PEPSICO INC
Form 10-Q
October 12, 2011
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

X QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 3, 2011 (36 weeks)

OR

__ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______ to ______

Commission file number 1-1183

PepsiCo, Inc.
(Exact Name of Registrant as Specified in its Charter)

North Carolina	13-1584302
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
700 Anderson Hill Road, Purchase, New York	10577
(Address of Principal Executive Offices)	(Zip Code)

914-253-2000

(Registrant s Telephone Number, Including Area Code)

N/A

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES X NO __

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES X NO __

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer X	Accelerated filer __
Non-accelerated filer __	Smaller reporting company __

(Do not check if a smaller reporting company)
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES__NO X

Number of shares of Common Stock outstanding as of October 5, 2011: 1,563,410,224

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PEPSICO, INC. AND SUBSIDIARIES

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PART I FINANCIAL INFORMATION

ITEM 1. Condensed Consolidated Financial Statements.

PEPSICO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF INCOME

(in millions except per share amounts, unaudited)

	12 Weeks Ended		36 Weeks Ended	
	9/3/11	9/4/10	**9/3/11**	9/4/10
Net Revenue	**$ 17,582**	$ 15,514	**$ 46,346**	$ 39,683
Cost of sales	**8,452**	7,008	**21,862**	18,216
Selling, general and administrative expenses	**6,186**	5,676	**16,995**	15,288
Amortization of intangible assets	**38**	30	**103**	78
Operating Profit	**2,906**	2,800	**7,386**	6,101
Bottling equity income		10		728
Interest expense	**(205)**	(169)	**(584)**	(495)
Interest income and other	**(4)**	18	**33**	26
Income before income taxes	**2,697**	2,659	**6,835**	6,360
Provision for income taxes	**686**	729	**1,775**	1,383
Net income	**2,011**	1,930	**5,060**	4,977
Less: Net income attributable to noncontrolling interests	**11**	8	**32**	22
Net Income Attributable to PepsiCo	**$ 2,000**	$ 1,922	**$ 5,028**	$ 4,955
Net Income Attributable to PepsiCo per Common Share				
Basic	**$ 1.27**	$ 1.21	**$ 3.18**	$ 3.11
Diluted	**$ 1.25**	$ 1.19	**$ 3.14**	$ 3.06
Cash dividends declared per common share	**$ 0.515**	$ 0.48	**$ 1.51**	$ 1.41

See accompanying notes to the condensed consolidated financial statements.

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PEPSICO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions, unaudited)

	36 Weeks Ended	
	9/3/11	9/4/10
Operating Activities		
Net income	**$ 5,060**	$ 4,977
Depreciation and amortization	**1,877**	1,580
Stock-based compensation expense	**222**	191
Cash payments for restructuring charges	**(1)**	(29)
Merger and integration costs	**174**	545
Cash payments for merger and integration costs	**(293)**	(272)
Gain on previously held equity interests in The Pepsi Bottling Group, Inc. (PBG) and PepsiAmericas, Inc. (PAS)		(958)
Asset write-off		145
Non-cash foreign exchange loss related to Venezuela devaluation		120
Excess tax benefits from share-based payment arrangements	**(56)**	(73)
Pension and retiree medical plan contributions	**(185)**	(1,350)
Pension and retiree medical plan expenses	**389**	310
Bottling equity income, net of dividends		37
Deferred income taxes and other tax charges and credits	**132**	291
Change in accounts and notes receivable	**(1,643)**	(1,287)
Change in inventories	**(466)**	224
Change in prepaid expenses and other current assets	**(54)**	(14)
Change in accounts payable and other current liabilities	**142**	762
Change in income taxes payable	**936**	787
Other, net	**(400)**	(198)
Net Cash Provided by Operating Activities	**5,834**	5,788
Investing Activities		
Capital spending	**(1,962)**	(1,670)
Sales of property, plant and equipment	**46**	55
Acquisitions of PBG and PAS, net of cash and cash equivalents acquired		(2,833)
Acquisition of manufacturing and distribution rights from Dr Pepper Snapple Group, Inc. (DPSG)		(900)
Acquisition of Wimm-Bill-Dann Foods OJSC (WBD), net of cash and cash equivalents acquired	**(2,428)**	
Investment in WBD	**(164)**	
Other acquisitions and investments in noncontrolled affiliates	**(160)**	(36)
Divestitures	**10**	
Cash restricted for pending acquisitions		(8)

Short-term investments, by original maturity		
More than three months purchases		(8)
More than three months maturities	**14**	21
Three months or less, net	**(48)**	(53)
Other investing, net	**(3)**	(12)
Net Cash Used for Investing Activities	**(4,695)**	(5,444)

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PEPSICO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (continued)

(in millions, unaudited)

	36 Weeks Ended	
	9/3/11	9/4/10
Financing Activities		
Proceeds from issuances of long-term debt	**$ 3,000**	$ 4,215
Payments of long-term debt	**(1,596)**	(73)
Debt repurchase	**(771)**	
Short-term borrowings, by original maturity		
More than three months proceeds	**224**	55
More than three months payments	**(274)**	(27)
Three months or less, net	**106**	3,351
Cash dividends paid	**(2,349)**	(2,218)
Share repurchases common	**(1,929)**	(4,418)
Share repurchases preferred	**(5)**	(3)
Proceeds from exercises of stock options	**724**	700
Excess tax benefits from share-based payment arrangements	**56**	73
Acquisition of noncontrolling interests	**(1,327)**	(159)
Other financing	**(2)**	(6)
Net Cash (Used for)/Provided by Financing Activities	**(4,143)**	1,490
Effect of exchange rate changes on cash and cash equivalents	**144**	(200)
Net (Decrease)/Increase in Cash and Cash Equivalents	**(2,860)**	1,634
Cash and Cash Equivalents, Beginning of Year	**5,943**	3,943
Cash and Cash Equivalents, End of Period	**$ 3,083**	$ 5,577
Non-cash activity:		
Issuance of common stock and equity awards in connection with our acquisitions of PBG and PAS, as reflected in investing and financing activities		$ 4,451

See accompanying notes to the condensed consolidated financial statements.

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PEPSICO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEET

(in millions)

	(Unaudited) 9/3/11	12/25/10
Assets		
Current Assets		
Cash and cash equivalents	$ **3,083**	$ 5,943
Short-term investments	**452**	426
Accounts and notes receivable, less allowance: 9/11 $147, 12/10 $144	**8,330**	6,323
Inventories		
Raw materials	**2,152**	1,654
Work-in-process	**237**	128
Finished goods	**1,816**	1,590
	4,205	3,372
Prepaid expenses and other current assets	**1,764**	1,505
Total Current Assets	**17,834**	17,569
Property, Plant and Equipment	**36,262**	33,041
Accumulated Depreciation	**(15,525)**	(13,983)
	20,737	19,058
Amortizable Intangible Assets, net	**2,426**	2,025
Goodwill	**16,272**	14,661
Other Nonamortizable Intangible Assets	**15,433**	11,783
Nonamortizable Intangible Assets	**31,705**	26,444
Investments in Noncontrolled Affiliates	**1,500**	1,368
Other Assets	**1,176**	1,689
Total Assets	$ **75,378**	$ 68,153

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PEPSICO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEET (continued)

(in millions except per share amounts)

	(Unaudited) **9/3/11**	12/25/10
Liabilities and Equity		
Current Liabilities		
Short-term obligations	**$ 5,070**	$ 4,898
Accounts payable and other current liabilities	**11,524**	10,923
Income taxes payable	**971**	71
Total Current Liabilities	**17,565**	15,892
Long-term Debt Obligations	**21,781**	19,999
Other Liabilities	**6,859**	6,729
Deferred Income Taxes	**5,170**	4,057
Total Liabilities	**51,375**	46,677
Commitments and Contingencies		
Preferred Stock, no par value	**41**	41
Repurchased Preferred Stock	**(155)**	(150)
PepsiCo Common Shareholders Equity		
Common stock, par value 1 2/3 cents per share:		
Authorized 3,600 shares, issued 9/11 and 12/10 1,865 shares	**31**	31
Capital in excess of par value	**4,406**	4,527
Retained earnings	**39,714**	37,090
Accumulated other comprehensive loss	**(2,800)**	(3,630)
Less: repurchased common stock, at cost: 9/11 297 shares, 12/10 284 shares	**(17,660)**	(16,745)
Total PepsiCo Common Shareholders Equity	**23,691**	21,273
Noncontrolling interests	**426**	312
Total Equity	**24,003**	21,476
Total Liabilities and Equity	**$ 75,378**	$ 68,153

See accompanying notes to the condensed consolidated financial statements.

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PEPSICO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF EQUITY

(in millions, unaudited)

	36 Weeks Ended			
	9/3/11		9/4/10	
	Shares	**Amount**	Shares	Amount
Preferred Stock	**0.8**	**$ 41**	0.8	$ 41
Repurchased Preferred Stock				
Balance, beginning of year	**(0.6)**	**(150)**	(0.6)	(145)
Redemptions	**( )**	**(5)**	( )	(3)
Balance, end of period	**(0.6)**	**(155)**	(0.6)	(148)
Common Stock				
Balance, beginning of year	**1,865**	**31**	1,782	30
Shares issued in connection with our acquisitions of PBG and PAS			83	1
Balance, end of period	**1,865**	**31**	1,865	31
Capital in Excess of Par Value				
Balance, beginning of year		**4,527**		250
Stock-based compensation expense		**222**		191
Stock option exercises/RSUs converted[a]		**(303)**		(399)
Withholding tax on RSUs converted		**(54)**		(57)
Equity issued in connection with our acquisitions of PBG and PAS				4,451
Other		**14**		99
Balance, end of period		**4,406**		4,535
Retained Earnings				
Balance, beginning of year		**37,090**		33,805
Net income attributable to PepsiCo		**5,028**		4,955
Cash dividends declared common		**(2,388)**		(2,270)
Cash dividends declared preferred		**(1)**		(1)
Cash dividends declared RSUs		**(15)**		(9)
Other				7
Balance, end of period		**39,714**		36,487
Accumulated Other Comprehensive Loss				
Balance, beginning of year		**(3,630)**		(3,794)
Currency translation adjustment		**870**		(291)

Cash flow hedges, net of tax:				
Net derivative losses		**(63)**		(123)
Reclassification of net losses to net income		**11**		39
Pension and retiree medical, net of tax:				
Reclassification of losses to net income		**49**		210
Remeasurement of net liabilities				(406)
Unrealized (losses)/gains on securities, net of tax		**(20)**		7
Other		**(17)**		
Balance, end of period		**(2,800)**		(4,358)
Repurchased Common Stock				
Balance, beginning of year	**(284)**	**(16,745)**	(217)	(13,383)
Share repurchases	**(30)**	**(1,970)**	(68)	(4,418)
Stock option exercises	**15**	**948**	17	1,029
Other	**2**	**107**	(15)	122
Balance, end of period	**(297)**	**(17,660)**	(283)	(16,650)
Total Common Shareholders Equity		**23,691**		20,045
Noncontrolling Interests				
Balance, beginning of year		**312**		638
Net income attributable to noncontrolling interests		**32**		22
Contributions from/(distributions to) noncontrolling interests, net		**13**		(347)
Currency translation adjustment		**69**		(14)
Other, net				(1)
Balance, end of period		**426**		298
Total Equity		**$ 24,003**		$ 20,236

[a] Includes total tax benefits of $35 million in 2011 and $50 million in 2010.

See accompanying notes to the condensed consolidated financial statements.

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PEPSICO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT

OF COMPREHENSIVE INCOME

(in millions, unaudited)

	12 Weeks Ended		36 Weeks Ended	
	9/3/11	9/4/10	**9/3/11**	9/4/10
Net Income	**$ 2,011**	$ 1,930	**$ 5,060**	$ 4,977
Other Comprehensive (Loss)/Income				
Currency translation adjustment	**(515)**	290	**939**	(305)
Cash flow hedges, net of tax:				
Net derivative losses	**(46)**	(37)	**(63)**	(123)
Reclassification of net losses to net income	**4**	16	**11**	39
Pension and retiree medical, net of tax:				
Reclassification of losses/(gains) to net income	**26**	(1)	**49**	210
Remeasurement of net liabilities		(406)		(406)
Unrealized (losses)/gains on securities, net of tax	**(18)**	6	**(20)**	7
Other			**(17)**	
	(549)	(132)	**899**	(578)
Comprehensive Income	**1,462**	1,798	**5,959**	4,399
Comprehensive income attributable to noncontrolling interests	**(8)**	(8)	**(101)**	(8)
Comprehensive Income Attributable to PepsiCo	**$ 1,454**	$ 1,790	**$ 5,858**	$ 4,391

See accompanying notes to the condensed consolidated financial statements.

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PEPSICO, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Basis of Presentation and Our Divisions

Basis of Presentation

Our Condensed Consolidated Balance Sheet as of September 3, 2011 and the Condensed Consolidated Statements of Income and Comprehensive Income for the 12 and 36 weeks ended September 3, 2011 and September 4, 2010, and the Condensed Consolidated Statements of Cash Flows and Equity for the 36 weeks ended September 3, 2011 and September 4, 2010 have not been audited. These statements have been prepared on a basis that is substantially consistent with the accounting principles applied in our Annual Report on Form 10-K for the fiscal year ended December 25, 2010 and in our Current Report on Form 8-K dated March 31, 2011. In our opinion, these financial statements include all normal and recurring adjustments necessary for a fair presentation. The results for the 12 and 36 weeks are not necessarily indicative of the results expected for the full year.

While the majority of our results are reported on a period basis, most of our international operations report on a monthly calendar basis for which the months of June, July and August are reflected in our third quarter results.

On February 26, 2010, we completed our acquisitions of PBG and PAS. The results of the acquired companies in the U.S. and Canada are reflected in our condensed consolidated results as of the acquisition date, and the international results of the acquired companies have been reported as of the beginning of our second quarter of 2010, consistent with our monthly international reporting calendar. Prior to our acquisitions of PBG and PAS, we recorded our share of equity income or loss from the acquired companies in bottling equity income in our income statement. Additionally, in the first quarter of 2010, in connection with our acquisitions of PBG and PAS, we recorded a gain on our previously held equity interests of $958 million, comprising $735 million which was non-taxable and recorded in bottling equity income and $223 million related to the reversal of deferred tax liabilities associated with these previously held equity interests. Our share of income or loss from noncontrolled affiliates is reflected as a component of selling, general and administrative expenses. See also *Acquisitions* and Items Affecting Comparability in Management s Discussion and Analysis of Financial Condition and Results of Operations.

In the first quarter of 2011, Quaker Foods North America (QFNA) changed its method of accounting for certain U.S. inventories from the last-in, first-out (LIFO) method to the average cost method. This change is considered preferable by management as we believe that the average cost method of accounting for all U.S. foods inventories will improve our financial reporting by better matching revenues and expenses and better reflecting the current value of inventory. In addition, the change from the LIFO method to the average cost method will enhance the comparability of QFNA s financial results with our other food businesses, as well as with peer companies where the average cost method is widely used. The impact of this change on consolidated net income in the first quarter of 2011 was approximately $9 million (or less than a penny per share). Prior periods were not restated as the impact of the change on previously issued financial statements was not considered material.

Our significant interim accounting policies include the recognition of a pro rata share of certain estimated annual sales incentives, and certain advertising and marketing costs, generally in

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proportion to revenue, and the recognition of income taxes using an estimated annual effective tax rate. Raw materials, direct labor and plant overhead, as well as purchasing and receiving costs, costs directly related to production planning, inspection costs and raw material handling facilities, are included in cost of sales. The costs of moving, storing and delivering finished product are included in selling, general and administrative expenses.

The following information is unaudited. Tabular dollars are in millions, except per share amounts. All per share amounts reflect common per share amounts, assume dilution unless otherwise noted, and are based on unrounded amounts. Certain reclassifications were made to the prior year s amounts to conform to the 2011 presentation. This report should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended December 25, 2010 and our Current Report on Form 8-K dated March 31, 2011, in which we reclassified historical segment information on a basis consistent with our current segment reporting structure.

Our Divisions

We are organized into four business units, as follows:

1. PepsiCo Americas Foods (PAF), which includes Frito-Lay North America (FLNA), Quaker Foods North America (QFNA) and all of our Latin American food and snack businesses (LAF);

2. PepsiCo Americas Beverages (PAB), which includes PepsiCo Beverages Americas and Pepsi Beverages Company;

3. PepsiCo Europe, which includes all beverage, food and snack businesses in Europe; and

4. PepsiCo Asia, Middle East and Africa (AMEA), which includes all beverage, food and snack businesses in AMEA.

Our four business units comprise six reportable segments (also referred to as divisions), as follows:

- FLNA,
- QFNA,
- LAF,
- PAB,
- Europe, and

AMEA.

	12 Weeks Ended		36 Weeks Ended	
	9/3/11	9/4/10	**9/3/11**	9/4/10
Net Revenue				
FLNA	**$ 3,173**	$ 3,050	**$ 9,167**	$ 8,906
QFNA	**614**	601	**1,837**	1,866
LAF	**1,841**	1,542	**4,757**	4,063
PAB	**5,947**	5,792	**16,107**	14,105
Europe[a]	**3,909**	2,848	**9,329**	6,390
AMEA	**2,098**	1,681	**5,149**	4,353
	$ 17,582	$ 15,514	**$ 46,346**	$ 39,683

	12 Weeks Ended		36 Weeks Ended	
	9/3/11	9/4/10	**9/3/11**	9/4/10
Operating Profit				
FLNA	**$ 918**	$ 866	**$ 2,545**	$ 2,394
QFNA	**177**	167	**558**	521
LAF	**275**	238	**720**	616
PAB	**992**	1,017	**2,533**	2,042
Europe	**514**	432	**984**	826
AMEA	**285**	235	**730**	657
Total division	**3,161**	2,955	**8,070**	7,056
Corporate Unallocated				
Net impact of mark-to-market on commodity hedges	**(53)**	16	**(31)**	58
Merger and integration costs	**(10)**	(16)	**(64)**	(128)
Venezuela currency devaluation				(129)
Asset write-off				(145)
Foundation contribution				(100)
Other	**(192)**	(155)	**(589)**	(511)
	$ 2,906	$ 2,800	**$ 7,386**	$ 6,101

	Total Assets	
	9/3/11	12/25/10
FLNA	**$ 6,185**	$ 6,027
QFNA	**1,242**	1,217
LAF	**4,288**	4,053
PAB	**32,641**	31,622
Europe[a]	**21,180**	13,032
AMEA	**6,163**	5,569
Total division	**71,699**	61,520
Corporate[b]	**3,679**	6,394
Investments in bottling affiliates		239

	$ 75,378	$ 68,153

(a) Change in 2011 relates primarily to our acquisition of WBD.

(b) Corporate assets consist principally of cash and cash equivalents, short-term investments, derivative instruments and property, plant and equipment.

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Acquisitions

PBG and PAS

On February 26, 2010, we acquired PBG and PAS to create a more fully integrated supply chain and go-to-market business model, improving the effectiveness and efficiency of the distribution of our brands and enhancing our revenue growth. The total purchase price was approximately $12.6 billion, which included $8.3 billion of cash and equity and the fair value of our previously held equity interests in PBG and PAS of $4.3 billion. The acquisitions were accounted for as business combinations, and, accordingly, the identifiable assets acquired and liabilities assumed were recorded at their estimated fair values at the date of acquisition. Our fair market valuations of the identifiable assets acquired and liabilities assumed have been completed and the final valuations did not materially differ from those fair values reported as of December 25, 2010.

The following table presents unaudited consolidated pro forma financial information as if the closing of our acquisitions of PBG and PAS had occurred on December 27, 2009 for purposes of the financial information presented for the 36 weeks ended September 4, 2010.

	(unaudited) 36 Weeks Ended 9/4/10
Net Revenue	$ 41,427
Net Income Attributable to PepsiCo	$ 4,491
Net Income Attributable to PepsiCo per Common Share Diluted	$ 2.75

The unaudited consolidated pro forma financial information was prepared in accordance with the acquisition method of accounting under existing standards, and the regulations of the U.S. Securities and Exchange Commission, and is not necessarily indicative of the results of operations that would have occurred if our acquisitions of PBG and PAS had been completed on the date indicated, nor is it indicative of the future operating results of PepsiCo.

The historical unaudited consolidated financial information has been adjusted to give effect to pro forma events that are (1) directly attributable to the acquisitions, (2) factually supportable, and (3) expected to have a continuing impact on the combined results of PepsiCo, PBG and PAS.

The unaudited pro forma results have been adjusted with respect to certain aspects of our acquisitions of PBG and PAS to reflect:

- the consummation of the acquisitions;

- consolidation of PBG and PAS which are now owned 100% by PepsiCo and the corresponding gain resulting from the remeasurement of our previously held equity interests in PBG and PAS;

the elimination of related party transactions between PepsiCo and PBG, and PepsiCo and PAS;

changes in assets and liabilities to record their acquisition date fair values and changes in certain expenses resulting therefrom; and

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additional indebtedness, including, but not limited to, debt issuance costs and interest expense, incurred in connection with the acquisitions.

The unaudited pro forma results do not reflect future events that either have occurred or may occur after the acquisitions, including, but not limited to, the anticipated realization of ongoing savings from operating synergies in subsequent periods. They also do not give effect to certain one-time charges we expect to incur in connection with the acquisitions, including, but not limited to, charges that are expected to achieve ongoing cost savings and synergies.

WBD

On February 3, 2011, we acquired the ordinary shares, including shares underlying American Depositary Shares (ADSs) and Global Depositary Shares (GDSs), of WBD, a company incorporated in the Russian Federation, which represented in the aggregate approximately 66% of WBD s outstanding ordinary shares, pursuant to the purchase agreement dated December 1, 2010 between PepsiCo and certain selling shareholders of WBD for approximately $3.8 billion in cash. The acquisition of those shares increased our total ownership to approximately 77%, giving us a controlling interest in WBD. Under the guidance on accounting for business combinations, once a controlling interest is obtained, we are required to recognize and measure 100% of the identifiable assets acquired, liabilities assumed and noncontrolling interests at their full fair values. As a result, the total consideration transferred was approximately $5.8 billion, which included the $3.8 billion of cash (or $2.4 billion, net of cash and cash equivalents acquired), the fair value of our previously held equity interest in WBD of $0.7 billion and the fair value of the remaining noncontrolling interests in WBD of $1.3 billion. The preliminary estimates of the fair value of the identifiable assets acquired and liabilities assumed in WBD as of the acquisition date include goodwill and other intangible assets of $4.9 billion; property, plant and equipment of $1.3 billion; debt obligations of $1.1 billion; and other net assets of $0.7 billion, all of which are recorded in our Europe segment. The preliminary estimates of the fair value of identifiable assets acquired and liabilities assumed are subject to revisions, which may result in adjustments to the preliminary values discussed above as valuations are finalized. We expect to finalize these amounts as soon as possible but no later than by the end of 2011.

Under the guidance on accounting for business combinations, merger and integration costs are not included as components of consideration transferred but are accounted for as expenses in the period in which the costs are incurred. See *Merger and Integration Charges* for details on the expenses incurred during 2011.

On March 10, 2011, we commenced our tender offers in Russia and the U.S. for all remaining outstanding ordinary shares and ADSs of WBD for 3,883.70 Russian rubles per ordinary share and 970.925 Russian rubles per ADS, respectively. The Russian offer was made to all holders of ordinary shares and the U.S. offer was made to all holders of ADSs. We completed the Russian offer on May 19, 2011 and the U.S. offer on May 16, 2011. After completion of the offers, we paid approximately $1.3 billion for WBD s ordinary shares (including shares underlying ADSs) and increased our total ownership of WBD to approximately 98.6%.

On June 30, 2011, we elected to exercise our squeeze-out rights under Russian law with respect to all remaining WBD ordinary shares not already owned by us. Therefore, under Russian law, all remaining WBD shareholders were required to sell their ordinary shares (including those underlying ADSs) to us at the same price that was offered to WBD shareholders in the Russian tender offer. Accordingly, all registered holders of ordinary shares on August 15, 2011 (including

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the ADS depository) received 3,883.70 Russian rubles per ordinary share. After completion of the squeeze-out in September 2011 (during our fourth quarter), we paid approximately $79 million for WBD s ordinary shares (including shares underlying ADSs) and increased our total ownership to 100% of WBD.

Intangible Assets

	9/3/11	12/25/10
Amortizable intangible assets, net		
Acquired franchise rights	**$ 967**	$ 949
Reacquired franchise rights	**110**	110
Brands	**1,538**	1,463
Other identifiable intangibles	**1,159**	747
	3,774	3,269
Accumulated amortization	**(1,348)**	(1,244)
	$ 2,426	$ 2,025

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The change in the book value of nonamortizable intangible assets is as follows:

	Balance 12/25/10	Acquisitions	Translation and Other	**Balance 9/3/11**
FLNA				
Goodwill	$ 313	$	$ 4	**$ 317**
Brands	31		1	**32**
	344		5	**349**
QFNA				
Goodwill	175			**175**
LAF				
Goodwill	497	18	9	**524**
Brands	143		3	**146**
	640	18	12	**670**
PAB				
Goodwill	9,946	57	9	**10,012**
Reacquired franchise rights	7,283	79	25	**7,387**
Acquired franchise rights	1,565		2	**1,567**
Brands	182	11	3	**196**
Other	10			**10**
	18,986	147	39	**19,172**
Europe (a)				
Goodwill	3,040	1,240	240	**4,520**
Reacquired franchise rights	793		36	**829**
Acquired franchise rights	227		20	**247**
Brands	1,380	3,300	162	**4,842**
	5,440	4,540	458	**10,438**
AMEA				
Goodwill	690		34	**724**
Brands	169		8	**177**
	859		42	**901**
Total goodwill	14,661	1,315	296	**16,272**
Total reacquired franchise rights	8,076	79	61	**8,216**

Total acquired franchise rights	1,792		22	**1,814**
Total brands	1,905	3,311	177	**5,393**
Total other	10			**10**
	$ 26,444	$ 4,705	$ 556	**$ 31,705**

(a) Net increases in 2011 relate primarily to our acquisition of WBD.

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Stock-Based Compensation

For the 12 weeks ended September 3, 2011, we recognized stock-based compensation expense of $77 million ($76 million recorded as stock-based compensation expense and $1 million included in merger and integration charges). For the 36 weeks ended September 3, 2011, we recognized stock-based compensation expense of $232 million ($222 million recorded as stock-based compensation expense and $10 million included in merger and integration charges). For the 12 weeks ended September 4, 2010, we recognized stock-based compensation expense of $77 million ($72 million recorded as stock-based compensation expense and $5 million included in merger and integration charges). For the 36 weeks ended September 4, 2010, we recognized stock-based compensation expense of $236 million ($191 million recorded as stock-based compensation expense and $45 million included in merger and integration charges).

For the 12 weeks ended September 3, 2011, our grants of stock options and restricted stock units (RSU) were nominal. For the 36 weeks ended September 3, 2011, we granted 6.8 million stock options at a weighted-average grant price of $64.28 and 5.2 million RSUs at a weighted-average grant price of $63.88, under the terms of our 2007 Long-Term Incentive Plan. For the 12 weeks ended September 4, 2010, our grants of stock options and RSUs were nominal. For the 36 weeks ended September 4, 2010, we granted 12.2 million stock options and 4.7 million RSUs at weighted-average grant prices of $66.50 and $66.46, respectively, under the terms of our 2007 Long-Term Incentive Plan.

Our weighted-average Black-Scholes fair value assumptions are as follows:

	36 Weeks Ended	
	9/3/11	9/4/10
Expected life	**6 yrs.**	5 yrs.
Risk free interest rate	**2.5%**	2.3%
Expected volatility[a]	**16%**	17%
Expected dividend yield	**2.9%**	2.8%

[a] Reflects movements in our stock price over the most recent historical period equivalent to the expected life.

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Pension and Retiree Medical Benefits

The components of net periodic benefit cost for pension and retiree medical plans are as follows:

	12 Weeks Ended					
	Pension				**Retiree Medical**	
	9/3/11	9/4/10	**9/3/11**	9/4/10	**9/3/11**	9/4/10
	U.S.		International			
Service cost	**$ 80**	$ 73	**$ 22**	$ 19	**$ 12**	$ 13
Interest cost	**127**	123	**28**	26	**20**	22
Expected return on plan assets	**(163)**	(158)	**(32)**	(31)	**(3)**	
Amortization of prior service cost/(benefit)	**3**	3	**1**	1	**(6)**	(5)
Amortization of experience loss	**34**	30	**10**	6	**2**	2
	81	71	**29**	21	**25**	32
Settlement/Curtailment gain						(62)
Total expense	**$ 81**	$ 71	**$ 29**	$ 21	**$ 25**	$ (30)

	36 Weeks Ended					
	Pension				**Retiree Medical**	
	9/3/11	9/4/10	**9/3/11**	9/4/10	**9/3/11**	9/4/10
	U.S.		International			
Service cost	**$ 242**	$ 203	**$ 62**	$ 52	**$ 35**	$ 39
Interest cost	**379**	341	**77**	70	**61**	65
Expected return on plan assets	**(487)**	(433)	**(89)**	(84)	**(10)**	
Amortization of prior service cost/(benefit)	**10**	8	**2**	2	**(19)**	(13)
Amortization of experience loss	**101**	80	**26**	16	**8**	4
	245	199	**78**	56	**75**	95
Settlement/Curtailment gain	**(9)**	(2)				(62)
Special termination benefits	**10**	23			**1**	1
Total expense	**$ 246**	$ 220	**$ 78**	$ 56	**$ 76**	$ 34

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Income Taxes

A rollforward of our reserves for all federal, state and foreign tax jurisdictions, is as follows:

	9/3/11	12/25/10
Balance, beginning of year	**$ 2,022**	$ 1,731
Additions for tax positions related to the current year	**143**	204
Additions for tax positions from prior years	**74**	517
Reductions for tax positions from prior years	**(66)**	(391)
Settlement payments	**(87)**	(30)
Statute of limitations expiration	**(3)**	(7)
Translation and other	**1**	(2)
Balance, end of period	**$ 2,084**	$ 2,022

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Net Income Attributable to PepsiCo per Common Share

The computations of basic and diluted net income attributable to PepsiCo per common share are as follows:

	12 Weeks Ended			
	9/3/11		9/4/10	
	Income	**Shares[a]**	Income	Shares[a]
Net income attributable to PepsiCo	**$2,000**		$1,922	
Preferred shares:				
Dividends				
Redemption premium	**(1)**			
Net income available for PepsiCo common shareholders	**$1,999**	**1,578**	$1,922	1,588
Basic net income attributable to PepsiCo per common share	**$1.27**		$1.21	
Net income available for PepsiCo common shareholders	**$1,999**	**1,578**	$1,922	1,588
Dilutive securities:				
Stock options and RSUs[b]		**20**		23
ESOP convertible preferred stock	**1**	**1**		1
Diluted	**$2,000**	**1,599**	$1,922	1,612
Diluted net income attributable to PepsiCo per common share	**$1.25**		$1.19	

	36 Weeks Ended			
	9/3/11		9/4/10	
	Income	**Shares[a]**	Income	Shares[a]
Net income attributable to PepsiCo	**$ 5,028**		$ 4,955	
Preferred shares:				
Dividends	**(1)**		(1)	
Redemption premium	**(4)**		(2)	
Net income available for PepsiCo common shareholders	**$ 5,023**	**1,581**	$ 4,952	1,593
Basic net income attributable to PepsiCo per common share	**$ 3.18**		$ 3.11	
Net income available for PepsiCo common shareholders	**$ 5,023**	**1,581**	$ 4,952	1,593
Dilutive securities:				
Stock options and RSUs[b]		**21**		24
ESOP convertible preferred stock	**5**	**1**	3	1
Diluted	**$ 5,028**	**1,603**	$ 4,955	1,618

Diluted net income attributable to PepsiCo per common share	**$ 3.14**	$ 3.06

(a) Weighted-average common shares outstanding (in millions).

(b) Options to purchase 22.1 million and 21.2 million shares, respectively, for the 12 and 36 weeks in 2011 were not included in the calculation of earnings per share because these options were out-of-the-money. These out-of-the-money options had average exercise prices of $67.67 and $67.46, respectively. Options to purchase 31.9 million and 25.1 million shares, respectively, for the 12 and 36 weeks in 2010 were not included in the calculation of earnings per share because these options were out-of-the-money. Out-of-the-money options for the 12 and 36 weeks in 2010 had average exercise prices of $66.85 and $67.13, respectively.

Debt Obligations and Commitments

In the second quarter of 2011, we issued $750 million of floating rate notes maturing in 2013, which bear interest at a rate equal to the three-month London Inter-Bank Offered Rate (LIBOR) plus 8 basis points, and $1.0 billion of 2.500% senior notes maturing in 2016. The net proceeds from the issuance of these notes were used for general corporate purposes.

In the third quarter of 2011, we issued $500 million of 0.800% senior notes maturing in 2014 and $750 million of 3.000% senior notes maturing in 2021. The net proceeds from the issuance of these notes will be used for general corporate purposes.

In the third quarter of 2011, we entered into a new four-year unsecured revolving credit agreement (Four-Year Credit Agreement) which expires in June 2015. Effective August 8, 2011, commitments under this agreement were increased to enable us to borrow up to $2.925 billion, subject to customary terms and conditions. We may request to increase the commitments under this agreement to up to $3.5 billion. Additionally, we may, once a year, request renewal of the agreement for an additional one-year period.

Also, in the third quarter of 2011, we entered into a new 364-day unsecured revolving credit agreement (364-Day Credit Agreement) which expires in June 2012. Effective August 8, 2011, commitments under this agreement were increased to enable us to borrow up to $2.925 billion, subject to customary terms and conditions. We may request to increase the commitments under this agreement to up to $3.5 billion. We may request renewal of this facility for an additional 364-day period or convert any amounts outstanding into a term loan for a period of up to one year, which would mature no later than June 2013.

The Four-Year Credit Agreement and the 364-Day Credit Agreement, together replaced our $2 billion unsecured revolving credit agreement, our $2.575 billion 364-day unsecured revolving credit agreement and our $1.080 billion amended PBG credit facility. Funds borrowed under the Four-Year Credit Agreement and the 364-Day Credit Agreement may be used for general corporate purposes, including but not limited to repayment of outstanding commercial paper issued by us and our subsidiaries, working capital, capital investments and/or acquisitions.

In the third quarter of 2011, we paid $784 million in a cash tender offer to repurchase $766 million (aggregate principal amount) of certain WBD debt obligations. As a result of this debt repurchase, we recorded a $16 million charge to interest expense in the third quarter, primarily representing the premium paid in the tender offer.

As of September 3, 2011, we had $2.8 billion of commercial paper outstanding.

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Long-Term Contractual Commitments[a]

	Payments Due by Period				
	Total	2011	2012 2013	2014 2015	2016 and beyond
Long-term debt obligations[b]	$ 21,226	$	$ 4,043	$ 4,866	$ 12,317
Interest on debt obligations[c]	7,538	244	1,564	1,161	4,569
Operating leases	1,942	154	755	435	598
Purchasing commitments	3,198	567	2,089	451	91
Marketing commitments	2,501	53	573	539	1,336
	$ 36,405	$ 1,018	$ 9,024	$ 7,452	$ 18,911

(a) Reflects non-cancelable commitments as of September 3, 2011 based on foreign exchange rates in effect on that date and excludes any reserves for uncertain tax positions as we are unable to reasonably predict the ultimate amount or timing of settlement.

(b) Excludes $1.5 billion related to current maturities of long-term debt, as well as $555 million related to the fair value step-up of debt acquired in connection with our acquisitions of PBG and PAS.

(c) Interest payments on floating-rate debt are estimated using interest rates effective as of September 3, 2011.

Most long-term contractual commitments, except for our long-term debt obligations, are not recorded on our balance sheet. Non-cancelable operating leases primarily represent building leases. Non-cancelable purchasing commitments are primarily for packaging materials, sugar and other sweeteners, oranges and orange juice. Non-cancelable marketing commitments are primarily for sports marketing. Bottler funding to independent bottlers is not reflected in our long-term contractual commitments as it is negotiated on an annual basis. Accrued liabilities for pension and retiree medical plans are not reflected in our long-term contractual commitments because they do not represent expected future cash outflows. See *Pension and Retiree Medical Benefits* for additional information regarding our pension and retiree medical obligations.

Merger and Integration Charges

In the 12 weeks ended September 3, 2011, we incurred merger and integration charges of $61 million ($53 million after-tax or $0.03 per share) related to our acquisitions of PBG, PAS and WBD, including $24 million recorded in the PAB segment, $11 million recorded in the Europe segment, $10 million recorded in corporate unallocated expenses and $16 million recorded in interest expense. In the 36 weeks ended September 3, 2011, we incurred merger and integration charges of $174 million ($147 million after-tax or $0.09 per share) related to our acquisitions of PBG, PAS and WBD, including $77 million recorded in the PAB segment, $17 million recorded in the Europe segment, $64 million recorded in corporate unallocated expenses and $16 million recorded in interest expense. All of these net charges, other than the interest expense portion, were recorded in selling, general and administrative expenses. These charges also include closing costs and advisory fees related to our acquisition of WBD. Substantially all cash payments related to the above charges are expected to be paid by the end of 2011.

In the 12 weeks ended September 4, 2010, we incurred merger and integration charges of $69 million related to our acquisitions of PBG and PAS, including $38 million recorded in the PAB segment, $15 million recorded in the Europe segment and $16 million recorded in corporate unallocated expenses. In the 36 weeks ended September 4, 2010, we incurred merger and

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integration charges of $536 million related to our acquisitions of PBG and PAS, including $334 million recorded in the PAB segment, $44 million recorded in the Europe segment, $128 million recorded in corporate unallocated expenses and $30 million recorded in interest expense. All of these charges, other than the interest expense portion, were recorded in selling, general and administrative expenses. These charges also include closing costs, one-time financing costs and advisory fees related to our acquisitions of PBG and PAS. In addition, in the first quarter of 2010, we recorded $9 million of charges, representing our share of the respective merger costs of PBG and PAS, in bottling equity income. Substantially all cash payments related to the above charges are expected to be paid by the end of 2011. In total, these charges had an after-tax impact of $51 million ($0.03 per share) and $431 million ($0.27 per share) for the 12 and 36 weeks ended September 4, 2010, respectively.

A summary of our merger and integration activity in 2011 is as follows:

	Severance and Other Employee Costs	Other Costs	Total
Liability as of December 25, 2010	$ 179	$ 25	$ 204
2011 merger and integration charges	54	120	174
Cash payments	(148)	(145)	(293)
Non-cash charges	(20)	7	(13)
Liability as of September 3, 2011	$ 65	$ 7	$ 72

Financial Instruments

We are exposed to market risks arising from adverse changes in:

- commodity prices, affecting the cost of our raw materials and energy,
- foreign exchange risks, and
- interest rates.

In the normal course of business, we manage these risks through a variety of strategies, including the use of derivatives. Certain derivatives are designated as either cash flow or fair value hedges and qualify for hedge accounting treatment, while others do not qualify and are marked to market through earnings. Ineffectiveness of our hedges is not material. We do not use derivative instruments for trading or speculative purposes. We perform assessments of our counterparty credit risk regularly, including a review of credit ratings, credit default swap rates and potential nonperformance of the counterparty. Based on our most recent assessment of our counterparty credit risk, we consider this risk to be low. In addition, we enter into derivative contracts with a variety of financial institutions that we believe are creditworthy in order to reduce our concentration of credit risk.

Commodity Prices

We are subject to commodity price risk because our ability to recover increased costs through higher pricing may be limited in the competitive environment in which we operate. This risk is managed through the use of fixed-price purchase orders, pricing agreements, geographic diversity and derivatives. We use derivatives, primarily with terms of no more than three years, to economically hedge price fluctuations related to a portion of our anticipated commodity purchases, primarily for aluminum, fuel and natural gas. For those derivatives that qualify for hedge accounting, any ineffectiveness is recorded immediately in corporate unallocated expenses. We classify both the earnings and cash flow impact from these derivatives consistent with the underlying hedged item. During the next 12 months, we expect to reclassify net gains of $2 million related to these hedges from accumulated other comprehensive loss into net income. Derivatives used to hedge commodity price risk that do not qualify for hedge accounting are marked to market each period and reflected in our income statement.

Our open commodity derivative contracts that qualify for hedge accounting had a face value of $586 million as of September 3, 2011 and $577 million as of September 4, 2010. These contracts resulted in net unrealized gains of $11 million as of September 3, 2011 and $7 million as of September 4, 2010.

Our open commodity derivative contracts that do not qualify for hedge accounting had a face value of $537 million as of September 3, 2011 and $254 million as of September 4, 2010. These contracts resulted in net losses of $6 million as of September 3, 2011 and $3 million as of September 4, 2010.

Foreign Exchange

Financial statements of foreign subsidiaries are translated into U.S. dollars using period-end exchange rates for assets and liabilities and weighted-average exchange rates for revenues and expenses. Adjustments resulting from translating net assets are reported as a separate component of accumulated other comprehensive loss within common shareholders equity as currency translation adjustment.

We may enter into derivatives, primarily forward contracts with terms of no more than two years, to manage our exposure to foreign currency transaction risk. Exchange rate gains or losses related to foreign currency transactions are recognized as transaction gains or losses in our income statement as incurred.

Our foreign currency derivatives had a total face value of $2.5 billion as of September 3, 2011 and $1.4 billion as of September 4, 2010. The contracts that qualify for hedge accounting resulted in net unrealized losses of $11 million as of September 3, 2011 and $5 million as of September 4, 2010. During the next 12 months, we expect to reclassify net losses of $10 million related to these hedges from accumulated other comprehensive loss into net income. The contracts that do not qualify for hedge accounting resulted in net losses of $14 million as of September 3, 2011 and a net gain of $1 million as of September 4, 2010. All losses and gains were offset by changes in the underlying hedged items, resulting in no net material impact on earnings.

Interest Rates

We centrally manage our debt and investment portfolios considering investment opportunities and risks, tax consequences and overall financing strategies. We use various interest rate derivative instruments including, but not limited to, interest rate swaps, cross currency interest rate swaps, Treasury locks and swap locks to manage our overall interest expense and foreign exchange risk. These instruments effectively change the interest rate and currency of specific debt issuances. Certain of our fixed rate indebtedness has been swapped to floating rates. The notional amount, interest payment and maturity date of the interest rate and cross-currency swaps match the principal, interest payment and maturity date of the related debt. Our Treasury locks and swap locks are entered into to protect against unfavorable interest rate changes relating to forecasted debt transactions.

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The notional amounts of the interest rate derivative instruments outstanding as of September 3, 2011 and September 4, 2010 were $8.9 billion and $9.2 billion, respectively. For those interest rate derivative instruments that qualify for cash flow hedge accounting, any ineffectiveness is recorded immediately. We classify both the earnings and cash flow impact from these interest rate derivative instruments consistent with the underlying hedged item. During the next 12 months, we expect to reclassify net losses of $16 million related to these hedges from accumulated other comprehensive loss into net income.

As of September 3, 2011, approximately 40% of total debt, after the impact of the related interest rate derivative instruments, was exposed to variable rates, compared to 43% as of December 25, 2010.

Fair Value Measurements

The fair values of our financial assets and liabilities as of September 3, 2011 and September 4, 2010 are categorized as follows:

	2011		2010	
	Assets[(a)]	**Liabilities[(a)]**	Assets[(a)]	Liabilities[(a)]
Available-for-sale securities[(b)]	**$ 61**	**$**	$ 88	$
Short-term investments index funds[(c)]	**$ 159**	**$**	$ 147	$
Deferred compensation[(d)]	**$**	**$ 519**	$	$ 553
Derivatives designated as hedging instruments:				
Forward exchange contracts[(e)]	**$ 12**	**$ 23**	$ 19	$ 24
Interest rate derivatives[(f)]	**428**	**56**	402	91
Commodity contracts other[(g)]	**27**	**16**	45	12
Commodity contracts futures[(h)]	**1**	**1**	1	27
	$ 468	**$ 96**	$ 467	$ 154
Derivatives not designated as hedging instruments:				
Forward exchange contracts[(e)]	**$ 5**	**$ 19**	$ 6	$ 5
Interest rate derivatives[(f)]	**104**	**140**	56	97
Commodity contracts other[(g)]	**24**	**29**	6	8
Commodity contracts futures[(h)]		**1**		1
Prepaid forward contracts[(i)]	**38**		48	
	$ 171	**$ 189**	$ 116	$ 111
Total derivatives at fair value	**$ 639**	**$ 285**	$ 583	$ 265
Total	**$ 859**	**$ 804**	$ 818	$ 818

(a) Financial assets are classified on our balance sheet within other assets, with the exception of short-term investments. Financial liabilities are classified on our balance sheet within other current liabilities and other liabilities. Unless specifically indicated, all financial assets and liabilities are categorized as Level 2 assets or liabilities.

(b) Based on the price of common stock. Categorized as a Level 1 asset.

(c) Based on price changes in index funds used to manage a portion of market risk arising from our deferred compensation liability. Categorized as a Level 1 asset.

(d) Based on the fair value of investments corresponding to employees investment elections. As of September 3, 2011 and September 4, 2010, $43 million and $147 million, respectively, are categorized as Level 1 liabilities. The remaining balances are categorized as Level 2 liabilities.

(e) Based on observable market transactions of spot and forward rates.

(f) Based on LIBOR and recently reported transactions in the marketplace.

(g) Based on recently reported transactions in the mar