

KELLOGG COMPANY
2009 ANNUAL REPORT

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Kellogg Company and Subsidiaries

Consolidated Statement of Income

(millions, except per share data)	2009	2008	2007
Net sales	\$12,575	\$12,822	\$11,776
Cost of goods sold	7,184	7,455	6,597
Selling, general and administrative expense	3,390	3,414	3,311
Operating profit	\$ 2,001	\$ 1,953	\$ 1,868
Interest expense	295	308	319
Other income (expense), net	(22)	(14)	(3)
Income before income taxes	1,684	1,631	1,546
Income taxes	476	485	444
Net income	\$ 1,208	\$ 1,146	\$ 1,102
Net loss attributable to noncontrolling interests	(4)	(2)	(1)
Net income attributable to Kellogg Company	\$ 1,212	\$ 1,148	\$ 1,103
Per share amounts:			
Basic	\$ 3.17	\$ 3.01	\$ 2.79
Diluted	\$ 3.16	\$ 2.99	\$ 2.76
Dividends per share	\$ 1.430	\$ 1.300	\$ 1.202

Refer to Notes to Consolidated Financial Statements.

Consolidated Balance Sheet

(millions, except share data)	2009	2008
Current assets		
Cash and cash equivalents	\$ 334	\$ 255
Accounts receivable, net	1,093	1,100
Inventories	910	897
Other current assets	221	269
Total current assets	\$ 2,558	\$ 2,521
Property, net	3,010	2,933
Goodwill	3,643	3,637
Other intangibles, net	1,458	1,461
Other assets	531	394
Total assets	\$11,200	\$10,946
Current liabilities		
Current maturities of long-term debt	\$ 1	\$ 1
Notes payable	44	1,387
Accounts payable	1,077	1,135
Other current liabilities	1,166	1,029
Total current liabilities	\$ 2,288	\$ 3,552
Long-term debt	4,835	4,068
Deferred income taxes	425	300
Pension liability	430	631
Other liabilities	947	940
Commitments and contingencies		
Equity		
Common stock, \$.25 par value, 1,000,000,000 shares authorized Issued: 419,058,168 shares in 2009 and 418,842,707 shares in 2008	105	105
Capital in excess of par value	472	438
Retained earnings	5,481	4,836
Treasury stock at cost 37,678,215 shares in 2009 and 36,981,580 shares in 2008	(1,820)	(1,790)
Accumulated other comprehensive income (loss)	(1,966)	(2,141)
Total Kellogg Company equity	2,272	1,448
Noncontrolling interests	3	7
Total equity	2,275	1,455
Total liabilities and equity	\$11,200	\$10,946

Refer to Notes to Consolidated Financial Statements.

Consolidated Statement of Cash Flows

(millions)	2009	2008	2007
Operating activities			
Net income	\$ 1,208	\$1,146	\$ 1,102
Adjustments to reconcile net income to operating cash flows:			
Depreciation and amortization	384	375	372
Deferred income taxes	(40)	157	(69)
Other	13	121	184
Pension and other postretirement benefit contributions	(100)	(451)	(96)
Changes in operating assets and liabilities:			
Trade receivables	(75)	48	(63)
Inventories	(13)	41	(88)
Accounts payable	(59)	32	167
Accrued income taxes	112	(85)	(67)
Accrued interest expense	(5)	3	(1)
Accrued and prepaid advertising, promotion and trade allowances	91	(10)	36
Accrued salaries and wages	21	(45)	5
Exit plan-related reserves	21	(2)	(9)
All other current assets and liabilities	85	(63)	30
Net cash provided by operating activities	\$ 1,643	\$1,267	\$ 1,503
Investing activities			
Additions to properties	\$ (377)	\$ (461)	\$ (472)
Acquisitions of businesses, net of cash acquired	—	(213)	(128)
Other	7	(7)	(1)
Net cash used in investing activities	\$ (370)	\$ (681)	\$ (601)
Financing activities			
Net increase (reduction) of notes payable, with maturities less than or equal to 90 days	\$(1,284)	\$ 23	\$ 625
Issuances of notes payable, with maturities greater than 90 days	10	190	804
Reductions of notes payable, with maturities greater than 90 days	(70)	(316)	(1,209)
Issuances of long-term debt	1,241	756	750
Reductions of long-term debt	(482)	(468)	(802)
Net issuances of common stock	131	175	163
Common stock repurchases	(187)	(650)	(650)
Cash dividends	(546)	(495)	(475)
Other	5	5	6
Net cash used in financing activities	\$(1,182)	\$ (780)	\$ (788)
Effect of exchange rate changes on cash and cash equivalents	(12)	(75)	(1)
Increase (decrease) in cash and cash equivalents	\$ 79	\$ (269)	\$ 113
Cash and cash equivalents at beginning of year	255	524	411
Cash and cash equivalents at end of year	\$ 334	\$ 255	\$ 524

Refer to Notes to Consolidated Financial Statements.

NOTE 4 EQUITY

Earnings per share

Basic net 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 net 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 are comprised principally of employee stock options issued by the Company. The total number of anti-dilutive potential common shares excluded from the reconciliation for each period was (in millions): 2009–12.2; 2008–2.6; 2007–0.8. Basic net earnings per share is reconciled to diluted net earnings per share in the following table:

(millions, except per share data)	Net income attributable to Kellogg Company	Average shares outstanding	Net earnings per share
2009			
Basic	\$1,212	382	\$3.17
Dilutive potential common shares	—	2	(.01)
Diluted	\$1,212	384	\$3.16
2008			
Basic	\$1,148	382	\$3.01
Dilutive potential common shares	—	3	(.02)
Diluted	\$1,148	385	\$2.99
2007			
Basic	\$1,103	396	\$2.79
Dilutive potential common shares	—	4	(.03)
Diluted	\$1,103	400	\$2.76

Stock transactions

The Company issues shares to employees and directors under various equity-based compensation and stock purchase programs, as further discussed in Note 7. The number of shares issued during the periods presented was (in millions): 2009–3; 2008–5; 2007–4. The Company issued shares totaling less than one million in each of the years presented under *Kellogg Direct*TM, a direct stock purchase and dividend reinvestment plan for U.S. shareholders.

The Board of Directors authorized stock repurchases of up to \$650 million for 2009. During 2009, the Company spent \$187 million to purchase approximately 4 million shares of common stock. The unused portion of the 2009 authorization, amounting to \$463 million, was rolled over and is available to be

executed in 2010. The Board of Directors has authorized an additional stock repurchase program of up to \$650 million for 2010. During 2008 and 2007, the Company repurchased \$650 million of common stock each year under programs authorized by its Board of Directors. The number of shares repurchased amounted to approximately 13 million and 12 million shares, respectively, in 2008 and 2007.

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 for the periods presented consists of foreign currency translation adjustments, unrealized gains and losses on cash flow hedges and adjustments for net experience losses and prior service cost associated with defined benefit pension and other postretirement plans.

During 2008, the assets of the Company's postretirement and postemployment benefit plans suffered losses of over \$1 billion due to the substantial allocation of assets in the equity market. These losses are recognized in other comprehensive income and for pension plans is recognized in the calculated value of plan assets over a five-year period and once recognized, are amortized using a declining-balance method over the average remaining service period of active plan participants.