DMND - Diamond Foods and P&G Conference Call to Announce Pringles Merger Into Diamond Foods, Inc

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PRESENTATION

Operator

Good morning. My name is Katie and I will be your conference operator. Today’s call is being recorded.

At this time I would like to welcome everyone to the Diamond Foods and Procter & Gamble investor conference call. All lines had been placed on mute to prevent any background noise. After the speakers’ remarks there will be a question-and-answer session. (Operator Instructions)

Ms. Segre, you may begin your conference.
Thank you, Katie, and good morning to everyone. Welcome to the Diamond Foods and Procter & Gamble investor conference call and webcast to discuss the merger of Pringles into Diamond Foods. On the call today are Michael Mendes, Chairman, President, and Chief Executive Officer of Diamond Foods; Steve Neal, Chief Financial and Administrative Officer of Diamond Foods; Bob McDonald, Chairman, President, and Chief Executive Officer of Procter & Gamble; and Jon Moeller, Chief Financial Officer of Procter & Gamble.

Before we get started, let’s cover a few housekeeping items. Today’s press release is available on both of our websites at DiamondFoods.com and PG.com. A printed copy of the prepared remarks will be available on both websites within one hour after the call’s conclusion. You can find the remarks at DiamondFoods.com and PG.com/investors.

We have arranged for a taped replay of this call to be available via telephone beginning about two hours after the call’s conclusion until 11.30 a.m. Eastern Time on April 12, 2011. Please refer to the press release for the dial in numbers. In addition, this call is being webcast live and a replay will be available on both companies’ websites.

I would like to remind you that during the course of today’s call we will make forward-looking statements as defined by the Private Securities Litigation Reform Act of 1995, including projections of our results. Since actual results may differ materially from these projections, please review the risk factors in our SEC filings and in the press release.

Our forward-looking statements are based on factors that are subject to change and speak only as of the date they are given. We do not undertake to update forward-looking statements.

At the conclusion of our prepared remarks you may stay on the line to ask questions of the Diamond Foods team. There is a separate dial in number for Procter & Gamble’s conference call that will begin at 10 a.m. Eastern Time this morning. The dial-in number is provided in the press release.

Now I would like to turn the call over to Michael Mendes, Chairman, President, and Chief Executive Officer of Diamond Foods.

Thanks, Linda. Good afternoon, everyone; good morning, everyone; and thank you for joining us. We are very pleased to announce that we have reached an agreement with Procter & Gamble to merge the global business into Diamond -- the global Pringles business into Diamond Foods. Pringles is a great strategic fit adding to our portfolio the world’s largest potato crisp brand with nearly $1.4 billion in sales in 140 countries.

With Pringles, Diamond gains a broad global manufacturing supply chain platform. Internationally, Pringles enjoys a premium positioning and has strong brand awareness which exceeds 90% in key markets outside of the US. More than half of Pringles sales are in the US and the UK, which are also Diamond’s two largest markets, allowing us to effectively leverage our existing infrastructure.

The business has been built on a combination of proprietary products, unique package design, and significant brand investments. The strength of the Pringles franchise reflects its long history and the investment of $2 billion in brand building over the past decade alone. We believe the transaction is financially compelling delivering significant margin expansion and meaningful use -- and a meaningful increase in free cash flow.

On a pro forma basis, for fiscal 2011 the transaction is anticipated to be double-digit EPS accretive. The transaction is expected to close by the end of calendar 2011 which would affect seven months of fiscal 2012. As a result, in fiscal 2012 we expect net sales for the combined company to be approximately $1.8 billion and full-year EPS to be in the range of $3 to $3.10. This reflects EPS accretion of $0.12 to $0.15 per share.
I will now turn the call over to Steve Neil to provide some additional transaction details and financial benefits.

**Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer**

Thank you, Michael, and good morning. First, let me say that I share Michael’s enthusiasm as we add one of the world’s truly iconic global snack brands to the Diamond portfolio.

We expect the acquisition to be structured as a Reverse Morris Trust split-merged transaction that is tax efficient to P&G shareholders. The P&G shareholders who choose to participate will receive approximately 29 million Diamond shares and own about 57% of the outstanding shares of the combined company. Current Diamond shareholders will own approximately 43% of the combined company resulting in approximately 51 million shares outstanding.

In addition, Diamond will assume around $850 million of Pringles debt. We expect to finalize the details of the transaction in the coming months.

The total transaction value is $2.3 billion and includes a collar that could adjust the amount of debt assumed depending on Diamond’s stock price before the commencement of the exchange offer period. We believe the merger provides significant financial benefits for Diamond and will be accretive to earnings in the first year.

On a pro forma basis, assuming Pringles was owned for all of fiscal 2011, net sales would be expected to increase to around $2.4 billion with a resulting EBITDA of $398 million to $410 million. This would result in an EBITDA margin of 17%, about 200 basis points higher than Diamond’s stand-alone performance. Note that these projections include approximately $25 million in synergies.

Similar to our successful Kettle Foods transaction, we have assumed that any additional synergies realized from the merger will be invested back into our portfolio in support of the growth of our brands. We expect to incur merger and integration related costs of approximately $100 million over the first two years. Additionally, we will enter into a transition services agreement with P&G for up to 12 months in order to facilitate an orderly integration of the Pringles business.

Diamond’s cash flow generation with the merger is expected to significantly improve and facilitate accelerated delevering of our balance sheet. We anticipate a pro forma leverage ratio below 4 times EBITDA at the closing and dropping to below 3 times at the end of fiscal 2013. We expect free cash flow, that is cash flow after investing in our brands and capital expenditures, approaching $200 million in the first full fiscal year post merger and we anticipate initially applying the funds to reduce our outstanding borrowings.

Diamond traditionally issues full-year earnings guidance on our fourth-quarter call in September. However, today we are providing our preliminary view for 2012 EPS for Diamond’s stand-alone operations. For fiscal year 2012 Diamond anticipates strong growth in its core business with EPS of $2.85 to $2.98 per share on a stand-alone basis. This is an increase of 15% to 20% from the midpoint of our fiscal 2011 guidance range, which represents a 30% increase over 2010 EPS.

Assuming $0.12 to $0.15 of accretion due to owning the Pringles business for seven months, we now expect full-year 2012 EPS guidance to be $3 to $3.10 per share before integration and acquisition related expenses.

Now I would like to turn the call over to Bob McDonald from P&G.

**Bob McDonald - Procter & Gamble - Chairman, President & CEO**

Thank you, Steve, and thank you all for joining us this morning. The announcement this morning of our plans to exit the snacks business is the result of our ongoing portfolio and strategy review process.
Strategically, P&G has exited several categories over the past few years in order to focus on our core businesses, and this is another step in that process. By focusing P&G’s efforts and investments on businesses closer to our core we can better advance our purpose of improving the lives of more consumers in more parts of the world more completely.

Our financial goals in this transaction, as with any exit of a business, are to maximize the after-tax value of the Snacks business for P&G shareholders while minimizing the earnings per share dilution. The value Diamond is offering for the business and the tax efficient structure of the deal accomplish both of these goals.

P&G is hosting a follow-up call at 10 o’clock this morning to discuss the financial implications of the deal in more detail, so I won’t take time to do that now. But I would like to thank all of our Snacks employees for their dedicated service to P&G and their tireless efforts to build such a strong global brand as Pringles. Pringles will be a core brand and a high priority for Diamond Foods, and I am confident that Diamond will be an excellent home for our Snacks employees.

Now I would like to turn the call back over to Michael.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Thank you, Bob. The addition of Pringles business is transformational to Diamond and its shareholders. We believe the financial benefits of improved margins, significant EPS accretion, and free cash flow will make Diamond an even stronger company in the future, delivering exceptional value to Diamond and P&G shareholders. We plan to continue our strategy investing our brands for growth over the long-term and look forward to welcoming the Pringles employees to Diamond.

Linda Segre - Diamond Foods, Inc. - SVP, Corporate Strategy and Communications

At this time, we will open the call to questions to the Diamond team. As a reminder, Procter & Gamble will host an investor conference call at 10 a.m. Eastern. Please refer to the press release for dial-in information.

QUESTIONS AND ANSWERS

Tim Ramey - D.A. Davidson - Analyst

Congratulations. This looks like an outstanding deal. Of course, the first question has to be kind of what does the growth rate contribution look like from Pringles. There is lots of slides that deal with category growth, but it would be nice to know a little bit more about how Pringles has been performing in US, UK, and Rest of World.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Tim, we are going to be providing some quite granular long-term guidance as we get close to closing, but most likely following closing, after we are able to do a ground-up forecasting model with the employees that are going to be in scope. That being said, I can just give you some general history about the brand.
Pringles in North America has done some work to reposition the product in order to make it more competitive and a lot of that was around the pack size configuration and moving away from a dollar price point. That was some work that had some affect on the top line in that period, but today we are seeing some nice growth in the last 12-month period from the brand.

I think when you look at the two biggest businesses, two most mature business, North America and Europe, those have been flat to modest single-digit growers. They are developing markets, which probably about $400 billion --

Unidentified Company Representative

$400 million.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

-- $400 million in business for them has been growing at a high single-digit rate.

We do think that there is a lot of opportunity to build the business by leveraging channels at retail that we are highly developed in that is less of a focus for the brand. We think on the international front there is a real opportunity to build out this product and this product type, given the product nature and its ability to transfer very effectively into a lot of global markets.

And so today our goal is to assume the asset, to retain its health, to put together a combined go-to-market team globally that is best suited to market our entire portfolio. And we will be out the gate investing in the brand to enable greater growth down the road.

Tim Ramey - D.A. Davidson - Analyst

Just one quick one on distribution. I think -- correct me if I am wrong, but I think Pringles is 100% warehouse. Does this change your distribution strategy from kind of the hybrid model that you have right now in snacks? It certainly would give you much more scale through the warehouse into some of these channels.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

This does allow us to leverage part of a distribution channel that we have probably the most experience and a lot of scale. We do like our more robust go-to-market strategy now and our ability to better serve customers through a variety of distribution models. We have got some great partners that are working with us for those customers who value and require a DSD model, and we are going to continue to leverage that.

We think that -- as long as we have got good partners and it’s mutually beneficial we think that is a way that adds to our capability to get to consumers that we might not be able to get to through the warehouse model. I would say that this business today fits very, very nicely though with our core traditional warehouse snacks such as Emerald and Pop Secret.

Tim Ramey - D.A. Davidson - Analyst

Thanks, Michael.

Operator

Heather Jones, BB&T Capital Markets.
Heather Jones - BB&T Capital Markets - Analyst

Good morning. I wanted to -- looking at your fiscal 2012 guidance, assuming that the Pringles deal closes in the calendar, so if it had closed at the beginning of your year could we just simply extrapolate that out to the -- you would be looking at $3.10 to $3.25 EPS?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

No, the $3.10 to $3.25 assumes seven months worth of combined operations.

Heather Jones - BB&T Capital Markets - Analyst

Right. You say it would be $3 to $3.10 and that is what I am saying. If you had it for the whole year, we could assume more like in the $3.10 to $3.25 range?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

I understand what you are saying. It certainly would be -- since it's going to be accretive right away, yes, it certainly would be greater than the $3 to $3.10 that we have, yes.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

It would be around $0.12 to $0.15 in those seven months of accretion.

Heather Jones - BB&T Capital Markets - Analyst

Okay. And when you were talking about $25 million in synergies is that number net of the anticipated increase in marketing spend?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Yes.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Yes, it is.

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Yes.

Heather Jones - BB&T Capital Markets - Analyst

Okay, okay. Thank you. Congratulations.
Operator
Ed Aaron, RBC Capital Markets.

Ed Aaron - RBC Capital Markets - Analyst
Thanks. Good morning, everybody. I guess my question is why now? We are not that far removed from your last transformational deal, so just organizationally how can we get a little more comfortable that you are ready to bite something off that is so big? And then I have one more after that.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO
One is our Kettle integration has been very, very successful. Couldn't be more proud of the team's energy behind that effort and we are today meaningfully complete on all of the major elements around the Kettle integration and are now running the business as a collective.

I would say on why now, I would say that generally you don't get to pick your time with good transactions. Our M&A calendar is not built on when is the optimal time and then buy the best thing that is available then.

I think this is a unique asset and being able to use a Reverse Morris Trust as a vehicle to acquire this asset and capture value that can perhaps be realized by the buyer and the seller is a unique structure. And it's an iconic brand that we think is going to be very additive for us. So it's very much on track with what we would like to do if it was available and we deemed it was available now; the timing worked for us. So that is a background.

Ed Aaron - RBC Capital Markets - Analyst
Fair enough. I guess my other question is just competitively how should we handicap the risk of you kind of coming more into the crosshairs of Frito in the snack aisle. This acquisition gives you a much bigger direct competition with them, so how should we kind of think about some of the risk that might come with that?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO
Well, this product does have a different pack type and a different form than the traditional salty chip category products. I think that distinct form, that distinct product delivery system, the freshness, and the shelf life of this product has in its ability to go through a warehouse system makes it meaningfully different in a lot of ways. And I think we will be competing more broadly as a savory snack.

I think that we are going to bring consumers to the shelf. And I think that we, as we compete with other brands, if somebody is going to compete -- we know there is going to be somebody out there -- if they are trying to help bring new ideas, innovation, and to invest resources to stimulate consumption at retail that is probably the kind of competition you would want to have. So I think that this is a brand that has competed well historically and there is a lot of people in that savory snack category to consider.

So I don't think it's a meaningful concern. I think our largest concern is our ability to execute, because I think that if we fail it will not be as a result of someone else's reaction. It will be the result of us not executing in order to satisfy the needs of the customers and our retail partners.
Ed Aaron - RBC Capital Markets - Analyst

That is fair enough. Thanks for taking my questions.

Operator

Alton Stump, Longbow Research.

Alton Stump - Longbow Research - Analyst

Good morning. Congrats on the deal. The margin guidance that you have offered with this, with the increase going from 26% to 27% gross margin up to 31% to 33% and then on the EBITDA front, could you give me some color as to how much of that is just a pure injection alone of Pringles obviously being a bit higher-margin business and corporate average versus how much of that is in -- with this brand being able to leverage behind your existing snack portfolio, whether it's through [cross and] motions or if it's through more efficient in-store spending?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Alton, this is Steve Neil. Yes, I think it's a combination of both. If you look at our portfolio that -- with Pop Secret and with Kettle I think Pringles comes in a similar type of margin structure, so certainly that will add to the overall portfolio. But we what we are actually seeing here is the distribution platform and the leverage that we can get with offering multiple brands to that snack buyer.

I think you are going to see some leverage both in the gross margin as well as in operating expenses, so we think it's definitely a combination of both. It does enrich our overall gross margin portfolio, but it also gives us a lot of scale. So I think as Michael mentioned to the comment that Ed had is it's up to us to execute to get that leverage and that is certainly a significant focus of us combining the two businesses to make the combination better. So a combination of both.

Alton Stump - Longbow Research - Analyst

Okay, that is all I had. Thank you.

Operator

Akshay Jagdale, KeyBanc.

Akshay Jagdale - KeyBanc Capital Markets - Analyst

Obviously there is making a pretty compelling case about scale here and I understand that. I just wanted to get your thoughts on your long-term growth expectations as a combined entity. Prior to this you gave five-year guidance not too long ago which implied double-digit growth on the top line. How does having the Pringles business enhance your ability to grow?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Well, speaking of that same guidance, we gave a target of $4 of EPS in 2015. I would argue that this transaction will further enable and build our confidence of achieving that 2015 EPS target, and that we think is very good for the business.
When it comes to the top line we feel that this is a business that has real potential to grow. Where that growth will take place, what we need to do to drive that growth, and in what periods do we expect to see that growth manifest itself is detail that we are going to be able to provide a little bit later after we close.

We are sitting here now in April and we are giving 2012 guidance when normally we are giving 2012 guidance in September. So, while I apologize to not give you more visibility on the out period, I hope that you will take some solace in that we are giving you 2012 guidance in April.

But at this point in time all I can tell you broadly as this brand is a thoroughbred. It has been built and handcrafted by some of the best CPG executives in the world. P&G, they don't just produce products, they produce brands. They have crafted the design of this product and the unique position of this product and built the brand around this product in a manner that we think is very leverageable and that is transferable into even more markets.

We are excited about having the portfolio and we are pleased that Procter & Gamble has actually increased their advertising level in 2011 versus 2010, which will be consistent with our disposition out the gate which will be to invest against the brand. So rather than just sit here today and forecast on information that would not be grounded on the kind of facts we normally have for long-term guidance, appreciate your patience as we get closer to the closing period when we have a lot more visibility around the underpinnings of the business and we revise our long-term guidance at that time.

Akshay Jagdale - KeyBanc Capital Markets - Analyst

That is helpful, Michael. Just a follow-up, I am sure there will be some investors who will be concerned about integration risk, especially given how close this comes to your Kettle deal. So can you comment on integration risk, how you look at it now after having integrated two pretty large businesses?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

We feel that the integration risk of this business at first glance would be lower on the average work per day that we would be doing in that Pringles, in a lot of ways, is more like some of our other snack portfolios than was Kettle in terms of its supply chain characteristics and some of its manufacturing processes.

So secondly, with the Company being quite a large company but really producing a majority of the product out of two manufacturing facilities -- one in Jackson, Tennessee, and one in Mechelen, Belgium -- it's really quiet operationally streamlined. There is some low-speed lines that are local market lines that they have in Malaysia and in China which they are working with a partnership, but the primary volume is produced out of these two manufacturing facilities.

They are all branded. It's very consistent in terms of -- the nature of the business is quite consistent in the way they have executed the strategy, which makes it quite a clean business for us to try to integrate into our business. So we are excited about it. We think that we learned a lot with our prior acquisitions about what it takes to effectively integrate a business.

The fact that we are finished, virtually finished, with all of our Kettle integration activity is, I think, beneficial in that we are still fresh from remembering what we didn't do as well and remembering the things that did work well.

The final thing is when you look at the two biggest markets, and we mentioned this in the script, that the US two largest markets -- the two largest markets for Pringles are the US and the UK. That is about 54% of their sales. And that would be our two largest markets where we have basically a fully vetted, go-to-market supply chain distribution system. By combining those two businesses we are going to get some real efficiency and leverage and hopefully be able to do even more with the two brands combined.
So we feel well prepared for -- we are looking forward to taking it on. Our concluded integration is there a great opportunity to help make you better as a company. Procter & Gamble has led the industry in many of their practices in terms of how they manage their facilities and their go-to-market strategies. We will try to leverage those strengths as we bring that business into Diamond and to use this opportunity to become a better company ourselves.

**Akshay Jagdale - KeyBanc Capital Markets - Analyst**

And just one last one for Steve. Steve, I jumped on a little bit late. I may have missed this, but how do you get to your $25 million in synergies? On the surface it sounds slightly low, but can you help me understand that. And the second one for you, Steve, is where does the collar kick in?

**Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer**

Okay. The synergies are when you take the Pringles stand-alone business and you combine it with us there is obviously overlapping services like corporate services that gets allocated to the Pringles business that we would have here and wouldn't have to replicate. So that is going to -- would be where our primary focus is.

Whether the $25 million is low or not, we certainly are targeted to get to $25 million and, frankly, what we want to do out the shoot is continue to invest behind the brand. So if we do, in fact, realize more then we will invest that back in the brand.

The collar kicks in in advance of the exchange offer period when we get near close. It's a formula that would compare to the stock price that the transaction was based on. So that is not until in advance of the exchange period; in late fall is where we expect it would land.

**Akshay Jagdale - KeyBanc Capital Markets - Analyst**

Perfect. So the synergies are purely cost synergies that you have at this point?

**Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer**

That is what the $25 million is based on. And as you know, very similar to Pop Secret and Kettle, we did experience significant revenue synergies with those brands and their effect on our existing brand portfolio. What we have done is invested that back into the growth of the brand so we don't want to lean out too far and not completely bring everything to the bottom line and not invest back into that brand, because this is a long-term investment.

But, yes, that $25 million is predominately cost synergies and just overlap cost that -- the corporate allocations that we would not have to incur.

**Akshay Jagdale - KeyBanc Capital Markets - Analyst**

Perfect, thanks a lot. I will pass it along.

**Operator**

Mitch Pinheiro, Janney Capital Markets.
Mitch Pinheiro - Janney Montgomery Scott - Analyst

Good morning. I jumped on a little late. Just had a couple questions, hopefully they haven't been answered. But the $100 million in one-time costs over the next two years, what are they?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Yes, I will take that, Mitch. Steve Neil here. It’s a combination of actually the transaction costs to put the deal together as well as costs as we are moving to stand-alone operations.

As I am sure you understand, Pringles is right now very much a part of P&G and the whole P&G infrastructure and we have to set that up as a part of the Diamond infrastructure. So that is going to happen over a period of time.

One thing to mention too on -- I think Akshay asked about integration risks. We do have a transition services agreement that will last for 12 months post closing. As we transition from the support services that P&G is supplying today to stand-alone operations there is going to be a cost associated with setting those up.

Mitch Pinheiro - Janney Montgomery Scott - Analyst

Of the $100 million how much is cash versus non-cash?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Good question. We really haven’t gotten to that granular detail, but I would say most of it is cash. There could be some -- there will be some non-cash, but I think you should assume that most of it will be cash related.

Mitch Pinheiro - Janney Montgomery Scott - Analyst

Okay. And then just one last question. In the current Pringles business what is their marketing spending as a percentage of sales or dollars or how you could frame that for us?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

I will give you an estimate. Again, one of the things that we don't have today is to make sure that their classification of marketing and advertising being similar to ours, so I am only going to qualify that. But their spending rate is about what we see on our snack brands and so it’s going to be somewhere in the upper single digits as a percentage of sales.

So somewhere 7% to 8% is what they have been spending and we would expect a similar level. Again, I qualify that just a bit because the classification of the costs may be slightly different, but that should give you a flavor.

Mitch Pinheiro - Janney Montgomery Scott - Analyst

Okay. And then actually I did -- one more question. When I look at Pringles’ performance over the last 12 weeks, it’s certainly picking up from being sort of declining sales to mid-single digit, maybe even higher, sales based on IRI. What has been happening? Could you talk about that a little bit? What has been happening over the last quarter or so with Pringles?
Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Well, you know what, we have been monitoring them over the last six to eight months and I would say, by and large, they have repositioned their pack size to get them out of this $1 price point issue. And it has allowed them to promote in a manner that the promotional level wasn't probably hitting the depth that they had to do to hit this $1 price point. They will probably get more frequency.

And I think their current promotional model is somewhat different than their tried-and-true prior 15-year model, so I think they are still refining that. But the broader trends in North America have seen two things. One is in the measured channel starting to see some solid uptick, but we have been more pleased in what they have been able to do in the value channel and the mass channel in particular. They have basically reestablished a foothold there and are getting a lot more display activity.

And so we think the brand health is generally good right now, but it's on a trajectory for flat to single-digit growth absent more investment. That is probably where we will get involved and look to try to provide some more resources to see that growth rate expand over time.

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Mitch, let me just add a bit. I am going to state the obvious here. Clearly, Procter & Gamble runs this business until we take it over so they are certainly going to continue to run their play.

And our visibility is limited to a certain extent to what they have announced or mentioned publicly. I think if you look at their last few earnings calls, when they do mention their Snacks division, across most geographies they have seen nice strong growth. And I think that is indicative of them continuing to invest behind the brand.

As Michael noted, they increased the spending here roughly $20 million in their fiscal 2011 fiscal year. So, again, we have to be careful that -- we can't run the business until we get it, but certainly they are doing the things that we think are the appropriate things to do.

Mitch Pinheiro - Janney Montgomery Scott - Analyst

By the way, I have said last question twice. I do have one more question; I promise this is the last. Are there any distribution channels, c-store, dollar store, drugstore that Pringles would be underpenetrated in and considered perhaps an opportunity?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Well, it's an interesting question. Their development in the c-store area compared to the national chip brand the percentage would be low. However, compared to our snack portfolio that penetration is quite high, so it depends, I guess, on where you come from.

I do think that our combined platform of offerings is very interesting and meaningful. We already have seen some real benefits of putting Kettle and Pringles together as a portfolio of products to offer into that convenience segment, and Pringles is going to really be a great addition to that effort. So we will look to leverage that.

But they do have -- in fairness, they do have a nice footprint there. We would like to expand that and at the same time enter with many of our other products in that same area, so we will be concentrating more in that segment.
I do think that compared to us we are quite developed. Maybe 75% of our sales are in the food category, in the traditional food. Of their sales maybe 25% are in that food segment. So our heightened attention on food and merchandising of food, hopefully, that will be an area that combined as a food company we can perhaps do a little more there.

I think their development in club, in mass, and drug and some of the value channels; they have penetration where we don't in customers that we should or could have a nice business with a certain part of our offering so we are going to leverage that footprint. So that will be a very nice combination for us in North America and UK.

Mitch Pinheiro - Janney Montgomery Scott - Analyst

All right, thank you very much.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Thank you.

Operator

Jane Gelfand, Barclays Capital.

Jane Gelfand - Barclays Capital - Analyst

Good morning, everyone. Just a quick question. For those of your shareholders who have kind of grown up with a Diamond Foods starting with primarily a culinary business that was in the running for a snacks kind of nut claim and then as you have added on Pop Secret and Kettle and so on, a lot of shareholders have come to view Diamond as this kind of smaller but growthier player. Clearly Pringles takes you in a little bit of a different kind of echelon being a more mainstream snack player.

So I guess for -- how would you get investors more comfortable with that transition given that there is a natural evolution that goes with it? Any concerns that you probably already anticipate hearing about, how do you begin to address them?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Well, the Pringles brand, as we noted, is being sold in over 140 different countries. When you deconstruct the brand positioning in the 60% of the world outside of the United States it is definitely enjoying a premium positioning relative to other chips or potato crisps in those markets. And its pricing position reflects that. So I think that is one consideration.

I think in the US Pringles has done a nice job of developing platform extensions, such as the gold product line, the multi-grain product line, their new sticks product line, and they do have development with a younger demographic that will be quite complementary to Diamond in that maybe our demographic skews just a tad bit older. I think it's going to be beneficial to our product line to be able to really get our arm around that demographic.

I think that you put the two companies together we are still, compared to the majors CPG companies, a relatively small company but a very focused company. So I think that a lot of times the issues around speed and the ability to grow are around your ability to focus. We think that being a pure-play snack company we are going to very much be able to focus.

We don't have a series of $20 million, $30 million brands here. We have got four snack brands and a culinary -- we have five brands. We are very focused on those brands and I think that we should be able to grow those brands over time.
We will -- one thing that Pringles does provide for us is scale in markets that matter. Our total sales of the Company combined, 49% of our sales will be outside of the United States. That platform that Pringles provides for us will be a great opportunity for us to sell Pringles as well as other products, and we look to leverage that.

So I feel very good about this business becoming more growthy than it is today. When we have had a chance to own the business, work closely with our in-scope employees, together craft the plans of what our new team believes we should do to help take this brand to the next level, we will be coming with some granularity about what that growth rate should look like.

I do think that it’s -- as a practicality, Procter & Gamble is a great company, gross margin structures north of 50%. A business like this in their portfolio with a gross margin in the 30%s, very hard to see how they could afford to invest in the business, say they can improve the gross margin by 5%, it’s still going to be margined dilutive to them.

Hard to see this being a part of the strategy in context of the kind of company they are on the beauty care side and this business for us works well and we are going into it looking to invest to make it more valuable. And how much it grows on the top line will be something we look forward to demonstrating in a lot more clarity after we close the transaction.

Jane Gelfand - Barclays Capital - Analyst

Perfect. Thanks so much. Then just maybe honing in on the international piece of the business, as we think about you building scale abroad, clearly there needs to be an ongoing distribution network, sales and marketing support. That is so critical to a geography that has far more momentum. So there is a transition services agreement in place for the first 12 months, but then what do you anticipate in terms of kind of plugging some of those holes where, right now, the P&G corporate salesforce is really responsible for some of that?

I know that there are third-party brokers in some regions, but how much -- I guess how much of that international exposure really is something that you have to address from a filling and distribution and marketing support standpoint that P&G will exit over time?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

That is a good question. Let me sort of break it down in component parts. So this 54% of the current Pringles sales that go through the US and the UK, and we have a team, which we will strengthen that seem in the context of larger business, but we have fundamentally the structure which we will manage that business of those two markets.

Then if you look at the rest of the world, I would say there is 20% to 25% of the sales in the rest of the world where we have an exclusive distribution broker relationship that Procter & Gamble has formed over years, and those relations will transfer over to us as Diamond Foods and we will sustain that relationship and build that partnership and work in those markets with those partners.

So what that really leaves is about 20% of the world that we have an opportunity to determine the best way to go to market in context of our current company. And we will make that decision on a market-by-market basis and we will use the 300 plus administrative level management members that are coming to us from Procter & Gamble to help us make that decision.

We have got some ideas. We have actually have a vetted plan that we would execute in the event that we needed to make a plan today. I would consider -- it’s a base plan and the fact that, again, we are getting a lot of great employees from Procter & Gamble joining us with the Pringles asset -- the leadership team in Cincinnati, in Singapore, in Asia. We look forward to them being a part of that decision.
So I would say that that is going to be an area that we plan to spend a bit more, if necessary, to have best-of-breed go-to-market strategy in those regions.

And so earlier I think someone commented our synergies seemed a bit low. I think one thing is we are trying to be wise to know there is probably going to be some dissynergies in some places where we can do a great job, but because we are not as big as Procter & Gamble our cost efficiency would not be as attractive. That doesn't mean that if we are going to have a little more cost that we can't get a lot more value with it being a Diamond Foods dedicated team.

So that would broadly kind of capture our thinking on that area.

Jane Gelfand - Barclays Capital - Analyst

Perfect. And then just two quick questions. I am just wondering on your EPS accretion guidance does that include an estimate for non-cash intangibles amortization and past RMT as we have seen those intangibles get marked up. That is usually a big bite out of at least GAAP earnings or -- not necessarily cash earnings, but wondering what that estimate is.

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Yes and the answer is, yes, it does. The expanded answer is and of course we have got to go through the valuation of the company from a purchase price allocation perspective. So today they are our best estimates but, yes, they do include it.

Clearly, as we close the transaction and work through those details they are likely to change somewhat, but we do have estimates for the step up in basis for those intangible assets, yes.

Jane Gelfand - Barclays Capital - Analyst

And then finally can you just give us a little bit of detail on -- clearly Pringles has more exposure to some inflationary agricultural commodities. Just given that this transition is going to be happening in what is a volatile kind of commodity market, what is the input cost situation look like? What do the hedges look like, if you can share that?

And then how much pricing has already been put through to try and offset or anticipate some of that inflationary pressure as it's coming on line?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Yes, I will take that. I would say that the commodity makeup is similar to what we experienced in Kettle Foods actually in Pop Secret where the core commodity, in this case potatoes, are less than 20% of the cost of goods sold. Oil is less than potatoes, etc.

So I think from an overall exposure to commodities it's managed. Certainly there has been some impact this year that has been experienced, but we feel it's pretty well managed. Most of the commodities that are utilized in the product there isn't an exchange that you can cover them on. In other words, potatoes aren't traded on the exchange. There are some surrogates that you can hedge.

But I think the move that Pringles and P&G management made several years ago to move off of a fixed price that had to absorb all commodity increases, obviously there will be some movement in price and certainly we don't patrol that piece of the business. But as we have looked at it we feel comfortable enough to give you estimates on our fiscal 2012 impact. We would say that it appears that the commodity impact, whether it's offset by efficiencies or offset by pricing, is well controlled.
Jane Gelfand - Barclays Capital - Analyst
Thank you for all the detail.

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer
Thanks, Jane.

Operator
Robert Moskow, Credit Suisse.

Robert Moskow - Credit Suisse - Analyst
I guess my first question is why didn't I pickup coverage of your company when I had the chance four years ago.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO
You know, Robert, that is big of you to say that but you know it's never too late.

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer
Right. We are always open for opportunities.

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO
I welcome an initiation with a buy.

Robert Moskow - Credit Suisse - Analyst
Well, great. I guess my only question would be it reminds me a little bit, I guess not much, of Ralcorp acquisition of Post, the Reverse Morris Trust structure. But I think one of the lessons that they learned is that when they combined two cereal organizations is that they have two separate sales forces and they don't necessarily cooperate with each other.

I have heard a lot about how you intend to combine the organizations, but I am not quite sure I get are you combining sales forces. And is it your expectation -- can you give us a little more detail as to what scale actually gets you with your customers? It's the same products, but is it -- specifically is it to the ability to fill up trucks, is this the ability to put multiple products on a display that you couldn't do before, or is this really just kind of like a whitespace opportunity where maybe Pringles had some distribution that Diamond didn't?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO
Let me speak to it broadly and hopefully I will get -- and double back if I didn't answer your question well.
One of the things that is -- about this transaction that is particularly attractive for us is that in the two markets that we have the sales and go-to-market infrastructure, by the nature of the way P&G is structured, sales people will not be coming over to us in any meaningful way as part of the bodies that we will get. So there won’t be two sales forces; there will be one single sales force.

We are excited to get the members of their team that are in scope that would like to be part of our organization and providing them exciting, meaningful roles in our organization. But the beauty is we are going to be a net hiring -- we will be on the net hiring people to fill voids that are currently being serviced by corporate Procter in a number of areas and sales will be one of those, both in the US and the UK.

As far as the relationship with our customers, every day we are doing our best to try to find optimal placement for our snack products on the shelf and working with the snack buyer and helping them consider the merits of their planogram. How meaningful you are in the aggregate to them is one of the ways you become of import to influence that planogram.

With this kind of scale we are hoping to have more meaning and more value and staff our organization in a way to better influence where our products are located on the shelf and how fast they get on the shelf. And to create display events where we get off-shelf display for a combination of our snack products during events and that we can have enough scale in this collective portfolio to get those important off-shelf events that our retail partners have a lot of people curry favor to get those events.

So the dollar -- to get a promotional event for the retailer they have an expectation of the kind of turnover you can yield when you have that special event. Obviously, given the kind of dollar movement Pringles can generate, that can be a very helpful addition to our portfolio. It’s just another way we can help them be successful and I think it’s going to be very complementary to what we already do.

Robert Moskow - Credit Suisse - Analyst
Okay, that is very helpful and congratulations again. Thanks.

Operator
Eric Katzman, Deutsche Bank.

Eric Katzman - Deutsche Bank - Analyst
Good morning, everybody. A couple of questions. How much of the business is through the food service channel, Pringles that is?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO
It’s a pretty small percentage.

Eric Katzman - Deutsche Bank - Analyst
Okay. Then second question has to do with -- I think maybe somebody asked this in part. But on the synergies typically the acquired company can generate, call it, on average 6% of sales as savings within three years. The $25 million I assume in the first year, would that -- so is that a reasonable target? Or is it the fact they basically just have two manufacturing facilities that are pretty manufacturing efficient limits what has kind of been the traditional measure for cost synergies?
Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Well, again I would remind you that, unlike some of the RMTs done in the US lately where it was 100% of the business was in the same geography, in this case 54% of the business are in markets that we have strong distribution footprint. The balance we would not have similar distribution; we have business but it would not be similar businesses that would provide us the normal synergy opportunity in those areas. And there might be a little bit of dissynergy in some of those markets. So I think that is one thing to factor down that expectation.

The second thing is that we will look to invest against these brands and redeploy those dollars back into the value proposition of the brands that we are selling. So I feel confident that we will capture more synergies but I don't know if those would be -- I wouldn't be baking those in and drop to the bottom line.

Our mindset is to try to -- that we can hit our earnings projections as we will outline, but that those incremental synergies we would like to invest against these brands. So that is how we are looking at it at this point in time.

Eric Katzman - Deutsche Bank - Analyst

Okay. And then two more. One, as a follow-up to Rob's question, did you say that there was no meaningful sales force coming with the business?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Yes, that is correct.

Eric Katzman - Deutsche Bank - Analyst

And that is because Procter basically -- I mean this was pretty much of an orphan brand within their global operation, so they didn't really have anybody dedicated in terms of sales. So do you see that as an opportunity, given the flat sales performance of the business over the last couple years?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

Well, I think that they were mindful that it was the last food asset that they had and they had elected to work with Acosta nationally in the last year to provide sales support function to try to provide more focus from a partner who was focused in the food area. Happens to be that Acosta is our national broker in supermarkets; hopefully we will have some good collaboration in that process.

I would hope that given that this is a brand that we saw as very additive to us and with a fresh disposition and energy -- it is what we do, we are a food company -- that it will get lot of attention and it will get a lot of energy and effort. And that, hopefully, we can yield results.

I do know that the incremental margin threshold for news sales in a company like ours would probably be lower than it would be for someone like Procter & Gamble, which means that I think we will have more chances to do things with new products that bring value to consumers than might be -- than Procter & Gamble might have based on kind of the bar that they had to clear to be incrementally margin accretive in the company. So we are going to work it and we will know a lot more after we have owned the business for a year.
Eric Katzman - Deutsche Bank - Analyst

Okay. And then just last one. Has the Board, your Board, considered how you are going to, I guess, get stock into the hands some of the senior managers that are coming over? I would think from, again kind of being somewhat of an orphan brand within global P&G to being a very focused snack entity, they would be probably pretty excited. Are you going to -- does the Board or the transaction provide for that?

Michael Mendes - Diamond Foods, Inc. - Chairman, President & CEO

We are very enthusiastic about creating an attractive home for the Pringles employees who are interested in coming to Diamond Foods. We are a big believer that one of the greatest economic values we provide our shareholders is a chance to participate in the equity in the Company and so that will definitely be a consideration in the total package we will try to put together for at least the leadership team.

Our effort will be to have very granular discussions and to listen closely to try to understand what -- and to not -- I am going to try not to project our sensibility of what total comp should look like and what those component parts should look like. We are going to really try to listen and learn and put together a compensation package that gets people excited and rewards the right kind of behavior. But I do believe that equity will be an important part of that.

Eric Katzman - Deutsche Bank - Analyst

Okay, I will pass it on. Thank you.

Operator

Tim Ramey, D.A. Davidson.

Tim Ramey - D.A. Davidson - Analyst

Steve, I was just wondering if you could give us some of the actual details of the collar since your stock is up 8% or 9% in the pre-market. What does that do to the amount of debt that gets assumed?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Yes, and I won't speculate here. What the collar on the share price -- but what the collar does is it allows us to -- if the share price is above the strike price or the negotiated price that we had, then we will reduce our debt up to $150 million. And if the price during the measurement period in advance of the exchange offer is below the strike price, then it would potentially increase our debt $200 million.

So in this instance, let's say if it is up, and I don't know what the market is doing, but if it is up then it would reduce our overall leverage, which obviously would be a good thing. Our projections, of course, are that it was going to be right on the strike price, so that would be a benefit. If it goes below then we absorb a little bit more of debt at the closing of the transaction.

Tim Ramey - D.A. Davidson - Analyst

Is that dollar for dollar, Steve, or is there a ratio on sort of the value of an equity improvement versus debt reduction?
Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Yes, it is dollar for dollar up and down around the collar. So it obviously depends on where the price is in advance of the exchange period, but, yes, it is dollar for dollar.

Tim Ramey - D.A. Davidson - Analyst

Good. And on the TSA, is there any early exit provisions on that, much like you did with General Mills where I think you were successful at reducing your integration costs by exiting the TSA early?

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Yes, I think there is certainly the incentive, and I would say it's not all cost driven at all. There is certainly an incentive for us to run the business stand-alone very, very similar to what we did with Pop Secret, as you mentioned. This being an international company and fantastic systems and infrastructure that comes with P&G I think our focus is going to be more on leveraging what they did and their positive skills in supporting the business.

And to the extent that we can get out early with equal to or better performance we will definitely do that, but it's more let's make sure we get the substance. They provide a fantastic, somebody back to lean on as we execute and focus on the business. So I think that is certainly a nice, in a sense safety valve, that we have. But we will convert as soon as we are ready to convert within that time frame.

Tim Ramey - D.A. Davidson - Analyst

Terrific, thanks.

Steve Neil - Diamond Foods, Inc. - EVP, Chief Financial & Administrative Officer

Thanks, Tim.

Operator

This concludes our question-and-answer session today. I would like to turn the conference back over to Ms. Segre for additional or closing remarks.

Linda Segre - Diamond Foods, Inc. - SVP, Corporate Strategy and Communications

We will now conclude this call. Thank you all for joining us. Goodbye.

Operator

This concludes today's conference. We appreciate your participation.
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