesn't continue in the second half? Is there something you are seeing on the commodity cost front? Is the flow of productivity savings? Just something that sort of raises that flag for the back half of the year, that you won't continue to kind of see the current growth? Thank you.

Hugh Johnston

I think there is three things I'd remind you of in that regard, Bryan. Number one, the back half lapse, particularly Q4 -- both Q3 and Q4 are more challenging than the first half overlap. So we are certainly facing more of an uphill for growth in the back half of the growth. Number two, you are correct, commodities are more of a headwind in the back half of the year than they were in the first half of the year. And number three, again recall, certainly based on what we are seeing in the news these days, the world remains a very volatile place. We have big businesses in the Middle East; we have big businesses in Russia. And as we model things out, we obviously try to ensure that we give investors appropriate guidance, at least incorporating some of that volatility. So we are not assuming the perfect sunny day going forward as well.

So that's what goes into our thinking, as you look at the so-called squeeze chart between the first half and the second half of the year.

Operator

Your next question comes from the line of Bill Schmitz of Deutsche Bank.

Bill Schmitz

Hi, good morning.

Indra Nooyi

Good morning.

Bill Schmitz

Couple of questions. The first one is, is there a price war going on in snacks, especially in the U.K.? because I look at some of the market share trends, it seems like the categories are in a lot of pressure, and Pringles and Kelloggs are getting pretty aggressive. I know it's not a huge business, but I just wonder, how far that travels across Europe, and what the competitive response has been? And I have a follow-up.

Indra Nooyi

I wouldn't call it a price war. I just think that the retail environment in the U.K. remains interesting. There is -- the high street retailers are going through their own set of challenges. You have got the entry of the discounters. All of that is closing. The entire competitive situation in the U.K. to be reset. And being one of the major food and beverage companies in the U.K. and the largest salty snack company in the U.K., I think we have to be careful how we make our transition with the high street retailers and the discounters.

And so in the short term, we did lose some share. But we have plans in place to recover that share and somehow navigate through these retail environment changes. Again Bill, I tell you, around the world, as we see major changes in the retail environment, always in the short term, there will be some dislocation, because we have to make changes in the business model very-very carefully.

Operator

Your next question comes from the line of Bill Marshall of Barclays.

Bill Marshall

Hey, good morning.

Indra Nooyi

Good morning.

Bill Marshall

I am just curious. So the syndicated data in June across a lot of categories looked a little tough. I think most have come to the conclusion that may be that was a little bit weather related. I am curious, if you could update us on what you are seeing in the market, and then specifically if you had any comments, kind of into the July 4th Holiday, how both of your beverage and snacks portfolio as we are doing on a volume and price perspective?

Indra Nooyi

I think from our perspective, our numbers look fine. I mean, we have got good price utilization. There were some weather related issues in some parts of the country. But I think overall, we are feeling pretty good about our results.

Hugh Johnston

Absolutely Bill. To some degree, I think there is some bifurcation between what's happening in the center of the store, and what's happening on the perimeter. But from the perspective of the categories we participate in, with the exception of center of the store, where we saw Quaker category slow down a little bit; most of our categories are robust and saw pretty good growth across the quarter.

Operator

Your next question comes from the line of Kevin Grundy of Jefferies.

Kevin Grundy

Hey, good morning.

Indra Nooyi

Good morning Kevin.

Kevin Grundy

So two quick ones for you. First with respect to North American carbonated soft drinks and broadly in the industry. And given the recent pricing discipline which has taken hold, my question is, given this dynamic, how materially does this change your view, with respect to North American carbonated soft drink profit pool, and do you see mid-single digit growth now, as sort of more sustainable here looking out, not just this year, but longer term? And then as sort of a follow-up speaking with North American beverages, can you give us an update Indra, on Diet Pepsi and the change to the formulation there your competitors are not following? And how you're thinking about that, how you're defining success there with that product? Thank you.

Indra Nooyi

In terms of the North American CSD pricing -- look, we have been talking about disciplined pricing for a long time; I'd say couple of years. I am glad that there is disciplined pricing in the marketplace right now. And there is lot more innovations in the market basically from our end. And look, we are going to keep playing our game; we are going to focus on disciplined pricing, good revenue management, put CSD innovation out in the marketplace. And ultimately, it depends on the competitive situation, what the profit pool is in this whole CSD business, or the North American beverage business in totality. But we believe this is the right way to participate and play in this very-very important and large segment.

In terms of Diet Pepsi; big business. And I think for some reason which we cannot really explain, as with the Enchilada [ph] flavor with some consumers. And from our perspective, we just want to make sure we have an offering for all of the consumers who want to switch out of aspartame. And we have formulated a very-very good product, which is aspartame free, and will be available in the market starting in late August. So for all of those consumers who are looking for an alternative, to an aspartame sweetened diet product, we will have a product. And for those consumers, who still love Diet Pepsi with aspartame, we will figure out how to make it available online. So I think, this is a consumer driven strategy to offer all of the Diet lovers, a diet cola that's aspartame free.

Operator

Your next question comes from the line of Rob Ottenstein of Evercore.

Rob Ottenstein

Great. Thank you very much.

Indra Nooyi

Good morning.

Rob Ottenstein

Very impressive introductions on the innovation front and progress there. So wondering if you could give us a little bit more granularity on the impact to the topline, both in terms of volume and price mix that you're getting from innovation?

Indra Nooyi

I'd say that, innovation has allowed us to get lot more price mix -- pricing realization in particular. Something that's very-very important in today's environment. And its -- product packaging process innovation, but we are also spending a lot of time on revenue management. I mean, really thinking through portion sizes, pack sizes, and I think this combination of interesting products coming to the marketplace and interesting packages in interesting combinations of packages, it's what's resulting in incrementality on the revenue side and actually resulting in higher profit flowthrough. And we are seeing it across carbonated soft drinks, I mean, whether its DEWshine or Baja Blast or any of those products, and we are seeing it even in Europe and Russia and Latin America and AMEA, where I'd say, creative revenue management tactics, coupled with innovation that cuts through the clutter is resulting in flow-through to the bottom line.

Again, I think in these environments, the focus should be on revenue and profit, not necessarily on volume growth. We focus more on unit growth, revenue and profit in these environments, because a change for volume, results in the whole business hurting. So I think the revenue management unit growth, value growth, and profit is what we focus on, and that's what our innovation efforts are yielding today, the almost 10%, I think the high 9s are innovation performances. Something that is a significant step-up, and we keep watching that metric very-very carefully.

Operator

Your next question comes from the line of Caroline Levy of CLSA.

Caroline Levy

Good morning. Thank you.

Indra Nooyi

Good morning Caroline.

Caroline Levy

Good morning Indra. Question on the -- it is actually talk of Russia putting an advertising ban I guess on sugar drinks and fatty foods and things like that. And in the context of that, I am just wondering, if you see increased regulatory risk to your food or beverage business around the globe, and what you think the impact might be, for example, in Russia, and how you would handle that?

Indra Nooyi

Caroline, we were among the first people to recognize this risk, and we have been retooling our portfolio, to make sure that, first of all we have a diverse portfolio that can weather any sort of action on any part of our portfolio. But we are also in constructive conversations with governments, to make sure there aren't any discriminatory taxes or discriminatory action on any of our categories.

Having said that, on Russia in particular, it is perhaps the most diverse portfolio of any part of our company between berry and juices and ranks ranging from fun-for-you to good-for-you, and beverages. This is actually a small portion of our business in Russia. And so if you want to use an example of the most diverse portfolio of doing fun-for-you, better-for-you and good-for-you is skewing towards good-for-you, I think it's our Russia portfolio.

So we feel good about Russia so far, and we all wish there weren't any geopolitical issues to deal with from a Russian perspective, but our business is doing well, and the economy has been good to us, and the Russian business environment has been good for us. So we like it.

Operator

Your next question comes from the line of Mark Swartzberg of Stifel.

Mark Swartzberg

Morning Indra, Morning Hugh. I was wondering if we could talk a little bit more about procurement specifically in that larger $5 billion productivity aim. Can you give us a bit of an update on -- to what extent that number is included in the $5 billion and how you're leveraging your global scale. And whether if at all, these changes in the reporting structure, particularly Latin America, have any influence on how you go after procurement savings of the global entity?

Indra Nooyi

Hugh, go ahead.

Hugh Johnston

Yeah, I am happy to take that one Mark. The entity question is actually quite straightforward. We don't include procurement savings as a part of productivity. Productivity is focused on the operating cost structure, not on the commodity and procurement cost structure. The way we report procurement savings is, we share with you all a net commodity inflation number, so that includes gross commodity inflation, less whatever we can do in terms of managing, what we call value engineering, so managing our commodities to a lower cost through more efficient packaging, trading different types of juices, and things like that. So the $5 billion number does not include any savings from procurement at all. That's all captured in net commodity inflation.

Operator

Your next question comes from the line of Steve Powers of UBS.

Steve Powers

Yes hi, good morning. I was actually hoping you could just talk us through personnel and segmentation decisions that you announced alongside today's results. Obviously, congrats to you Hugh, but could you maybe also provide a little more color on the other people movements that were highlighted, and then also a bit broader window into your thinking on the resegmentation? I think it makes sense to bring Latin America in line with Europe and Asia, as you have mentioned, an increased visibility into North American beverages is welcome, at least from my perspective. But I love your broader perspective on it as well. Thanks.

Indra Nooyi

Steve, I will tell you, one of the things we did some time ago, is really sit back from the world and say, how should we think about groups of countries and clusters of operations that make sense? And based on all the work we did, basically the world broke out into eight clusters\; North America is cluster one, Western Europe is the next developed market with cluster two; three was Latin America; four was Russia and East Europe; five is Middle East and North Africa; cluster six was the Indian subcontinent; seven was China and the whole Pacific Rim; and cluster 8 was Sub-Sahara Africa. So those were the eight clusters.

And North America is so big, that grouping it together and not providing visibility into the pieces didn't make sense. So we have kept North America separate in terms of North American beverages and Frito-Lay and Quaker being so different. But all other clusters, we just cleaned it up. Cluster three is Latin America, we put it together, and Sub-Sahara Africa, we had the snacks business of South Africa and Simba reporting into Europe, and beverages reporting to our Asia and Middle East sector, we just cleaned it up.

So the segment changes that we reported, were a clean-up of these clusters, so that we can think of cluster strategies. So that's the first one, and more and more strategic thinking and designs of the future are based on how do we establish and grow our positions in each of these clusters. And more importantly, how do we get more productive working across our partners within each of the clusters. That's what we have been focused on. So the last two got cleaned up.

In terms of personnel changes, as I talked to you earlier in my strips, talent management is something that the board and I are focused on a lot. I mean, our phenomenal board, spends a lot of time thinking through succession for the top couple of hundred jobs. And one of the things we always looked at is, where is that bright talent across the company that should be lifted up, so that they can be part of a succession process in the company. And every time we get an opportunity, we figure out ways to lift them up, in order to stretch people, in order to really build exciting talent for the future, and that's what the most recent changes enabled us to do.

And just to give you an idea, let me start with Brian Newman, and I have worked with Brian now for 20 years, off and on. Brian started in corporate strategy, but then went to China, he went to Russia, he went to Spain, worked in European headquarters. Went to Canada, was the Treasurer of the Pepsi Bottling Group, and both Hugh and I have been mentoring him now for 20 years, Hugh? And now giving him this job with operations coupled with corporate strategy, allows him to get a whole perspective of the company across snacks and beverages, even though he has worked in it for a while. And here is a person that speaks Mandarin Chinese, speaks multiple other languages, and just a very great executive to lift up. And we are looking for opportunities to do that, and with the departure of Anderson, gave us that opportunity.

And Eugene likewise, he has been running the key partnership, but again a Dutch national who has worked in multiple countries, and truly global executive. Travels, 60%, 70% of his time in every part of the world. I remember, when he was running Turkey, he started to learn Turkish. Everywhere he goes, he becomes a national. And again a very exciting executive; and you will all get a chance to see these people in action, as we move along. And all of the people we are elevating, whether it's Laxman who is now going to be running Latin America. Ramon has got additional responsibilities in Europe. Sanjeev was running a gigantic geography. You will see all of them over the next few quarters. And of course you all know Al Carey and Tom Greco and Hugh very-very well.

So I think that you will find that, what PepsiCo is doing is, just reinforcing the fact that they are a talent academy. And any company that's looking for talent always relates PepsiCo. So we have to constantly make sure that our best and brightest move up, and we keep them engaged and excited about the company. And that's my job, and the job of the board, and that's what we are doing.

Operator

Your next question comes from the line of Judy Hong of Goldman Sachs.

Judy Hong

Thank you. Good morning.

Indra Nooyi

Good morning Judy.

Judy Hong

So I had two questions. One, Indra, its just really more of a longer term kind of strategy questions as you think about your global snack business. You obviously have a very good business there, but in a world where skill is becoming increasingly important and you have got other macro-snacking categories that perhaps you may not be participating as actively, how do you think about accelerating really top line, as well as the profit growth, as you think about the global snack platform? It's really looking at integrated beverage and snack nationally is the answer, or can you really do something more with the platform?

And then second question is, just really talking about your global e-commerce effort. It's not an easy opportunity for CPG companies, so can you just give us some perspectives on what efforts you have made already, and what are some of the opportunities as you think about over the next few years?

Indra Nooyi

Sure Judy. Interesting question, because I think in global snacks, we are in an interesting position; because our base is savory snacks, and we are a very-very strong player in savory snacks.

First of all globally, we still have a lot of growth within savory snacks. We came from a salty crisp snack background, and we are expanding more and more into other savory snacks, be it crackers, be it nuts and seeds, we are expanding into those areas, there is lot of opportunity there. I see growth in global snacks along two dimensions. Dimension one is, a compliment to our snack, and that's what made us go into dips, because many of our snacks are consumed by themselves. Other times, your snacks serve as sort of a substrate upon which you can put on meal like products like our Sabra hummus or our Tostitos dips. So that's one vector to grow, and we still haven't scratched the surface, and we have got lots of growth.

The other area is taking away eating occasions from other macro-snacks category. Its interesting, unlike beverages, in the case of snacks, we can go off and take eating occasions from other macro-snacks, be it cookies, or confectionery or chocolate. And our goal is to focus on what we are doing, but looking at our signs of demand spaces, which I talked about briefly, look at each eating occasion by cohort group, and figure out, how we can leverage our salty snack platform, to go after other macro snacks, be it -- replace it with a salty occasion, or do some sort of a salty-sweet combination, for example Stacy's with cinnamon sugar. It's based on a pita chip, but it's certainly sweet when you taste it, and has a much better mouth feel and experience, than if you eat something totally sweet by itself. At least, that's my perspective.

So I think that, our growth is all about growing the core and then leveraging all of the other eating occasions, taking share away from other macro snacks, and other savory snacks.

In addition, I think it's leveraging the beverage occasion to really figure out how to go into all retail outlets that beverages are in already; because beverages retail outlet, our penetration is much higher than snacks. And so if you leverage that retail base, it gives you lot more opportunities for growth.

And internationally, we are leveraging in-store promotional displays a lot more. I mean, I was in the Middle East a few months ago, and I was just amazed to see the in-store display of Lay's and Pepsi; and again, with the shares of Pepsi that we have there, it is really a powerful in-store promotion that results in tremendous lifts. So the opportunities for growth, by itself and in combination with beverages, are pretty significant.

So with that, let me turn to Hugh to talk about global e-commerce, because he is the leader of the global e-commerce activity. Hugh?

Hugh Johnston

Okay. Thank you, Indra. I mean, global e-commerce to talk about in two minutes, is a bit of a challenge to say the least. I guess, I'd make just a couple of quick comments to start the dialog on that.

Number one, global e-commerce can mean so many things, anywhere from just changing the way the product is ordered and picked, the so-called click-and-collect model, where people order online and then go pick up products at their local retail outlet, all the way through to in China, where the product is delivered significantly to door and in more and more proportions of the overall spend. Clearly, one of the leading areas, to the U.K., where you see retailers also doing a lot more delivery to the store, all the way through to new emerging players like the Blue Aprons of the world, who are actually sort of designing meal solutions, in effect filling demand moments for consumers by giving them an entire pre-packaged meal, which you see in some urban markets in the U.S. and starting to expand outside the U.S. as well.

From the perspective of PepsiCo, we are looking at it two ways. Number one is, the existing products going through the existing channels, either current retailers or the traditional online retailers. And then second really, looking hard at demand moments and designing products that fit the e-commerce types of distribution channels and e-commerce types of consumers in a more tailored way. So that's sort of a very brief view towards what's happening in the e-commerce world. The biggest opportunity obviously is to be able to have more of a one-on-one relationship with those consumers than we have ever had in the past, through traditional linear TV advertising.

I expect you will see a lot more from us in this regard, but that's probably the best two minutes that I can give in terms of what it is that we are doing right now.

Operator

Your next question comes from the line of Ali Dibadj of Bernstein.

Ali Dibadj

Hey guys.

Indra Nooyi

Hey Ali.

Ali Dibadj

Hi. Wanted a thought on volume versus price question that we heard about FLNA about, but wanted to hear more about Europe, and what really was driving that and if we are seeing any end in sight in terms of slower volumes there is the first question, in Europe specifically? And then the second one is, if you could help us, I guess, give some quantification for the buckets where the remaining cost cutting will be coming from? What the buckets are, how much? And if we were to talk to your employees at this point, would we hear any concerns that you are cutting too deeply into the organization from a cost perspective?

Indra Nooyi

Let me take the first one Ali. The thing I'd tell you is, Europe is a difficult economy, between east and the west, there is some sort of volatility there all the time. I think today, year-to-date, we are the best performing European CPG company, based on all the numbers we have looked at. If you combine east and west, or whether you look at them individually, both on the top line and the profit performance, we are performing the best.

The challenge in Europe is, especially with Russia there, the high street battle in U.K. going on, I think it's very important, we play a very judicious game between revenue and profits. And we have been playing that game very-very carefully, and if you look at our year-to-date numbers, I won't look at it on a quarterly basis, I'd look at it on a year-to-date basis. I think on a year-to-date basis, we are performing at or above our expectations in Europe, and we feel comfortable with what the team is doing, and that's what we intend to keep doing for the balance of the year.

And in terms of cost cutting opportunity, Hugh well you can talk about what other opportunities exist, but in terms of employees, look nobody likes cost cutting, everybody likes growth. I think we are one of those companies that are doing a wonderful balance of growing the top line and delivering productivity, and that's what we want to focus on. Swinging the pendulum too much to cost cutting, I don't think is a good idea at all, because it just jeopardizes the future of the company. So we look at opportunities to shrink the cost base and get more lean and mean, but without sacrificing our ability to innovate and grow; and that's really all I have to [indiscernible]. Do you want to add anything Hugh?

Hugh Johnston

No. I think you captured it well. The areas for cost cutting I think remain inside the manufacturing facilities, we are using automation where it makes more sense. Inside of the selling system, we are using technology to make our [indiscernible] system more productive, and inside of the G&A buckets, we are doing more combinations of shared services to create more efficiency in the way we delivered shared services to the organization. And Indra, to reiterate what you said, which is finding the right balance of driving productivity, reinvesting some in growth, and delivering some to the bottom line, is yielding results at brand building and innovation and taking some of that growth. Investing it back and driving more productivity and delivering some of that to the bottom line, is working well. I think we are in the sweet spot right now in terms of being able to deliver performance and it is a careful balance to manage.

Operator

We have time for one more question. Your final question comes from the line of Nik Modi of RBC Capital Markets.

Nik Modi

Yes, good morning everyone and congrats Hugh. I guess the question is on cost savings, so clearly you have this $1 billion three year program over the next few years. But every meeting I go in with an investor or an industry conference, the word zero based budgeting comes up or the terms of a zero-based budgeting comes up. So I just wanted to get your perspective on that particular cost saving initiatives and if you're thinking about zero base budgeting at all within the business, in addition to the $1 billion program?

Indra Nooyi

We look at every opportunity to tighten our belts and become more efficient. As I said earlier, and as Hugh reiterated Nick, we are balancing top line and bottom line growth very-very judiciously. When you embark on a zero base budgeting program that costs to the bone, and jeopardizes your ability to grow the top line. I think that's a formula for disaster.

We believe into the smart spending initiatives where we look across all of our cost structure, and see where we can selectively reduce costs, intelligently, not for the short term, but find a way to make sure it does not affect top line growth initiatives. So rest assured, that we look at every possible way to make our company more efficient, and I think we are -- as Hugh said, in the sweet spot of balancing investments against top line growth, and figuring out ways through automation, shared services, taking out work that's not needed, simplifying our processes, coordinating across the company, reducing our cost. And that's what we are focused on.

And with that, let me reiterate that we are pleased with our results for the first half. We are confident that our plans are working and believe we are on the track to deliver our financial targets for 2015. I want to thank you all for your time and questions this morning, and more importantly for the confidence you have placed in us. Have a wonderful day.