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PepsiCo, Inc. (PEP)

Q4 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

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

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

Ravi Pamnani

Senior Vice President, Investor Relations, PepsiCo, Inc.

Thank you, operator. Good morning, everyone. I hope everyone has had a chance this morning to review our press release and prepared remarks, both of which are available on our website. Before we begin, please take note of our cautionary statement. We may make forward-looking statements on today's call, including about our business plans, guidance and outlook. Forward-looking statements inherently involve risks and uncertainties and only reflect our view as of today, February 9, 2024; and we are under no obligation to update.

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

As a reminder, our reported fourth quarter and fiscal year 2022 financial results included one extra reporting week for our North America businesses. Our reported fourth quarter and fiscal year 2023 financial results in North America reflect the impacts associated with one less reporting week versus when compared to the prior year.

Joining me today are PepsiCo's Chairman and CEO, Ramon Laguarta; and PepsiCo's Executive Vice President and CFO, Jamie Caulfield. We ask that you please limit yourself to one question.

With that, operator, I'll turn it over for the first question.

QUESTION AND ANSWER SECTION

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

Bryan D. Spillane
Analyst, BofA Securities
Q

Thanks, operator. Good morning, everybody. Jamie, I'm not sure who's more surprised we're seeing each other again? Me or you? But, welcome back.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.
A

It's great to talk to you again, Bryan.

Bryan D. Spillane
Analyst, BofA Securities
Q

So I have a question, I guess, just in – we fielded a few questions today about the organic sales growth guidance for the year. And maybe if you can help dimensionalize not just the reduction, but how much is, recall, things that are sort of external, how much are things that are under your control? And maybe you can think about, as we think the balance of that, just how much of improvement are you expecting maybe in North America versus international? Just trying to understand the moving parts of how we get to the organic sales guide for the year.

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

Great. Good morning, Bryan. This is Ramon. Listen, let me step back for a minute and talk about the last few years and then how next year fits into that. So, the last three years we've seen a double-digit growth, top line in the business consistently. So I think it's at 11% CAGR and a 14% or double-digit EPS growth consistently as well. So, three very good years. Now, we see – in 2024, we see normalization of the categories, normalization of the cost, normalization of inflation. So we see everything trending back to our long-term algorithm.

Now, we guided to upper end of the both top line and bottom line at the previous earnings call. We maintained the top line at the upper end for the EPS and we moved back to at least four for the top line; and there's a few factors that I think are material. One is the Quaker Recall. We had a food safety incident in our Quaker supply chain in the US, which has impacted us in November-December; and it will continue to impact us, I think, at least for the first half of the year until we recover our supply chain to normality.

We're also seeing some geopolitical events around the world that are impacting some of our markets, which might potentially continue in the first half of next year. And then the third element is, we're seeing a bit of a slowdown in the US, both the food category and the beverage category in the Q4. Part of that is a slowdown due to pricing and disposable income situation. Part of that is also pivoting between in-home consumption and away-from-home consumption that we're seeing in our business in the US. We think that that might continue in next year, so that's why we're lowering our guidance.

We feel good about the consumer in 2024 in the US. We feel good in the sense of very low unemployment. We feel good about the fact that we think wages will go higher than inflation next year. And we hope that, by the summer interest rates will go down and that will create another source of oxygen for disposable income in households. So, we feel good about the consumer in the US. But if you think about those three elements, we decided to have at least 4% as the guidance for the top line.

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

Lauren R. Lieberman
Analyst, Barclays Capital, Inc.

Q

Great. Thanks. Good morning. Just kind of continuing on that thread, perhaps Ramon, but focusing more on Frito. So, track channel data hasn't looked great. The reported volume decline sort of bigger than what we've seen in some times for this business. But when I look on the multiyear stack, things look kind of steadier sequentially when I look at the second half.

So just curious, how much of maybe these near-term results on Frito and looking into the beginning of the year is more – is multiyear comps? Is it the consumer backdrop, the impact of pricing? But just thinking a little bit about your expectations for and plans, I guess, for driving greater unit versus volume growth in 2024, thinking about those two pieces?

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

A

Yeah. Great, Lauren. I think it's a great question. Just to summarize. We're seeing the Frito business going back to profitable volume growth in 2024. So, that's how we're thinking about the business. If you think about the slowdown in Q4 and you link it to the elements that I was referring to, there is a unit versus volume dynamic in the Frito business that is quite relevant. As you see, consumption moving from in-home to away-from-home, the portion size is meaningfully different. So, we're seeing growth in convenience stores. We're seeing growth in away-from-home in like 2 to 3 times the retail growth, but obviously has an implication on volume.

As we look at the 2024, we have a very strong commercial plan for Frito. We have our core brands very well invested. You saw that in 2023, we increased our A&M meaningfully. We're planning to do that as well in 2024. So, Lay's has a big increase in A&M. Doritos has a big increase in A&M. All our permissible portfolio, which – if you think about a combination of SunChips, PopCorners, the whole Simply line, Smartfoods, that part of the portfolio is growing almost 3 times the average of Frito.

So, we're putting a lot of emphasis on that particular part of the portfolio, to make sure that it is well-executed in the store. And now that supply chain is back to 100%, we're going to push that part of the portfolio even more aggressively. So, we think that Frito will have a continuation of the share of market gains that it's been having for the last couple of years, and we expect the category will rebound as well.

Part of that because of what we'll do with our brands which obviously have a lot of weight in the overall category, but also the fact that we think consumers will continue to feel better throughout the year and that will recover the Frito-Lay top line with a more balanced profitable volume growth and pricing versus what we've seen this year.

Operator: Thank you. One moment for our next question. The next question comes from Bonnie Herzog with Goldman Sachs. Your line is open.

Bonnie Herzog
Analyst, Goldman Sachs & Co. LLC

Q

All right. Thank you so much, [ph] everyone (00:09:38). I guess, I had a question on PBNA profitability. I believe you still have a goal to reach the mid-teen operating margin levels. But so far, we really haven't seen much progress. So, Ramon, I guess, hoping you could touch on your plans to achieve this, and then maybe whether you're considering making bigger structural changes to your business, such as possible re-franchising of your bottling network?

I know you've mentioned in the past that you do see some advantages with broadly owning your network, but just curious to hear if your thoughts on this have changed. And I guess if not, what other initiatives do you plan to implement to improve profitability at PBNA? Thanks.

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

A

Yeah. So, yeah. Listen, I would say, we don't contemplate at this point any of the structural changes to our business. We continue to think that operating the business has advantages for us in terms of speed of execution and some other elements that – as we see, where the business is growing in e-commerce, away-from-home and some other channels of the future including direct-to-consumer, we think that that's going to create an advantage for us.

Now, we've been making progress at a good pace in our margin improvement. If you think about the last three years, the net revenue for PBNA has grown over $5 billion and the operating profit has grown $1 billion, core operating margin has expanded more than 150 bps. So, we see the last few years a good improvement in the PBNA business. We think this will continue in the coming years, actually 2024. That's a first step.

We are optimizing the portfolio. We're eliminating parts of the portfolio that were less profitable. We've referred to bottled water. We've referred to some multi-serve parts of the portfolio that were not that profitable. We continue to optimize our – efficiency of our supply chain. We're digitalizing our supply chain. We continue to eliminate waste from that. We continue to work on Global Business Services that reduces the G&A. We're also optimizing A&M, trying to get to higher ROI on A&M and our trade investments.

So, we continue to think that optimizing all those elements in the different parts of the P&L will continue to drive a sustainable margin improvement whilst we remain very competitive in the marketplace. And that's the balance that we're trying to strike with this business. So far, we feel good. The business grew with the rest of the category.

If you take everything that is in our system, grew in line with the category, and we increased the operating margin. So, that's how we're thinking at this point about the PBNA business with a long-term perspective obviously, in how we will achieve those two elements of growing with the category and increasing the margins.

Operator: Thank you. One moment for our next question. Our next question comes from Kaumil Gajrawala with Jefferies. Your line is open.

Kaumil Gajrawala
Analyst, Jefferies LLC

Q

Hey, everybody. Good morning. Welcome back, Jamie. Well, I suppose you've gone nowhere, but welcome back to dealing with us, I guess.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.
A

Thank you, Kaumil. It's always great...

Kaumil Gajrawala
Analyst, Jefferies LLC
Q

Can you maybe talk a bit more about international, particularly margins are picking up above the average now, it's scaling quite nicely. But also if there's anything we need to be aware of as it relates to hyperinflation, Argentina, anything like that.

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

No. Listen, I'll start and maybe Jamie can add to this. Listen, the international opportunity continues to be probably the most remarkable and exciting opportunity that we have as a company. As you're saying, our international business is very scaled now. It's almost $40 billion between beverages and snacks. So you compare it to some of the consumer goods companies, it's much bigger than many other consumer goods companies, where we saw clearly a big opportunity. And we have just scratched the surface when you think about the per capita consumption that we have in many markets and the opportunity we have ahead of us.

So, yes, your point is right. As we scale it, some of those businesses are becoming more profitable. And obviously, you start the virtuous circle of scale, reinvestment, margin expansion, and getting to a much more profitable and advantaged businesses across many markets. So, this year is not going to be a different one. So, 2024 we continue to think that international will grow faster than the US business.

We're seeing good momentum as we start the year in many of our international businesses. Our position is of investment in those markets, so we're going aggressively with productivity and reinvestment for growth. Reinvestment in the brands, reinvestments in systems, in capabilities that continue to drive the per caps and our share of market position. So, you should think about our international business as a big opportunity for PepsiCo.

And with regards to the Argentina situation, it's...

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.
A

Yeah, we've already taken a hyper accounting, and you shouldn't expect any material impact on organic sales growth.

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

Dara Mohsenian
Analyst, Morgan Stanley & Co. LLC
Q

Hey. Good morning, guys. And Jamie, great to hear your voice again.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.
A

Hey, Dara.

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

Hello, Dara.

Dara Mohsenian
Analyst, Morgan Stanley & Co. LLC
Q

So, I wanted to drill down a bit more on Bonnie's question, but looking at PBNA top line more than profit, there's clearly been some market share struggles in pieces of the portfolio there, sports drinks, CSDs, et cetera. So, I guess, can you just talk a little bit more about strategy changes from a top line standpoint? How you sort of manage the business by product category, and your thoughts around share trends as we look going forward? Thanks.

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

Hi, Dara. Listen, we feel good about the overall portfolio of PBNA. You know we manage the business as a full LRB business; not as a CSD or any particular sub category. We're looking at the full portfolio and how it – it's always everywhere for consumers from the morning to the night in other multiple occasions. We continue to believe that we have an advantaged portfolio. If you think about our positions in sports and hydration, our positions in coffee, tea, now the portfolio we have in energy, and our CSD position as well. So, we continue to manage as a full LRB.

Now, if you think about our priorities for the year, relaunch of Pepsi brand with a new image. We focus on Zero. Zero has been growing very fast and continues to be an advantage proposition for us. We're putting a lot of additional investment in Mountain Dew and we're launching Baja Blast as a permanent SKU. Baja Blast had been a success as an LTO, a limited time offer, for many years. Now, we're launching it. We're using the Super Bowl as a platform this weekend to launch Baja Blast.

We continue to build a position in lemon-lime with Starry. Starry, it's been a good first year. I think we had – we're over-indexing with Gen Z. We see the brand getting some good repeat. You will see also an investment around Super Bowl and continue during the year, so that's our CSD portfolio. We feel very good about Gatorade. Gatorade is – we're moving from historically a liquid for high-performing athletes to an ecosystem of solutions in hydration and fuel for every type of active person.

And we're seeing a lot of traction. It's not only Gatorade per se, but it's Gatorlyte, it's GFit, it's Propel, it's Muscle Milk, all under one umbrella. And it's not only liquid solutions, it's powders, it's tablets, it's equipment, personalized equipment, bottles and others. And now, we're launching around the Super Bowl, Gatorade iD, which is also an ecosystem of loyalty and, I would say, personalization for our consumers that will bring even more attention to the brand and more loyalty with younger consumers.

On energy, we're very happy with our portfolio. Obviously, the Starbucks coffee energy on one side, Rockstar and obviously our collaboration with Celsius which has been a great success, and it provides scale to our go-to-market and kind of a point of entry as well with some of our customers. And then, our tea business continues to do very well with Pure Leaf, and our Starbucks collaboration now moving more into, beyond coffee I would say, more refreshers and some other innovation that Starbucks is developing for their cafes and we bring it to ready-to-drink.

So, I think we have a beautiful portfolio. We continue to grow in retail and we're putting a lot of focus in away-from-home, as we're seeing that the away-from-home channel is getting much more traffic as people go back to normal mobility, and that will be a focus for us going forward. This year, we think we'll continue to grow both the market and continue to gain share in what is a very profitable and high-growth channel. So, this is how we're thinking about the business, Dara. Hopefully, it gives you a good sense of the intentionality, how we're thinking about the broad portfolio, and our willingness to compete with innovation, with brand investment and with great execution.

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

Peter Grom
Analyst, UBS Securities LLC

Q

Thanks, operator, and good morning, everyone. Ramon, I just wanted to ask a follow-up based on your response to both Bryan and Lauren's question on the organic growth. And I may have misheard or could be misinterpreting this, but you touched on some of the things that you are doing internally that will drive the improved performance. But I think you also mentioned some sort of assumption around maybe the US consumer would feel better. I mean, if that doesn't happen, would that put the organic revenue guidance at risk, or would an improved backdrop be more of a source of upside versus greater than 4%. Thanks.

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

A

The current assumption is what I said. We think that the consumer will continue to improve in its confidence and its disposable income throughout the year, and that's the ongoing assumption. We have a very strong productivity program in the company which gives us the fuel for investment and it gives us also a lot of flexibility to manage a potential different consumer reality.

But at this point, we think this is the ongoing assumption. We will invest in our brands. We will invest in our innovation. And now that supply chain is in a very good place compared to what it was a couple of years ago, even last year, we can rely on the tools that we're very good at, which is brand-building, innovation, execution, distribution increases, strong commercial programs with our partners. And that's where we think we'll drive the growth of our top line here.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.

A

I'd add, just to remind you, 40% of our business is now international. So, US is significant, but we've got a big business outside the US.

Operator: Thank you. One moment for our next question. Our next question comes from Gerald Pascarelli with Wedbush. Your line is open.

Gerald Pascarelli
Analyst, Wedbush Securities, Inc.

Q

Great, thanks very much. Ramon, I have a question on energy drinks. Can you just speak about your plans to maybe drive performance in Rockstar this year? It's kind of been a relative underperformer in energy drinks for some time, and now you have Bang coming back into the market which could potentially result in some incremental disruption. So maybe just some color on how you're thinking about driving an improvement in that brand, and then maybe broader thoughts on the competitive dynamics within energy drinks this year. Thank you.

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

A

Yeah. It's a great question. The energy category continues to grow, as you see, above the LRB category, so continues to expand into new consumers and new consumer occasions, which obviously creates growth for everyone that participates in the category. So, we participate, as we've always said, with multiple vectors. We're proud of our Starbucks partnership and some of the products we offer, Doubleshot, Tripleshot.

We're proud of the Rockstar brand. Rockstar has been growing with the category. More or less, there's some parts of the country where it's well-distributed and well-preferred. Other parts of the country, we're trying to get consumer penetration and consumer adoption. The areas where we've been successful with Rockstar which we will double down the Zero and the Recover parts of the portfolio. Both of them, if you think, is energy with functionality and where we think our R&D can create advantage. So, we're pushing those two platforms, Rockstar Zero and Rockstar Recover; and that will continue to be the focus of the brand.

We've also been focusing on Hispanic consumer and that also we've seen an increase in the penetration of the brand with the Hispanic population, Hispanic consumers. We'll continue to drive that commercial activity. But we see this as a portfolio of solutions including Celsius and how the combined portfolio creates a very good point of execution for us, multi-brand. It gives us an entry into convenience stores and some other points of sale away-from-home, and we'll continue to drive the portfolio as the unit of execution.

Operator: Thank you. One moment for our next question.

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

A

Forgot, maybe I can say, the other thing we're doing with Rockstar which we don't talk a lot, but it's an important part of our growth is, we're launching Rockstar internationally in many markets around the world, from Asia to Europe to parts of Latin America; and we're having good success. Again, as a portfolio of solutions, that complements our esteemed brand that we have in Asia or some other brands that we have in Europe as well.

Operator: Our next question comes from Robert Moskow with TD Cowen. Your line is open.

Robert Moskow
Analyst, TD Cowen

Q

Hi. Thank you for the question. In your prepared remarks, you said that you expect less commodity inflation, but some agricultural inputs might be higher. Can you be more specific? And I was hoping you could focus a little on Frito, because there's a very big potato crop this past year, vegetable oil costs are coming down. Do you see any relief on the horizon for Frito in that regard?

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.

A

Hey, Rob. It's Jamie. Yeah. As a practice, we comment on the basket of inputs, we don't comment on specific commodity movement. But you're absolutely correct that we do expect commodity inflation to moderate from what we had in 2023.

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

Andrea Teixeira
Analyst, JPMorgan Securities LLC

Q

Thank you, operator. Good morning to you all, and great having you back, Jamie, on the investor-facing mode. I have one question and then a clarification. First, for Ramon. I was hoping to see if you can elaborate a little bit more on how you're going to be lapping? And if you ever lapped, the mix drags and the shift from away from – to away-from-home, and where your market share is not probably as strong as in snacks as you have in at-home channels.

And given your strong gross margin delivery and your experience in negotiating with large box retailers, especially in Europe, are retailers asking you to invest back in promo rollbacks, given your gross margin delivery and productivity gains in particularly North America and in Europe?

And my clarification for Jamie is, in terms of like the organic sales growth and EPS cadence for the year, anything we should be considering on your guide as part of cadence? Thank you.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.

A

Yeah. So on the organic sales growth – first of all, Andrea, it's great to hear your voice again and look forward to interacting as we go forward. Organic sales growth cadence, I'd say, back half stronger than the first half. As we talked about before, we've got the impact of that the Quaker Recall is going to be front-half loaded. The laps get easier as we get into the back half of the year. And then some of these consumer pressures that have existed with elimination of stimulus benefits, resumption of student loan payments, we'll lap those as we get into the year.

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

A

Yeah, Andrea. Listen, with regards to the customer, I think we're all trying to build win-win plans in the sense that we grow the business and we create profit growth for both our customers and ourselves. We normally – we have always the consumer at the center, so it will be a combination of how – we generate growth through, as I said, innovation and we have a few big innovations and brand relaunches this year. We'll put a lot of investment there together with our customers.

We'll continue to try to expand our SKUs with the customers and there will be investments there, and there will be some investments in trying to give more value to consumers in a very holistic way, right? Through pack price, through promotions, through consumer events that eventually will drive preference for our brands. But that's the way we're thinking about creating this joint business planning with our large customers that create growth for the category, growth for our customers, and growth for us.

Operator: Thank you.

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

A

With regards to away-from-home, sorry, I forgot, Andrea. The away-from-home, we see it as an and, not as an or. So, we see as an opportunity for us to continue to be in consumers' lives always everywhere. And as consumers pivot away-from-home, we'll try to be there for them. It's been an area of investment for us both in distribution and specific solutions for away-from-home for quite some time, and we're seeing our businesses in the large markets growing above the market in away-from-home.

So clearly, this will be an opportunity for us for many years to come, and I think we're getting better at mixology, we're getting better at more food experiences, walking tacos, Doritos Loaded. We're testing food trucks, we're testing many things that will make our brands available to consumers beyond what is a packaged bag or a can or a bottle. Now, I think consumers are expecting from us away-from-home a much more holistic experience, and that's where we're working on and I think we're making good progress.

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

Robert Ottenstein
Analyst, Evercore ISI
Q

Great. Thank you very much. A little bit more of a detailed question on PBNA, and just want to talk about Gatorade and Celsius. So in terms of Gatorade, could you just remind us in terms of the timing of the move to DSD, and how that impacted your income statement?

And then in terms of Celsius, obviously, the brand has done phenomenally well. It's getting pretty big now. Can you talk about how Celsius impacts the income statement in the US? And then, how your relationship with the company has evolved? You talked about taking Rockstar internationally. Celsius is going international now. Are you part of that plan as well? Thank you.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.
A

Yeah. So on Gatorade, we're 90% through on the transition. Obviously, that move is positive to the financial results overall. That's what we did is to enhance performance, and we're happy with the margins we have on that business. On Celsius, the way that works is, we're sharing the system revenue with Celsius.

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

Yeah. Listen, we're happy with the collaboration with Celsius and that continues to be a part of our growth strategy. There is an opportunity for us to collaborate in the international expansion as well. At this point, it's not, I would say, a scaled opportunity. It's a market-by-market opportunity and very particular market. So, yeah, we are contemplating that as an option, and we're having conversation with Celsius how we can leverage the PepsiCo system for a bigger expansion. Nothing short term, I would say, at this point.

Operator: Thank you. One moment for our next question. Our next question comes from Chris Carey with Wells Fargo. Your line is open.

Chris Carey
Analyst, Wells Fargo Securities LLC
Q

Hi. Good morning, everyone. So, I just wanted to ask about SG&A over the past four years. We've talked about this before in this forum, but with the annual disclosures now out, I thought it'd be a good time to revisit the topic.

Just specifically, Ramon, can you help contextualize the increase that we've seen in SG&A over the past four years, specifically the distribution costs? I'm really curious about maybe how much of this is underlying inflation as opposed to discretionary investments that PepsiCo is making, and I'm not really looking for a specific number per se. I realize that's probably difficult.

But distribution's up 40% over the past four years and I'm just wondering how much of this is within your control, maybe some of the capabilities that you've been able to build over this timeframe, and maybe get a sense of how this line item should be trending going forward. So, thanks.

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

A

Yeah. So as you point out, selling and distribution is the biggest part of that. The A part is less sell. And it's going to be a reflection what you see is, one, you've got market mix or sector mix components in there. We've driven a lot of productivity in our OpEx, but at the same time we're investing in OpEx to drive distribution and growth in the business.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.

A

One other thing, Chris, that you should be mindful of is, we do have a big direct store delivery business, so we've had inflation in various things like labor and so forth, and that's what's gone up. A&M has gone up as well which is also kind of all part of that SG&A bucket. We've made numerous capability investments in there as well. So, it's all of the above. I wouldn't hone in just on the distribution costs which I know you focus on from the 10-K, but there's a lot of buckets that go in that are far deeper that we can't get into for competitive reasons.

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

Filippo Falorni
Analyst, Citigroup Global Markets, Inc.

Q

Hey. Good morning, everyone. So, Ramon and Jamie, you both mentioned the organic sales growth guidance is going to be more second half weighted, and I know you don't provide breakdown and guidance on volumes. But given the importance of volume trends, can you give us a sense of how you see volumes evolving? Is there a possibility in your guidance where you see positive volumes in the second half of the year?

And then, on the pricing front, maybe you can give us a sense of what are you assuming in terms of pricing. I assume in the US or developed markets, it's limited and there's more pricing in emerging markets. But any color on pricing would be also helpful. Thank you.

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

A

Yeah. I think you should be thinking about, we want to grow units next year. We will see profitable volume growth next year and you'll see a more balance between pricing and volume that you have seen in previous year, where obviously we had to cover a huge commodity increase and OpEx increase. As commodities kind of normalize and OpEx inflation normalizes, that lever will be less necessary outside of what has been a normal pricing levels of our category in the 2% to 3%. So you should be thinking about profitable volume growth and more of a normalized pricing compared to what it was in the 2018-2019 timeframe.

Operator: Thank you. One moment for our next question. Our next question comes from Callum Elliott with Bernstein. Your line is open.

Callum Elliot
Analyst, Bernstein Autonomous LLP

Q

Hi. Good morning. I wanted to build upon Chris' question, please, and ask you about the A&M buckets and the spending behind your brands. I think K shows advertising up around 10% year-on-year and that's around a 20 basis points increase as a percentage of sales. But we're still quite a long way below pre-pandemic levels as a percentage of sales and comfortably below the average over the last several years. So, I guess the question is, are your brands getting enough support, and do we need to see upwards pressure on advertising spend as a percentage of sales over the coming years? Thank you.

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

A

That was great. Good point. Obviously, in absolute terms, we have much more A&M, so I think we have increased – last year was $500 million. And if you think about a longer timeframe, a meaningful over $1 billion increase in absolute A&M, so that's absolute dollars that go against our business. We're thinking about continuing that trend. Continuing to support both our large brands across multiple markets and then smaller brands where we take the portfolio into the future. So, that should be a composition of our A&M.

Now, when you look at the last few years, you should bear in mind, we stopped advertising in Russia which was a meaningful market for us. So, that is reflected in our absolute numbers or relative numbers. So that you should contemplate that. But if you think about where and how we're going to create demand in the future, you should be thinking about A&M continuing to increase. Obviously, we'll look at ways to optimize A&M, and we have very strong measures on ROI, and there's ways to invest in our brands. But you should be thinking about as a company that continues to build brands, continues to innovate, continue to create value through investment in consumer.

And obviously, we also create a lot of demand through our push model to some of the questions that was asked before. You should be thinking about our selling and distribution costs not only as a cost, but also as a way for us to execute very granularly across millions and millions of point-of-sale around the world where we reach the final point-of-sale and we create, I would say, visibility for our brands and impulse for our brands which are relevant, if you think about the categories where we compete.

Operator: One moment for our next question. Our last question comes from Steve Powers with Deutsche Bank. Your line is open.

Steve Powers
Analyst, Deutsche Bank Securities, Inc.

Q

Oh, great. Good morning; and thanks, everybody. Jamie, add me to the list of people excited to work with you again.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.

A

Thanks, Steve.

Steve Powers
Analyst, Deutsche Bank Securities, Inc.

Q

Hey. Actually, this question may be for you. It probably is for you. On these calls, for the last several years, we've been talking about on and off just sort of the cash flow profile of the business and the capital investments that have been made in the business in the past, eventually back towards a higher level of free cash flow conversion.

I guess, you're acknowledging that you've been there in the room the whole time. I guess, now as you assume the role of CFO, do you see any opportunities to speed that process of cash flow generation and a return to higher levels of free cash flow conversion from where we've been trending, or is it more steady-state? And if you could just give us a little perspective on how you're seeing that cash flow profile of the business evolving from here, that'd be great. Thank you.

Jamie Caulfield
Executive Vice President & Chief Financial Officer, PepsiCo, Inc.

A

Yeah. So clearly, cash flow continues to be a priority. I'd focus on CapEx, and we've been very intentional about the levels of capital we've invested in the business. Part of that was to catch up more on capacity. We're currently in the midst of big investments in IT and digitalization. But over time, I think you'll see the level of CapEx as a percent of sales begin to trend down, and that'll help with the cash flow conversion.

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

Great. So, thank you, everybody. I'm glad everybody's happy that Jamie's back, and I see a lot of bonding. Great. But obviously, thank you for the confidence that you've placed in our investment, and we look forward to seeing many of you at CAGNY in a couple of weeks and having a longer conversation there. Thank you very much.

Operator: Ladies and gentlemen, that concludes today's presentation. You may now disconnect, and have a wonderful day.