

Fitch Affirms PepsiCo's IDRs at 'A/F1'; Outlook Stable

Written by Australian Business

CHICAGO--([BUSINESS WIRE](#))--Fitch Ratings has affirmed the ratings of PepsiCo, Inc. (PepsiCo), Pepsi-Cola Metropolitan Bottling Company, Inc., and Bottling Group, LLC as follows:

PepsiCo (Parent)

--Long-term Issuer Default Rating (IDR) at 'A';

--Senior unsecured debt at 'A';

--Bank credit facilities at 'A';

--Short-term IDR at 'F1';

--Commercial paper program at 'F1'.

Pepsi-Cola Metropolitan Bottling Company, Inc. (Operating Holding Co.)	Company/Intermediate
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--Long-term IDR at 'A';

--Guaranteed senior notes at 'A'.

Bottling Group, LLC (Operating Company)

--Long-term IDR at 'A';

--Guaranteed senior notes at 'A'.

The Rating Outlook is Stable. PepsiCo had approximately \$29.5 billion of debt at Sept. 7, 2013.

KEY RATING DRIVERS:

PepsiCo's ratings reflect its considerable financial flexibility, substantial cash flow, significant scale, product diversification, increasing exposure to faster growing emerging markets, and position as the world's second largest food and beverage company. PepsiCo's \$66.4 billion of net revenue in the latest 12 month (LTM) period was split approximately 51% food / 49% beverages. Roughly 50% of PepsiCo's revenues are generated outside of the United States with emerging or developing markets representing a little over one-third of the total revenues.

PepsiCo's brand strength is demonstrated by its portfolio that consists of 22 brands; including Pepsi, Gatorade, Lay's, Doritos, and Quaker, with more than \$1 billion in annual retail sales that are typically No. 1 or No. 2 in their respective categories. PepsiCo also has over 40 brands with between \$250 million to \$1 billion in sales. PepsiCo's financial profile is supported by the strong cash generation derived from its brand strength. Annual cash flow from operations and free cash flow (FCF) have averaged \$8.6 billion and \$2.4 billion, respectively for the past three years. Fitch expects PepsiCo to generate in excess of \$9 billion in CFO and at least \$2.6 billion in FCF for 2013.

PepsiCo's financial strategy, which has historically been viewed as aggressive, is also factored into ratings. PepsiCo's primary goals are investing in its business, returning cash to shareholders and maintaining credit ratings that provide ready access to global capital and credit markets. Share buybacks have averaged a net \$2.5 billion per year since 2010. In the first quarter of 2013, PepsiCo approved a new share repurchase program, for up to \$10 billion of PepsiCo common stock from July 2013 through June 2016. Dividends have

grown annually by 6% or more over the past several years to approximately \$3.4 billion during the LTM period. PepsiCo anticipates dividends and share repurchases will total approximately \$6.4 billion in 2013.

PepsiCo's challenges include global concerns with health and wellness trends, its mature developed markets and sentiment toward artificial sweeteners that has grown increasingly negative during 2013 with diet CSD declines accelerating in the U.S. Several of PepsiCo's developed markets are more mature with stagnant or declining per capita consumption trends, weak economies and/or low population growth. This places more dependence on growth in emerging markets and on new product innovation thus likely increasing the firm's longer-term operating risk.

PepsiCo maintains a good breadth of products across its beverage segment with strong positions in its non-carbonated soft drinks to balance the declines within its CSD portfolio. However, PepsiCo and the rest of the industry must successfully develop new beverage products that are healthier, natural sweetener based with lower calorie options to evolve their portfolios. Fitch anticipates that innovation will not fully ameliorate the continued expected declines in some developed markets due to changing habits that are causing some consumers to leave the carbonated soft drink category and seek out healthier options.

Operationally, PepsiCo is focused on increasing brand support to grow market share, expanding its emerging market presence, growing its nutrition business, reducing overhead, and leveraging technology and processes across its organization. PepsiCo has made noticeable progress on this strategy. Fitch believes PepsiCo's strategic initiatives should help the company improve trends. Brand building efforts have helped offset beverage volume declines in North America as consolidated volumes were flat and pricing increased 4% for the 36 weeks ended Sept. 7, 2013. PepsiCo's core operating profit increased 8% year-to-date to \$7.3 billion driven by gains in Frito-Lay North America and Latin America Foods that more than offset weakness in certain segments including Europe and Quaker Foods North America.

Credit Statistics:

For the LTM period ended Sept. 7, 2013, total debt-to-operating EBITDA was 2.3x, operating EBITDA-to-gross interest expense was 13.5x, and FFO adjusted leverage was

3.2x. PepsiCo's leverage is modestly higher than similarly rated food and beverage companies but ratings are supported by, as mentioned previously, the company's substantial and stable FCF, significant scale, diversification, and brand leadership. Fitch anticipates potential restructuring actions could include a spin-out of at least its North American bottling operations with an accompanied reduction in debt and leverage. Absent any long-term debt reductions, Fitch believes downside ratings risk is present particularly if beverage segment operating trends weaken globally.

Fitch's ratings reflect expectations that total debt-to-operating EBITDA leverage to remain in the low 2.0x range. Moreover, PepsiCo's cash flow growth should benefit from its strategic initiatives around brand support and productivity as savings are realized. PepsiCo's 2013 operating cash flow will be much less affected by pension and retirement medical plan contributions. PepsiCo expects to make contributions of approximately \$240 million in 2013 compared to payments of almost \$1.5 billion in 2012.

Liquidity, Covenants, and Maturities:

PepsiCo maintains good liquidity. As of Sept. 7, 2013, the firm had \$9.6 billion of cash and short-term investments, with \$8.6 billion of the cash offshore, and combined capacity of \$5.85 billion under its 364-day and five-year revolving credit facilities. PepsiCo's revolvers expire in June 2014 and June 2018, respectively, and are not bound by financial covenants. Fitch recognizes that repatriation of cash could result in incremental taxes but believes PepsiCo would more likely use the cash to grow in overseas markets. At Sept. 7, 2013, debt due within the next year totaled \$3.3 billion. Upcoming maturities of long-term debt are \$4.1 billion in 2014 and 2015 and \$4.4 billion in 2016 and 2017. PepsiCo had issued \$2 billion in commercial paper.

PepsiCo guarantees all of the senior notes of its bottling subsidiaries - Pepsi-Cola Metropolitan Bottling Company (wholly owned by PepsiCo; Metropolitan Bottling) and Bottling Group, LLC (wholly owned by PMBC). While the notes of Metropolitan Bottling and Bottling Group, LLC are structurally superior to the notes issued by PepsiCo, Inc., Fitch has chosen not to make a distinction in the ratings at the single-A level as default risk is very low.

RATING SENSITIVITIES

Future developments that may, individually or collectively, lead to a positive rating action include:

--Total debt-to-operating EBITDA below 2.0x and Fitch's belief that PepsiCo would manage its balance sheet to sustain an 'A+' rating.

Future developments that may, individually or collectively, lead to a negative rating action include:

--Significant debt-financed acquisitions and/or deteriorating operating performance that causes total debt-to-operating EBITDA to be sustained above the mid 2.0x level;

--Substantial and sustained declines in cash flow would also likely prompt negative rating actions;

Financial policy changes including higher level of share repurchases or dividends that would increase financial leverage;

--Event risk related to any potential restructuring actions that PepsiCo currently has under consideration that would result in higher leverage.

Additional information is available at ' www.fitchratings.com '.

Applicable Criteria and Related Research:

--'Corporate Rating Methodology' (Aug. 5, 2013).

Applicable Criteria and Related Research:

Corporate Rating Methodology: Including Short-Term Ratings and Parent and Subsidiary Linkage

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=715139

Additional Disclosure

Solicitation Status

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