KELLOGG CO
Form 10-Q
May 11, 2015
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended April 4, 2015

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 1-4171

KELLOGG COMPANY

State of Incorporation Delaware IRS Employer Identification No.38-0710690
One Kellogg Square, P.O. Box 3599, Battle Creek, MI 49016-3599

Registrant s telephone number: 269-961-2000

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 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 ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

Common Stock outstanding as of May 2, 2015 352,898,107 shares

Table of Contents

KELLOGG COMPANY

INDEX

	Page
PART I Financial Information	
Item 1: Financial Statements	
Consolidated Balance Sheet April 4, 2015 and January 3, 2015	3
Consolidated Statement of Income quarters ended April 4, 2015 and March 29, 2014	4
Consolidated Statement of Comprehensive Income quarters ended April 4, 2015 and March 29, 2014	5
Consolidated Statement of Equity year ended January 3, 2015 and quarter ended April 4, 2015	6
Consolidated Statement of Cash Flows quarters ended April 4, 2015 and March 29, 2014	7
Notes to Consolidated Financial Statements	8
Item 2: Management s Discussion and Analysis of Financial Condition and Results of Operations	26
Item 3: Quantitative and Qualitative Disclosures about Market Risk	40
Item 4: Controls and Procedures	41
PART II Other Information	
Item 1A: Risk Factors	42
Item 2: Unregistered Sales of Equity Securities and Use of Proceeds	42
Item 6: Exhibits	42
Signatures	43
Exhibit Index	44

Table of Contents

Part I FINANCIAL INFORMATION

Item 1. Financial Statements.

Kellogg Company and Subsidiaries

CONSOLIDATED BALANCE SHEET

(millions, except per share data)

	April 4, 2015 (unaudited)	January 3, 2015 *
Current assets		
Cash and cash equivalents	**$ 349**	$ 443
Accounts receivable, net	**1,503**	1,276
Inventories:		
Raw materials and supplies	**353**	327
Finished goods and materials in process	**846**	952
Deferred income taxes	**170**	184
Other prepaid assets	**220**	158
Total current assets	**3,441**	3,340
Property, net of accumulated depreciation of $5,466 and $5,526	**3,719**	3,769
Goodwill	**4,993**	4,971
Other intangibles, net of accumulated amortization of $45 and $43	**2,282**	2,295
Pension	**254**	250
Other assets	**519**	528
Total assets	**$ 15,208**	$ 15,153
Current liabilities		
Current maturities of long-term debt	**$ 360**	$ 607
Notes payable	**809**	828
Accounts payable	**1,537**	1,528
Accrued advertising and promotion	**453**	446
Accrued income taxes	**72**	39
Accrued salaries and wages	**226**	320
Other current liabilities	**543**	596
Total current liabilities	**4,000**	4,364
Long-term debt	**6,561**	5,935
Deferred income taxes	**764**	726
Pension liability	**760**	777
Nonpension postretirement benefits	**75**	82
Other liabilities	**396**	418

Commitments and contingencies		
Equity		
Common stock, $.25 par value	**105**	105
Capital in excess of par value	**689**	678
Retained earnings	**6,739**	6,689
Treasury stock, at cost	**(3,696)**	(3,470)
Accumulated other comprehensive income (loss)	**(1,291)**	(1,213)
Total Kellogg Company equity	**2,546**	2,789
Noncontrolling interests	**106**	62
Total equity	**2,652**	2,851
Total liabilities and equity	**$ 15,208**	$ 15,153

* Condensed from audited financial statements.
Refer to Notes to Consolidated Financial Statements.

Table of Contents

Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF INCOME

(millions, except per share data)

(Results are unaudited)	Quarter ended April 4, 2015	Quarter ended March 29, 2014
Net sales	**$ 3,556**	$ 3,742
Cost of goods sold	**2,311**	2,238
Selling, general and administrative expense	**861**	890
Operating profit	**384**	614
Interest expense	**54**	52
Other income (expense), net	**(26)**	10
Income before income taxes	**304**	572
Income taxes	**76**	165
Earnings (loss) from joint ventures	**(1)**	(1)
Net income	**$ 227**	$ 406
Net income (loss) attributable to noncontrolling interests		
Net income attributable to Kellogg Company	**$ 227**	$ 406
Per share amounts:		
Basic	**$ 0.64**	$ 1.13
Diluted	**$ 0.64**	$ 1.12
Dividends per share	**$ 0.490**	$ 0.460
Average shares outstanding:		
Basic	**355**	360
Diluted	**357**	362
Actual shares outstanding at period end	**353**	358

Refer to Notes to Consolidated Financial Statements.

Table of Contents

Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(millions)

	Quarter ended April 4, 2015		
(Results are unaudited)	**Pre-tax amount**	**Tax (expense) benefit**	**After-tax amount**
Net income			**$ 227**
Other comprehensive income (loss):			
Foreign currency translation adjustments	**(62)**	**(21)**	**(83)**
Cash flow hedges:			
Unrealized gain (loss) on cash flow hedges	**8**	**(1)**	**7**
Reclassification to net income	**(4)**		**(4)**
Postretirement and postemployment benefits:			
Amount arising during the period:			
Prior service credit (cost)	**(1)**		**(1)**
Reclassification to net income:			
Net experience loss	**1**		**1**
Prior service cost	**3**	**(1)**	**2**
Other comprehensive income (loss) attributable to Kellogg Company	**$ (55)**	**$ (23)**	**$ (78)**
Comprehensive income attributable to noncontrolling interests			**(1)**
Comprehensive income			**$ 148**

	Quarter ended March 29, 2014		
(Results are unaudited)	Pre-tax amount	Tax (expense) benefit	After-tax amount
Net income			$ 406
Other comprehensive income (loss):			
Foreign currency translation adjustments	3		3
Cash flow hedges:			
Unrealized gain (loss) on cash flow hedges	(1)		(1)
Reclassification to net income	(10)	3	(7)
Postretirement and postemployment benefits:			
Reclassification to net income:			
Net experience loss	1		1
Prior service cost	2	(1)	1
Other comprehensive income (loss) attributable to Kellogg Company	$ (5)	$ 2	$ (3)
Comprehensive income			$ 403

Refer to Notes to Consolidated Financial Statements.

Table of Contents

Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF EQUITY

(millions)

(unaudited)	Common stock shares	Common stock amount	Capital in excess of par value	Retained earnings	Treasury stock shares	Treasury stock amount	Accumulated other comprehensive income (loss)	Total Kellogg Company equity	Non-controlling interests	Total equity	Total comprehensive income (loss)
Balance, December 28, 2013	420	$ 105	$ 626	$ 6,749	57	$ (2,999)	$ (936)	$ 3,545	$ 62	$ 3,607	
Common stock repurchases					11	(690)		(690)		(690)	
Net income				632				632	1	633	633
Dividends				(680)				(680)	(1)	(681)	
Other comprehensive loss							(277)	(277)		(277)	(277)
Stock compensation			29					29		29	
Stock options exercised and other			23	(12)	(4)	219		230		230	
Balance, January 3, 2015	420	$ 105	$ 678	$ 6,689	64	$ (3,470)	$ (1,213)	$ 2,789	$ 62	$ 2,851	$ 356
Common stock repurchases					4	(285)		(285)		(285)	
Acquisition of noncontrolling interest									20	20	
Net income				227				227		227	227
Dividends				(174)				(174)		(174)	
Other comprehensive loss							(78)	(78)	(1)	(79)	(79)
Stock compensation			10					10		10	
Stock options exercised and other			1	(3)	(1)	59		57	25	82	
Balance, April 4, 2015	**420**	**$ 105**	**$ 689**	**$ 6,739**	**67**	**$ (3,696)**	**$ (1,291)**	**$ 2,546**	**$ 106**	**$ 2,652**	**$ 148**

Refer to notes to Consolidating Financial Statements.

Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF CASH FLOWS

(millions)

	Year-to-date period ended	
(unaudited)	**April 4, 2015**	March 29, 2014
Operating activities		
Net income	**$ 227**	$ 406
Adjustments to reconcile net income to operating cash flows:		
Depreciation and amortization	**131**	116
Postretirement benefit plan expense (benefit)	**(21)**	(22)
Deferred income taxes	**(2)**	45
Other	**57**	6
Postretirement benefit plan contributions	**(12)**	(28)
Changes in operating assets and liabilities, net of acquisitions:		
Trade receivables	**(240)**	(195)
Inventories	**70**	(29)
Accounts payable	**27**	(49)
Accrued income taxes	**33**	76
Accrued interest expense	**17**	45
Accrued and prepaid advertising, promotion and trade allowances	**(12)**	(9)
Accrued salaries and wages	**(88)**	(84)
All other current assets and liabilities	**(92)**	(10)
Net cash provided by (used in) operating activities	**95**	268
Investing activities		
Additions to properties	**(83)**	(97)
Acquisitions, net of cash acquired	**(117)**	
Other	**3**	(2)
Net cash provided by (used in) investing activities	**(197)**	(99)
Financing activities		
Net issuances (reductions) of notes payable	**(19)**	986
Issuances of long-term debt	**672**	
Reductions of long-term debt	**(243)**	(682)
Net issuances of common stock	**57**	37
Common stock repurchases	**(285)**	(321)
Cash dividends	**(174)**	(166)
Other	**5**	(1)
Net cash provided by (used in) financing activities	**13**	(147)

Effect of exchange rate changes on cash and cash equivalents	**(5)**	(11)
Increase (decrease) in cash and cash equivalents	**(94)**	11
Cash and cash equivalents at beginning of period	**443**	273
Cash and cash equivalents at end of period	**$ 349**	$ 284

Refer to Notes to Consolidated Financial Statements.

Notes to Consolidated Financial Statements

for the quarter ended April 4, 2015 (unaudited)

Note 1 Accounting policies

Basis of presentation

The unaudited interim financial information of Kellogg Company (the Company) included in this report reflects normal recurring adjustments that management believes are necessary for a fair statement of the results of operations, comprehensive income, financial position, equity and cash flows for the periods presented. This interim information should be read in conjunction with the financial statements and accompanying footnotes within the Company s 2014 Annual Report on Form 10-K.

The condensed balance sheet data at January 3, 2015 was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States. The results of operations for the quarterly period ended April 4, 2015 are not necessarily indicative of the results to be expected for other interim periods or the full year.

Accounts payable

Beginning in 2014, the Company has an agreement with a third party to provide an accounts payable tracking system which facilitates participating suppliers ability to monitor and, if elected, sell payment obligations from the Company to designated third-party financial institutions. Participating suppliers may, at their sole discretion, make offers to sell one or more payment obligations of the Company prior to their scheduled due dates at a discounted price to participating financial institutions. The Company s goal in entering into this agreement is to capture overall supplier savings, in the form of pricing, payment terms or vendor funding, created by facilitating suppliers ability to sell payment obligations, while providing them with greater working capital flexibility. We have no economic interest in the sale of these suppliers receivables and no direct financial relationship with the financial institutions concerning these services. The Company s obligations to its suppliers, including amounts due and scheduled payment dates, are not impacted by suppliers decisions to sell amounts under this arrangement. However, the Company s right to offset balances due from suppliers against payment obligations is restricted by this agreement for those payment obligations that have been sold by suppliers. As of April 4, 2015, $261 million of the Company s outstanding payment obligations had been placed in the accounts payable tracking system, and participating suppliers had sold $212 million of those payment obligations to participating financial institutions. As of January 3, 2015, $236 million of the Company s outstanding payment obligations had been placed in the accounts payable tracking system, and participating suppliers had sold $184 million of those payment obligations to participating financial institutions.

Accounting standards to be adopted in future periods

In April 2015, the Financial Accounting Standards Board (FASB) issued an Accounting Standards Update (ASU) to simplify the presentation of debt issuance costs. The ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. Early adoption is permitted. Entities should apply the new guidance on a retrospective basis. The Company will adopt the updated standard in the first quarter of 2016. The Company does not expect the adoption of this guidance to have a significant impact on its financial statements.

In April 2015, the FASB issued an ASU to provide a practical expedient for the measurement date of an employer s defined benefit obligation and plan assets. For an entity with a fiscal year-end that does not coincide with a month-end, the amendments in this Update provide a practical expedient that permits the entity to measure defined benefit plan assets and obligations using the month-end that is closest to the entity s fiscal year-end and apply that practical expedient consistently to all plans from year to year. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. Early adoption is permitted. Entities should apply the new guidance on a prospective basis. The Company will early adopt the updated standard when measuring the fair value of plan assets at the end of its 2015 fiscal year. The Company does not expect the adoption of this guidance to have a significant impact on its financial statements.

In April 2015, the FASB issued an ASU to help entities evaluate the accounting for fees paid by a customer in a cloud computing arrangement. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. Early adoption is permitted. Entities should apply the new guidance either; 1) prospectively to all arrangements entered into or materially modified after the effective date or 2) retrospectively. The Company will adopt the updated standard prospectively in the first quarter of 2016. The Company does not expect the adoption of this guidance to have a significant impact on its financial statements.

Table of Contents

In May 2014, the FASB issued an ASU which provides guidance for accounting for revenue from contracts with customers. The core principle of this ASU is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration the entity expects to be entitled to in exchange for those goods or services. To achieve that core principle, an entity would be required to apply the following five steps: 1) identify the contract(s) with a customer; 2) identify the performance obligations in the contract; 3) determine the transaction price; 4) allocate the transaction price to the performance obligations in the contract and 5) recognize revenue when (or as) the entity satisfies a performance obligation. When the ASU was originally issued it was effective for fiscal years, and interim periods within those years, beginning after December 15, 2016, and early adoption was not permitted. On April 29, 2015, the FASB issued an exposure draft of a proposed ASU that would delay the effective date of the new revenue standard by one year. Under the proposal, the updated standard will be effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. Entities will be permitted to adopt the new revenue standard early, but not before the original effective date. Comments on the proposal are due by May 29, 2015. Entities will have the option to apply the final standard retrospectively or use a modified retrospective method, recognizing the cumulative effect of the ASU in retained earnings at the date of initial application. An entity will not restate prior periods if it uses the modified retrospective method, but will be required to disclose the amount by which each financial statement line item is affected in the current reporting period by the application of the ASU as compared to the guidance in effect prior to the change, as well as reasons for significant changes. The Company will adopt the updated standard in the first quarterly reporting period after it becomes effective. The Company is currently evaluating the impact that implementing this ASU will have on its financial statements and disclosures, as well as whether it will use the retrospective or modified retrospective method of adoption.

Note 2 Goodwill and other intangible assets

Bisco Misr acquisition

In January 2015, the Company completed its acquisition of a majority interest in Bisco Misr, the number one packaged biscuits company in Egypt for $125 million, or $117 million net of cash and cash equivalents acquired. The acquisition was accounted for under the purchase method and was financed through cash on hand. The assets and liabilities of Bisco Misr are included in the Consolidated Balance Sheet as of April 4, 2015 and the results of its operations subsequent to the acquisition date, which are immaterial, are included in the Consolidated Statement of Income within the Europe operating segment. In addition, the pro-forma effect of this acquisition if the acquisition had been completed at the beginning of 2014 would have been immaterial.

The acquired assets and assumed liabilities include the following:

(millions)	**January 18, 2015**
Current assets	$ 11
Property	79
Goodwill	58
Intangible assets and other	30
Current liabilities	(14)
Other non current liabilities, primarily deferred taxes	(27)
Non-controlling interests	(20)
	$ 117

Goodwill, which is not expected to be deductible for statutory tax purposes, is calculated as the excess of the purchase price over the fair value of the net assets recognized. The goodwill recorded primarily reflects the value of providing an established platform to leverage the Company s existing brands in the markets served by Bisco Misr as well as any intangible assets that do not qualify for separate recognition. The above amounts represent the preliminary allocation of purchase price and are subject to revision when appraisals are finalized, which is expected to occur by the first quarter of 2016.

Table of Contents

Carrying amount of goodwill

(millions)	U.S. Morning Foods	U.S. Snacks	U.S. Specialty	North America Other	Europe	Latin America	Asia Pacific	Consoli-dated
January 3, 2015*	$ 131	$ 3,589	$ 82	$ 465	$ 389	$ 83	$ 232	$ 4,971
Additions					58			58
Currency translation adjustment				(5)	(26)	(1)	(4)	(36)
April 4, 2015	**$ 131**	**$ 3,589**	**$ 82**	**$ 460**	**$ 421**	**$ 82**	**$ 228**	**$ 4,993**

* In conjunction with the establishment of the Kashi operating segment, included within the North America Other reportable segment, goodwill was reallocated on a relative fair value basis. All prior period balances were updated to conform with current presentation. See Note 12 for further discussion.

Intangible assets subject to amortization

(millions)

Gross carrying amount	U.S. Morning Foods	U.S. Snacks	U.S. Specialty	North America Other	Europe	Latin America	Asia Pacific	Consoli-dated
January 3, 2015	$ 8	$ 65	$	$ 5	$ 38	$ 6	$ 10	$ 132
Additions					4			4
Currency translation adjustment					(2)			(2)
April 04, 2015	**$ 8**	**$ 65**	**$**	**$ 5**	**$ 40**	**$ 6**	**$ 10**	**$ 134**

Accumulated Amortization								
January 3, 2015	$ 8	$ 16	$	$ 4	$ 7	$ 6	$ 2	$ 43
Amortization		1			1			2
April 4,2015	**$ 8**	**$ 17**	**$**	**$ 4**	**$ 8**	**$ 6**	**$ 2**	**$ 45**

Intangible assets subject to amortization, net								
January 3, 2015	$	$ 49	$	$ 1	$ 31	$	$ 8	$ 89
Additions					4			4
Currency translation adjustment					(2)			(2)
Amortization		(1)			(1)			(2)
April 04, 2015	**$**	**$ 48**	**$**	**$ 1**	**$ 32**	**$**	**$ 8**	**$ 89**

For intangible assets in the preceding table, amortization was $2 million for the quarters ended April 4, 2015 and March 29, 2014. The currently estimated aggregate annual amortization expense for full-year 2015 is approximately $9 million.

Intangible assets not subject to amortization

(millions)	U.S. Morning Foods	U.S. Snacks	U.S. Specialty	North America Other	Europe	Latin America	Asia Pacific	Consoli-dated
January 3, 2015*	$	$ 1,625	$	$ 158	$ 423	$	$	$ 2,206
Additions					25			25
Currency translation adjustment					(38)			(38)
April 4, 2015	**$**	**$ 1,625**	**$**	**$ 158**	**$ 410**	**$**	**$**	**$ 2,193**

* In conjunction with the establishment of the Kashi operating segment, included within the North America Other reportable segment, certain intangible assets were reallocated. All prior period balances were updated to conform with current presentation. See Note 12 for further discussion.

Note 3 Restructuring and cost reduction activities

The Company views its continued spending on restructuring and cost reduction activities as part of its ongoing operating principles to provide greater visibility in achieving its long-term profit growth targets. Initiatives undertaken are currently expected to recover cash implementation costs within a five-year period of completion. Upon completion (or as each major stage is completed in the case of multi-year programs), the project begins to deliver cash savings and/or reduced depreciation.

Project K

The most recent and largest program that is currently active is Project K, a four-year efficiency and effectiveness program announced in November 2013. The program is expected to generate a significant amount of savings that will be invested in key strategic areas of focus for the business. The Company expects that this investment will drive future growth in revenues, gross margin, operating profit, and cash flow.

Table of Contents

The focus of the program will be to strengthen existing businesses in core markets, increase growth in developing and emerging markets, and drive an increased level of value-added innovation. The program is expected to provide a number of benefits, including an optimized supply chain infrastructure, the implementation of global business services, and a new global focus on categories.

The Company currently anticipates that Project K will result in total pre-tax charges, once all phases are approved and implemented, of $1.2 to $1.4 billion, with after-tax cash costs, including incremental capital investments, estimated to be $900 million to $1.1 billion. The Company currently expects the charges will consist of asset-related costs totaling $450 to $500 million which will consist primarily of asset impairments, accelerated depreciation and other exit-related costs; employee-related costs totaling $425 to $475 million which will include severance, pension and other termination benefits; and other costs totaling $325 to $425 million which will consist primarily of charges related to the design and implementation of global business capabilities. A significant portion of other costs are the result of the implementation of global business service centers which are intended to simplify and standardize business support processes.

The Company currently expects that total pre-tax charges will impact reportable segments as follows: U.S. Morning Foods (approximately 18%), U.S. Snacks (approximately 12%), U.S. Specialty (approximately 1%), North America Other (approximately 9%), Europe (approximately 13%), Latin America (approximately 3%), Asia-Pacific (approximately 6%), and Corporate (approximately 38%). A majority of the costs impacting Corporate relate to additional initiatives to be approved and executed in the future. When these initiatives are fully defined and approved, the Company will update its estimated costs by reportable segment as needed.

Since the inception of Project K, the Company has recognized charges of $574 million that have been attributed to the program. The charges consist of $4 million recorded as a reduction of revenue, $358 million recorded in COGS and $212 million recorded in SGA.

All Projects

During the quarter ended April 4, 2015, the Company recorded total charges of $68 million across all restructuring and cost reduction activities. The charges consist of $2 million recorded as a reduction of revenue, $32 million recorded in cost of goods sold (COGS) and $34 million recorded in selling, general and administrative (SGA) expense.

During the quarter ended March 29, 2014 the Company recorded total charges of $54 million across all restructuring and cost reduction activities. The charges consist of $25 million being recorded in COGS and $29 million recorded in SGA expense.

The tables below provide the details for charges across all restructuring and cost reduction activities incurred during the quarters ended April 4, 2015 and March 29, 2014 and program costs to date for programs currently active as of April 4, 2015.

(millions)	2015	2014	Program costs to date April 4, 2015
Employee related costs	**$ 17**	$ 17	**$ 214**
Asset related costs	**23**	3	**66**
Asset impairment			**87**
Other costs	**28**	34	**207**
Total	**$ 68**	$ 54	**$ 574**

(millions)	2015	2014	Program costs to date April 4, 2015
U.S. Morning Foods	**$ 8**	$ 11	**$ 168**
U.S. Snacks	**9**	7	**85**
U.S. Specialty	**1**	1	**7**
North America Other	**6**	3	**33**
Europe	**19**	12	**118**
Latin America		4	**12**
Asia Pacific	**5**	6	**66**
Corporate	**20**	10	**85**
Total	**$ 68**	$ 54	**$ 574**

For the quarters ended April 4, 2015 and March 29, 2014 employee related costs consist primarily of severance benefits, asset related costs consist primarily of accelerated depreciation, and other costs consist primarily of third-party incremental costs related to the development and implementation of global business capabilities.

At April 4, 2015 total exit cost reserves were $87 million, related to severance payments and other costs of which a substantial portion will be paid out in 2015 and 2016. The following table provides details for exit cost reserves.

	Employee Related Costs	Asset Impairment	Asset Related Costs	Other Costs	Total
Liability as of January 3, 2015	$ 96	$	$	$ 14	$ 110
2015 restructuring charges	17		23	28	68
Cash payments	(39)		(4)	(27)	(70)
Non-cash charges and other	(3)		(18)		(21)
Liability as of April 4, 2015	**$ 71**	**$**	**$ 1**	**$ 15**	**$ 87**

Note 4 Equity

Earnings per share

Basic earnings per share is determined by dividing net income attributable to Kellogg Company by the weighted average number of common shares outstanding during the period. Diluted earnings per share is similarly determined, except that the denominator is increased to include the number of additional common shares that would have been outstanding if all dilutive potential common shares had been issued. Dilutive potential common shares consist principally of employee stock options issued by the Company, and to a lesser extent, certain contingently issuable performance shares. Basic earnings per share is reconciled to diluted earnings per share in the following table. There were 2 million and 8 million anti-dilutive potential common shares excluded from the reconciliation for the quarters ended April 4, 2015 and March 29, 2014, respectively.

Table of Contents

Quarters ended April 4, 2015 and March 29, 2014:

(millions, except per share data)	Net income attributable to Kellogg Company	Average shares outstanding	Earnings per share
2015			
Basic	**$ 227**	**355**	**$ 0.64**
Dilutive potential common shares		**2**	
Diluted	**$ 227**	**357**	**$ 0.64**
2014			
Basic	$ 406	360	$ 1.13
Dilutive potential common shares		2	(0.01)
Diluted	$ 406	362	$ 1.12

In February 2014, the Company s board of directors approved a share repurchase program authorizing the repurchase of up to $1.5 billion of our common stock through December 2015. This authorization supersedes the April 2013 authorization and is intended to allow the Company to repurchase shares for general corporate purposes and to offset issuances for employee benefit programs.

During the quarter ended April 4, 2015, the Company repurchased approximately 4 million shares of common stock for a total of $285 million. During the quarter ended March 29, 2014, the Company repurchased 5 million shares of common stock for a total of $321 million.

Comprehensive income

Comprehensive income includes net income and all other changes in equity during a period except those resulting from investments by or distributions to shareholders. Other comprehensive income consists of foreign currency translation adjustments, fair value adjustments associated with cash flow hedges and adjustments for net experience losses and prior service cost related to employee benefit plans.

	Quarter ended April 04, 2015			Quarter ended March 29, 2014		
(millions)	Pre-tax amount	Tax (expense) or benefit	After-tax amount	Pre-tax amount	Tax (expense) or benefit	After-tax amount
Net income			$ 227			$ 406
Other comprehensive income (loss):						
Foreign currency translation adjustments	$ (62)	$ (21)	(83)	$ 3	$	3
Cash flow hedges:						
Unrealized gain (loss) on cash flow hedges	8	(1)	7	(1)		(1)
Reclassification to net income	(4)		(4)	(10)	3	(7)
Postretirement and postemployment benefits:						
Amounts arising during the period:						
Prior service credit (cost)	(1)		(1)			
Reclassification to net income:						
Net experience loss	1		1	1		1
Prior service cost	3	(1)	2	2	(1)	1
Other comprehensive income (loss) attributable to Kellogg	$ (55)	$ (23)	(78)	$ (5)	$ 2	(3)
Comprehensive income attributable to noncontrolling interest			(1)			
Comprehensive income			$ 148			$ 403

13

Table of Contents

Reclassifications out of Accumulated Other Comprehensive Income (AOCI) consisted of the following:

(millions) Details about AOCI components	Amount reclassified from AOCI Quarter ended April 4, 2015	Quarter ended March 29, 2014	Line item impacted within Income Statement
Gains and losses on cash flow hedges:			
Foreign currency exchange contracts	**$ (7)**	$ (1)	COGS
Foreign currency exchange contracts		(1)	SGA
Interest rate contracts		(9)	Interest expense
Commodity contracts	**3**	1	COGS
	$ (4)	$ (10)	Total before tax
		3	Tax (expense) benefit
	$ (4)	$ (7)	Net of tax
Amortization of postretirement and postemployment benefits:			
Net experience loss	**$ 1**	$ 1	See Note 7 for further details
Prior service cost	**3**	2	See Note 7 for further details
	$ 4	$ 3	Total before tax
	(1)	(1)	Tax (expense) benefit
	$ 3	$ 2	Net of tax
Total reclassifications	**$ (1)**	$ (5)	Net of tax

Accumulated other comprehensive income (loss) as of April 4, 2015 and January 3, 2015 consisted of the following:

(millions)	April 4, 2015	January 3, 2015
Foreign currency translation adjustments	**$ (1,202)**	$ (1,119)
Cash flow hedges unrealized net gain (loss)	**(21)**	(24)
Postretirement and postemployment benefits:		
Net experience loss	**(17)**	(18)
Prior service cost	**(51)**	(52)
Total accumulated other comprehensive income (loss)	**$ (1,291)**	$ (1,213)

Noncontrolling interests

In December 2012, the Company entered into a series of agreements with a third party including a subordinated loan (VIE Loan) of $44 million which is convertible into approximately 85% of the equity of the entity (VIE). Due to this convertible subordinated loan and other agreements, the Company determined that the entity is a variable interest entity, the Company is the primary beneficiary and the Company has consolidated the financial statements of the VIE. The assets and liabilities of the VIE are included in the Consolidated Balance Sheets as of April 4, 2015 and January 3, 2015 and the results of the VIE s operations are included in the Consolidated Statements of Income for the quarters ended April 4, 2015 and March 29, 2014. The Company evaluates the consolidated assets of the VIE as well as the VIE Loan and related accrued interest for recoverability based on the actual and projected financial results of the VIE, the amount of senior collateralized borrowings of the VIE as well as other matters impacting the VIE s operations. During the quarter ended April 4, 2015, the Company has determined that certain assets related to the VIE may not be fully recoverable and has recorded a non-cash charge of $25 million, which has been recorded as other income (expense), net.

Table of Contents

Note 5 Debt

The following table presents the components of notes payable at April 4, 2015 and January 3, 2015:

	April 4, 2015		January 3, 2015	
(millions)	**Principal amount**	**Effective interest rate**	Principal amount	Effective interest rate
U.S. commercial paper	**$ 610**	**0.39%**	$ 681	0.36%
Europe commercial paper	**121**	**0.07**	96	0.09
Bank borrowings	**78**		51	
Total	**$ 809**		$ 828	

In February 2015, the Company repaid its $250 million floating-rate U.S. Dollar Notes due 2015 at maturity with U.S. commercial paper.

In March 2015, the Company issued 600 million (approximately $658 million USD at April 4, 2015, which reflects the discount and translation adjustments) of ten-year 1.25% Euro Notes due 2025, using the proceeds from these Notes for general corporate purposes, including the repayment of a portion of its commercial paper borrowings. The Notes contain customary covenants that limit the ability of the Company and its restricted subsidiaries (as defined) to incur certain liens or enter into certain sale and lease-back transactions, as well as a change of control provision. The Notes were designated as a net investment hedge of the Company s investment in its Europe subsidiary when issued.

In the first quarter of 2015, the Company entered into interest rate swaps with notional amounts totaling $558 million, which were designated as fair value hedges for (a) $300 million of its 4.15% fixed rate U.S. Dollar Notes due 2019, (b) $200 million of its 4.0% fixed rate U.S. Dollar Notes due 2020 and (c) $58 million of its 3.125% fixed rate U.S. Dollar Notes due 2022.

In the first quarter of 2015, the Company terminated interest rate swaps with notional amounts totaling $1.5 billion, which were designated as fair value hedges for (a) $800 million of its 4.15% fixed rate U.S. Dollar Notes due 2019, (b) $500 million of its 4.0% fixed rate U.S. Dollar Notes due 2020 and (c) $216 million of its 3.125% fixed rate U.S. Dollar Notes due 2022 (collectively, the Notes). The interest rate swaps effectively converted the interest rate on the Notes from fixed to variable and the unrealized gain upon termination of $26 million will be amortized to interest expense over the remaining term of the Notes.

As of April 4, 2015, the Company has interest rate swaps with notional amounts totaling $1.4 billion, which effectively converts a portion of the associated U.S. Dollar Notes from fixed rate to floating rate obligations. These derivative instruments are designated as fair value hedges. The effective interest rates on debt obligations resulting from the Company s current and previous interest rate swaps as of April 4, 2015 were as follows: (a) seven-year 4.45% U.S. Dollar Notes due 2016 3.41%; (b) five-year 1.875% U.S. Dollar Notes due 2016 1.58%; (c) five-year 1.75% U.S. Dollar Notes due 2017 - 1.34%; (d) seven-year 3.25% U.S. Dollar Notes due 2018 1.87%; (e) ten-year 4.15% U.S. Dollar Notes due 2019 - 3.86%; (f) ten-year 4.00% U.S. Dollar Notes due 2020 - 2.59%; (g) ten-year 3.125% U.S. Dollar Notes due 2022 - 2.03%.

Table of Contents

Note 6 Stock compensation

The Company uses various equity-based compensation programs to provide long-term performance incentives for its global workforce. Currently, these incentives consist principally of stock options, restricted stock units, and to a lesser extent, executive performance shares and restricted stock grants. During 2015, the Company changed the mix of equity compensation, awarding an increasing number of restricted stock units and fewer stock option awards. The Company also sponsors a discounted stock purchase plan in the United States and matching-grant programs in several international locations. Additionally, the Company awards restricted stock to its outside directors. The interim information below should be read in conjunction with the disclosures included within the stock compensation footnote of the Company s 2014 Annual Report on Form 10-K.

The Company classifies pre-tax stock compensation expense in SGA expense principally within its corporate operations. For the periods presented, compensation expense for all types of equity-based programs and the related income tax benefit recognized were as follows:

	Quarter ended	
	April 4,	March 29,
(millions)	**2015**	2014
Pre-tax compensation expense	**$ 12**	$ 14
Related income tax benefit	**$ 4**	$ 5

As of April 4, 2015, total stock-based compensation cost related to non-vested awards not yet recognized was $90 million and the weighted-average period over which this amount is expected to be recognized was 2 years.

Stock options

During the quarters ended April 4, 2015 and March 29, 2014, the Company granted non-qualified stock options to eligible employees as presented in the following activity tables. Terms of these grants and the Company s methods for determining grant-date fair value of the awards were consistent with that described within the stock compensation footnote in the Company s 2014 Annual Report on Form 10-K.

Quarter ended April 4, 2015:

Employee and director stock options	Shares (millions)	Weighted-average exercise price	Weighted-average remaining contractual term (yrs.)	Aggregate intrinsic value (millions)
Outstanding, beginning of period	**21**	**$ 56**		
Granted	**3**	**64**		
Exercised	**(1)**	**52**		
Forfeitures and expirations				
Outstanding, end of period	**23**	**$ 57**	**7.4**	**$ 204**
Exercisable, end of period	**14**	**$ 55**	**6.3**	**$ 163**

Quarter ended March 29, 2014:

Employee and director stock options	Shares (millions)	Weighted-average exercise price	Weighted-average remaining contractual term (yrs.)	Aggregate intrinsic value (millions)
Outstanding, beginning of period	20	$ 54		
Granted	6	60		
Exercised	(1)	47		
Forfeitures and expirations				
Outstanding, end of period	25	$ 55	7.6	$ 166
Exercisable, end of period	13	$ 52	6.2	$ 131

Table of Contents

The weighted-average fair value of options granted was $7.20 per share and $6.70 per share for the quarter ended April 4, 2015 and March 29, 2014, respectively. The fair value was estimated using the following assumptions:

	Weighted-average expected volatility	Weighted-average expected term (years)	Weighted-average risk-free interest rate	Dividend yield
Grants within the quarter ended April 4, 2015:	16%	6.87	1.98%	3.00%
Grants within the quarter ended March 29, 2014:	15%	7.34	2.35%	3.00%

The total intrinsic value of options exercised was $17 million and $8 million for the quarter ended April 4, 2015 and March 29, 2014, respectively.

Performance shares

In the first quarter of 2015, the Company granted performance shares to a limited number of senior executive-level employees, which entitle these employees to receive a specified number of shares of the Company s common stock upon vesting. The number of shares earned could range between 0 and 200% of the target amount depending upon performance achieved over the three year vesting period. The performance conditions of the award include three-year cumulative operating cash flow (CCF) and total shareholder return (TSR) of the Company s common stock relative to a select group of peer companies.

A Monte Carlo valuation model was used to determine the fair value of the awards. The TSR performance metric is a market condition. Therefore, compensation cost of the TSR condition is fixed at the measurement date and is not revised based on actual performance. The TSR metric was valued as a multiplier of possible levels of CCF achievement. Compensation cost related to CCF performance is revised for changes in the expected outcome. The 2015 target grant currently corresponds to approximately 184,000 shares, with a grant-date fair value of $58 per share.

Based on the market price of the Company s common stock at April 4, 2015, the maximum future value that could be awarded to employees on the vesting date for all outstanding performance share awards was as follows:

(millions)	**April 4, 2015**
2013 Award	**$ 26**
2014 Award	**$ 29**
2015 Award	**$ 24**

The 2012 performance share award, payable in stock, was settled at 35% of target in February 2015 for a total dollar equivalent of $3 million.

Other stock-based awards

During the quarter ended April 4, 2015, the Company granted restricted stock units and a nominal number of restricted stock awards to eligible employees as presented in the following table. Terms of these grants and the Company s method of determining grant-date fair value were consistent with that described within the stock compensation footnote in the Company s 2014 Annual Report on Form 10-K.

Quarter ended April 4, 2015

Employee restricted stock and restricted stock units	Shares (thousands)	Weighted-average grant-date fair value
Non-vested, beginning of year	346	$ 54
Granted	563	58
Vested	(48)	51
Forfeited	(2)	58
Non-vested, end of year	859	$ 57

Grants of restricted stock and restricted stock units for the comparable period ended March 29, 2014 were 51,000.

Table of Contents

Note 7 Employee benefits

The Company sponsors a number of U.S. and foreign pension plans as well as other nonpension postretirement and postemployment plans to provide various benefits for its employees. These plans are described within the footnotes to the Consolidated Financial Statements included in the Company s 2014 Annual Report on Form 10-K. Components of Company plan benefit expense for the periods presented are included in the tables below.

Pension

	Quarter ended	
(millions)	**April 4, 2015**	March 29, 2014
Service cost	**$ 28**	$ 26
Interest cost	**53**	57
Expected return on plan assets	**(100)**	(104)
Amortization of unrecognized prior service cost	**3**	3
Total pension (income) expense	**$ (16)**	$ (18)

Other nonpension postretirement

	Quarter ended	
(millions)	**April 4, 2015**	March 29, 2014
Service cost	**$ 8**	$ 7
Interest cost	**12**	14
Expected return on plan assets	**(25)**	(24)
Amortization of unrecognized prior service cost (credit)		(1)
Total postretirement benefit (income) expense	**$ (5)**	$ (4)

Postemployment

	Quarter ended	
(millions)	**April 4, 2015**	March 29, 2014
Service cost	**$ 2**	$ 2
Interest cost	**1**	1
Recognized net loss	**1**	1
Total postemployment benefit expense	**$ 4**	$ 4

Company contributions to employee benefit plans are summarized as follows:

(millions)	Pension	Nonpension postretirement	Total
Quarter ended:			
April 4, 2015	**$ 9**	**$ 3**	**$ 12**
March 29, 2014	$ 24	$ 4	$ 28
Full year:			
Fiscal year 2015 (projected)	**$ 39**	**$ 16**	**$ 55**
Fiscal year 2014 (actual)	$ 37	$ 16	$ 53

Plan funding strategies may be modified in response to management s evaluation of tax deductibility, market conditions, and competing investment alternatives.

Note 8 Income taxes

The consolidated effective tax rate for the quarter ended April 4, 2015 was 25% as compared to the prior year s rate of 29%. The effective tax rate for the first quarter of 2015 benefited from a reduction in tax related to current year remitted and unremitted earnings and the completion of certain tax examinations.

As of April 4, 2015, the Company classified $9 million of unrecognized tax benefits as a net current liability. Management s estimate of reasonably possible changes in unrecognized tax benefits during the next twelve months consists of the

Table of Contents

current liability balance expected to be settled within one year, offset by approximately $7 million of projected additions related primarily to ongoing intercompany transfer pricing activity. Management is currently unaware of any issues under review that could result in significant additional payments, accruals or other material deviation in this estimate.

Following is a reconciliation of the Company s total gross unrecognized tax benefits for the quarter ended April 4, 2015; $50 million of this total represents the amount that, if recognized, would affect the Company s effective income tax rate in future periods.

(millions)	
January 3, 2015	**$ 78**
Tax positions related to current year:	
Additions	**2**
Reductions	
Tax positions related to prior years:	
Additions	
Reductions	**(7)**
Settlements	
April 4, 2015	**$ 73**

For the quarter ended April 4, 2015, the Company recognized a decrease of $1 million for tax-related interest and penalties. The Company recognized no cash settlements during the current quarter. The accrual balance was $19 million at April 4, 2015.

Note 9 Derivative instruments and fair value measurements

The Company is exposed to certain market risks such as changes in interest rates, foreign currency exchange rates, and commodity prices, which exist as a part of its ongoing business operations. Management uses derivative financial and commodity instruments, including futures, options, and swaps, where appropriate, to manage these risks. Instruments used as hedges must be effective at reducing the risk associated with the exposure being hedged.

The Company designates derivatives as cash flow hedges, fair value hedges, net investment hedges, and uses other contracts to reduce volatility in interest rates, foreign currency and commodities. As a matter of policy, the Company does not engage in trading or speculative hedging transactions.

Total notional amounts of the Company s derivative instruments as of April 4, 2015 and January 3, 2015 were as follows:

(millions)	**April 4, 2015**	January 3, 2015
Foreign currency exchange contracts	**$ 946**	$ 764
Interest rate contracts	**1,400**	2,958
Commodity contracts	**651**	492
Total	**$ 2,997**	$ 4,214

Following is a description of each category in the fair value hierarchy and the financial assets and liabilities of the Company that were included in each category at April 4, 2015 and January 3, 2015, measured on a recurring basis.

Level 1 Financial assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market. For the Company, level 1 financial assets and liabilities consist primarily of commodity derivative contracts.

Level 2 Financial assets and liabilities whose values are based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability. For the Company, level 2 financial assets and liabilities consist of interest rate swaps and over-the-counter commodity and currency contracts.

The Company s calculation of the fair value of interest rate swaps is derived from a discounted cash flow analysis based on the terms of the contract and the interest rate curve. Over-the-counter commodity derivatives are valued using an income approach based on the commodity index prices less the contract rate multiplied by the notional amount. Foreign currency contracts are valued using an income approach based on forward rates less the contract rate multiplied by the notional amount. The Company s calculation of the fair value of level 2 financial assets and liabilities takes into consideration the risk of nonperformance, including counterparty credit risk.

Table of Contents

Level 3 Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect management s own assumptions about the assumptions a market participant would use in pricing the asset or liability. The Company did not have any level 3 financial assets or liabilities as of April 4, 2015 or January 3, 2015.

The following table presents assets and liabilities that were measured at fair value in the Consolidated Balance Sheet on a recurring basis as of April 4, 2015 and January 3, 2015:

Derivatives designated as hedging instruments

	April 4, 2015			January 3, 2015		
(millions)	**Level 1**	**Level 2**	**Total**	Level 1	Level 2	Total
Assets:						
Foreign currency exchange contracts:						
Other prepaid assets	**$**	**$ 45**	**$ 45**	$	$ 29	$ 29
Interest rate contracts (a):						
Other assets		**2**	**2**		7	7
Total assets	**$**	**$ 47**	**$ 47**	$	$ 36	$ 36