

KELLOGG CO
Form 10-K
February 29, 2012

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the Fiscal Year Ended December 31, 2011

.. **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

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of Incorporation

or organization)

38-0710690
(I.R.S. Employer Identification No.)

One Kellogg Square
Battle Creek, Michigan 49016-3599
(Address of Principal Executive Offices)

Registrant's telephone number: (269) 961-2000

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Securities registered pursuant to Section 12(b) of the Securities Act:

Title of each class:
Common Stock, \$.25 par value per share

Name of each exchange on which registered:
New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Securities Act: None

Indicate by a check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15 (d) of the Act. Yes No

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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. (Check one)

Large accelerated filer 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 Act). Yes No

The aggregate market value of the common stock held by non-affiliates of the registrant (assuming for purposes of this computation only that the W. K. Kellogg Foundation Trust, directors and executive officers may be affiliates) as of the close of business on July 2, 2011 was approximately \$15.5 billion based on the closing price of \$55.40 for one share of common stock, as reported for the New York Stock Exchange on that date.

As of January 28, 2012, 357,161,392 shares of the common stock of the registrant were issued and outstanding.

Parts of the registrant's Proxy Statement for the Annual Meeting of Shareowners to be held on April 20, 2012 are incorporated by reference into Part III of this Report.

PART 1.

ITEM 1. BUSINESS

The Company. Kellogg Company, founded in 1906 and incorporated in Delaware in 1922, and its subsidiaries are engaged in the manufacture and marketing of ready-to-eat cereal and convenience foods.

The address of the principal business office of Kellogg Company is One Kellogg Square, P.O. Box 3599, Battle Creek, Michigan 49016-3599. Unless otherwise specified or indicated by the context, Kellogg, we, us and our refer to Kellogg Company, its divisions and subsidiaries.

Financial Information About Segments. Information on segments is located in Note 16 within Notes to the Consolidated Financial Statements.

Principal Products. Our principal products are ready-to-eat cereals and convenience foods, such as cookies, crackers, toaster pastries, cereal bars, fruit-flavored snacks, frozen waffles and veggie foods. These products were, as of February 28, 2012, manufactured by us in 17 countries and marketed in more than 180 countries. Our cereal products are generally marketed under the **Kellogg** s name and are sold principally to the grocery trade through direct sales forces for resale to consumers. We use broker and distributor arrangements for certain products. We also generally use these, or similar arrangements, in less-developed market areas or in those market areas outside of our focus.

We also market cookies, crackers, and other convenience foods, under brands such as **Kellogg** s, **Keebler**, **Cheez-It**, **Murray**, **Austin** and **Famous Amos**, to supermarkets in the United States through a direct store-door (DSD) delivery system, although other distribution methods are also used.

Additional information pertaining to the relative sales of our products for the years 2009 through 2011 is located in Note 16 within Notes to the Consolidated Financial Statements, which are included herein under Part II, Item 8.

Raw Materials. Agricultural commodities, including corn, wheat, soy bean oil, sugar and cocoa, are the principal raw materials used in our products. Cartonboard, corrugated, and plastic are the principal packaging materials used by us. We continually monitor world supplies and prices of such commodities (which include such packaging materials), as well as government trade policies. The cost of such commodities may fluctuate widely due to government policy and regulation, weather conditions, climate change or other unforeseen circumstances. Continuous efforts are made to maintain and improve the quality and supply of such commodities for purposes of our short-term and long-term requirements.

The principal ingredients in the products produced by us in the United States include corn grits, wheat and wheat derivatives, oats, rice, cocoa and chocolate, soybeans and soybean derivatives, various fruits, sweeteners, flour, vegetable oils, dairy products, eggs, and other filling ingredients, which are obtained from various sources. Most of these commodities are purchased principally from sources in the United States.

We enter into long-term contracts for the commodities described in this section and purchase these items on the open market, depending on our view of possible price fluctuations, supply levels, and our relative negotiating power. While the cost of some of these commodities has, and may continue to, increase over time, we believe that we will be able to purchase an adequate supply of these items as needed. As further discussed herein under Part II, Item 7A, we also use commodity futures and options to hedge some of our costs.

Raw materials and packaging needed for internationally based operations are available in adequate supply and are sometimes imported from countries other than those where used in manufacturing.

Natural gas and propane are the primary sources of energy used to power processing ovens at major domestic and international facilities, although certain locations may use oil or propane on a back-up or alternative basis. In addition, considerable amounts of diesel fuel are used in connection with the distribution of our products. As further discussed herein under Part II, Item 7A, we use over-the-counter commodity price swaps to hedge some of our natural gas costs.

Trademarks and Technology. Generally, our products are marketed under trademarks we own. Our principal trademarks are our housemarks, brand names, slogans, and designs related to cereals and convenience foods manufactured and marketed by us, and we also grant licenses to third parties to use these marks on various goods. These trademarks include **Kellogg** s for cereals, convenience foods and our other products, and the brand names of certain ready-to-eat cereals, including **All-Bran**, **Apple Jacks**, **Bran Buds**, **Cinnamon Crunch Crispix**, **Choco Zucaritas**, **Cocoa Krispies**, **Complete**, **Kellogg** s **Corn Flakes**, **Corn Pops**, **Cracklin Oat Bran**, **Crispix**, **Cruncheroos**, **Crunchmania**, **Crunchy Nut**, **Eggo**, **Kellogg** s **FiberPlus**, **Froot Loops**, **Kellogg** s **Frosted Flakes**, **Kellogg** s **Krave**, **Frosted Krispies**, **Frosted Mini-Wheats**, **Fruit Harvest**, **Just Right**, **Kellogg** s

Low Fat Granola, Mueslix, Pops, Product 19, Kellogg's Raisin Bran, Raisin Bran Crunch, Rice Krispies, Rice Krispies Treats, Smacks/Honey Smacks, Smart Start, Kellogg's Smorz, Special K, Special K Red Berries and Zucaritas in the United States and elsewhere; *Crusli, Sucrilhos, Vector, Musli, NutriDia*, and *Choco Krispis* for cereals in Latin America; *Vive* and *Vector* in Canada; *Coco Pops, Chocos, Frosties, Fruit n Fibre, Kellogg's Crunchy Nut Corn Flakes, Honey Loops, Kellogg's Extra, Sustain, Muslix, Country Store, Ricicles, Smacks, Start, Pops, Optima* and *Tresor* for cereals in Europe; and *Cerola, Sultana Bran, Chex, Frosties, Goldies, Rice Bubbles, Nutri-Grain, Kellogg's Iron Man Food*, and *BeBig* for cereals in Asia and Australia. Additional Company trademarks are the names of certain combinations of ready-to-eat Kellogg's cereals, including *Fun Pak, Jumbo*, and *Variety*.

Other Company brand names include *Kellogg's* Corn Flake Crumbs; *All-Bran, Choco Krispis, Froot Loops, Special K, NutriDia, Kuadri-Krispis, Zucaritas* and *Crusli* for cereal bars, *Komplete* for biscuits; and *Kaos* for snacks in Mexico and elsewhere in Latin America; *Pop-Tarts* and *Pop-Tarts Ice Cream Shoppe* for toaster pastries; *Pop-Tarts Mini Crisps* for crackers; *Eggo, Eggo FiberPlus* and *Nutri-Grain* for frozen waffles and pancakes; *Rice Krispies Treats* for baked snacks and convenience foods; *Special K* and *Special K2O* for flavored protein water mixes and protein shakes; *Nutri-Grain* cereal bars, *Nutri-Grain* yogurt bars, for convenience foods in the United States and elsewhere; *K-Time, Rice Bubbles, Day Dawn, Be Natural, Sunibrite* and *LCMs* for convenience foods in Asia and Australia; *Nutri-Grain* Squares, *Nutri-Grain Elevenes*, and *Rice Krispies Squares* for convenience foods in Europe; *Kashi* and *GoLean* for certain cereals, nutrition bars, and mixes; *TLC* for granola and cereal bars, crackers and cookies; *Special K* and *Vector* for meal replacement products; *Bear Naked* for granola cereal, bars and trail mix and *Morningstar Farms, Loma Linda, Natural Touch, Gardenburger* and *Worthington* for certain meat and egg alternatives.

We also market convenience foods under trademarks and tradenames which include *Keebler, Austin, Keebler Baker's Treasures, Cheez-It, Chips Deluxe, Club, E. L. Fudge, Famous Amos, Fudge Shoppe, Kellogg's FiberPlus, Gripz, Jack's, Jackson's, Krispy, Mother's, Murray, Murray Sugar Free, Ready Crust, Right Bites, Sandies, Special K, Soft Batch, Stretch Island, Sunshine, Toasteds, Town House, Vienna Creams, Vienna Fingers, Wheatables* and *Zesta*. One of our subsidiaries is also the exclusive licensee of the *Carr's* cracker line in the United States.

Our trademarks also include logos and depictions of certain animated characters in conjunction with our products, including *Snap!Crackle!Pop!* for *Cocoa Krispies* and *Rice Krispies* cereals and *Rice Krispies Treats* convenience foods; *Tony the Tiger* for *Kellogg's Frosted Flakes, Zucaritas, Sucrilhos* and *Frosties* cereals and convenience foods; *Ernie Keebler* for cookies, convenience foods and other products; the *Hollow Tree* logo for certain convenience foods; *Toucan Sam* for *Froot Loops* cereal; *Dig Em* for *Smacks/Honey Smacks* cereal; *Sunny* for *Kellogg's Raisin Bran* and *Raisin Bran Crunch* cereals, *Coco* the Monkey for *Coco Pops* cereal; *Cornelius* for *Kellogg's Corn Flakes*; *Melvin* the Elephant for certain cereal and convenience foods; *Chocos* the Bear, *Sammy* the Seal (aka *Smaxe* the Seal) for certain cereal products.

The slogans *The Best To You Each Morning, The Original & Best, They're Gr-r-reat!, The Difference is K, One Bowl Stronger, Supercharged, Earn Your Stripes* and *Gotta Have My Pops*, are used in connection with our ready-to-eat cereals, along with *L Eggo my Eggo*, used in connection with our frozen waffles and pancakes, *Elfin Magic, Childhood Is Calling, The Cookies in the Passionate Purple Package* and *Uncommonly Good* used in connection with convenience food products, *Seven Whole Grains on a Mission* used in connection with *Kashi* all-natural foods and *See Veggies Differently* used in connection with meat and egg alternatives are also important Kellogg trademarks.

The trademarks listed above, among others, when taken as a whole, are important to our business. Certain individual trademarks are also important to our business. Depending on the jurisdiction, trademarks are generally valid as long as they are in use and/or their registrations are properly maintained and they have not been found to have become generic. Registrations of trademarks can also generally be renewed indefinitely as long as the trademarks are in use.

We consider that, taken as a whole, the rights under our various patents, which expire from time to time, are a valuable asset, but we do not believe that our businesses are materially dependent on any single patent or group of related patents. Our activities under licenses or other franchises or concessions which we hold are similarly a valuable asset, but are not believed to be material.

Seasonality. Demand for our products has generally been approximately level throughout the year, although some of our convenience foods have a bias for stronger demand in the second half of the year due to events and holidays. We also custom-bake cookies for the Girl Scouts of the U.S.A., which are principally sold in the first quarter of the year.

Working Capital. Although terms vary around the world and by business types, in the United States we generally have required payment for goods sold eleven or sixteen days subsequent to the date of invoice as 2% 10/net 11 or 1% 15/net 16. Receipts from goods sold, supplemented as required by borrowings, provide for our payment of dividends, repurchases of our common stock, capital expansion, and for other operating expenses and working capital needs.

Customers. Our largest customer, Wal-Mart Stores, Inc. and its affiliates, accounted for approximately 20% of consolidated net sales during 2011, comprised principally of sales within the United States. At December 31, 2011, approximately 18% of our consolidated receivables balance and 28% of our U.S. receivables balance was comprised of amounts owed by Wal-Mart Stores, Inc. and its affiliates. No other customer accounted for greater than 10% of net sales in 2011. During 2011, our top five customers, collectively, including Wal-Mart, accounted for approximately 33% of our consolidated net sales and approximately 46% of U.S. net sales. There has been significant worldwide consolidation in the grocery industry in recent years and we believe that this trend is likely to continue. Although the loss of any large customer for an extended length of time could negatively impact our sales and profits, we do not anticipate that this will occur to a significant extent due to the consumer demand for our products and our relationships with our customers. Our products have been generally sold through our own sales forces and through broker and distributor arrangements, and have been generally resold to consumers in retail stores, restaurants, and other food service establishments.

Backlog. For the most part, orders are filled within a few days of receipt and are subject to cancellation at any time prior to shipment. The backlog of any unfilled orders at December 31, 2011 and January 1, 2011 was not material to us.

Competition. We have experienced, and expect to continue to experience, intense competition for sales of all of our principal products in our major product categories, both domestically and internationally. Our products compete with advertised and branded products of a similar nature as well as unadvertised and private label products, which are typically distributed at lower prices, and generally with other food products. Principal methods and factors of competition include new product introductions, product quality, taste, convenience, nutritional value, price, advertising and promotion.

Research and Development. Research to support and expand the use of our existing products and to develop new food products is carried on at the W. K. Kellogg Institute for Food and Nutrition Research in Battle Creek, Michigan, and at other locations around the world. Our expenditures for research and development were approximately (in millions): 2011-\$192; 2010-\$187; 2009-\$181.

Regulation. Our activities in the United States are subject to regulation by various government agencies, including the Food and Drug Administration, Federal Trade Commission and the Departments of Agriculture, Commerce and Labor, as well as voluntary regulation by other bodies. Various state and local agencies also regulate our activities. Other agencies and bodies outside of the United States, including those of the European Union and various countries, states and municipalities, also regulate our activities.

Environmental Matters. Our facilities are subject to various U.S. and foreign, federal, state, and local laws and regulations regarding the release of material into the environment and the protection of the environment in other ways. We are not a party to any material proceedings arising under these regulations. We believe that compliance with existing environmental laws and regulations will not materially affect our consolidated financial condition or our competitive position.

Employees. At December 31, 2011, we had approximately 30,700 employees.

Financial Information About Geographic Areas. Information on geographic areas is located in Note 16 within Notes to the Consolidated Financial Statements, which are included herein under Part II, Item 8.

Executive Officers. The names, ages, and positions of our executive officers (as of February 28, 2012) are listed below, together with their business experience. Executive officers are generally elected annually by the Board of Directors at the meeting immediately prior to the Annual Meeting of Shareowners.

James M. Jenness
Chairman of the Board

Mr. Jenness has been our Chairman since February 2005 and has served as a Kellogg director since 2000. From February 2005 until December 2006, he also served as our Chief Executive Officer. He was Chief Executive Officer of Integrated Merchandising Systems, LLC, a leader in outsource management of retail promotion and branded merchandising from 1997 to December 2004. He is also a director of Kimberly-Clark Corporation.

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John A. Bryant
President and Chief Executive Officer

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Mr. Bryant has served as a Kellogg director since July 2010. In January 2011, he was appointed President

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and Chief Executive Officer after having served as our Executive Vice President and Chief Operating Officer since August 2008. Mr. Bryant joined Kellogg in March 1998, and was promoted during the next eight years to a number of key financial and executive leadership roles. He was appointed Executive Vice President and Chief Financial Officer, Kellogg Company, President, Kellogg International in December 2006. In July 2007, Mr. Bryant was appointed Executive Vice President and Chief Financial Officer, Kellogg Company, President, Kellogg North America and in August 2008, he was appointed Executive Vice President, Chief Operating Officer and Chief Financial Officer. Mr. Bryant served as Chief Financial Officer through December 2009.

Bradford J. Davidson

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Senior Vice President, Kellogg Company

President, Kellogg North America

Brad Davidson was appointed President, Kellogg North America in August 2008. Mr. Davidson joined Kellogg Canada as a sales representative in 1984. He held numerous positions in Canada, including manager of trade promotions, account executive, brand manager, area sales manager, director of customer marketing and category management, and director of Western Canada. Mr. Davidson transferred to Kellogg USA in 1997 as director, trade marketing. He later was promoted to Vice President, Channel Sales and Marketing and then to Vice President, National Teams Sales and Marketing. In 2000, he was promoted to Senior Vice President, Sales for the Morning Foods Division, Kellogg USA, and to Executive Vice President and Chief Customer Officer, Morning Foods Division, Kellogg USA in 2002. In June 2003, Mr. Davidson was appointed President, U.S. Snacks and promoted in August 2003 to Senior Vice President.

Ronald L. Dissinger

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Senior Vice President and Chief Financial Officer

Ron Dissinger was appointed Senior Vice President and Chief Financial Officer effective January 2010. Mr. Dissinger joined Kellogg in 1987 as an accounting supervisor, and during the next 14 years served in a number of key financial leadership roles, both in the United States and Australia. In 2001, he was promoted to Vice President and Chief Financial Officer, U.S. Morning Foods. In 2004, Mr. Dissinger became Vice President, Corporate Financial Planning, and CFO, Kellogg International. In 2005, he became Vice President and CFO, Kellogg Europe and CFO, Kellogg International. In 2007, Mr. Dissinger was appointed Senior Vice President and Chief Financial Officer, Kellogg North America.

Paul T. Norman

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Senior Vice President, Kellogg Company

President, Kellogg International

Paul Norman was appointed President, Kellogg International in August 2008. Mr. Norman joined Kellogg's U.K. sales organization in 1987. He was promoted to director, marketing, Kellogg de Mexico in January 1997; to Vice President, Marketing, Kellogg USA in February 1999; and to President, Kellogg Canada Inc. in December 2000. In February 2002, he was promoted to Managing Director, United Kingdom/Republic of Ireland and to Vice President in August 2003. He was appointed President, U.S. Morning Foods in September 2004. In December 2005, Mr. Norman was promoted to Senior Vice President.

Gary H. Pilnick

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Senior Vice President, General Counsel,

Corporate Development and Secretary

Mr. Pilnick was appointed Senior Vice President, General Counsel and Secretary in August 2003 and assumed responsibility for Corporate Development in June 2004. He joined Kellogg as Vice President Deputy General Counsel and Assistant Secretary in September 2000 and served in that position until August 2003. Before joining Kellogg, he served as Vice President and Chief Counsel of Sara Lee Branded Apparel

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and as Vice President and Chief Counsel, Corporate Development and Finance at Sara Lee Corporation.

Dennis W. Shuler

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Senior Vice President, Global Human Resources

Mr. Shuler joined Kellogg on February 18, 2010. In 2009, Mr. Shuler served as President of Core Strengths Management Consulting. From April 2008 to April 2009, he was Executive Vice President and Chief Human Resources Officer at The Walt Disney Company. Prior to that, Mr. Shuler served in progressively responsible human resources positions over a period of 23 years at Procter & Gamble Company in the United States and the United Kingdom, serving as Vice President of the P&G Beauty global business unit from July 2001 and the Vice President of P&G Beauty and Health & Well Being global business units from July 2006 through March 2008.

Steven A. Sterling

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Senior Vice President, Global Supply Chain

Steven Sterling joined Kellogg Company in April 2011 and was appointed Senior Vice President, Global Supply Chain. Prior to joining Kellogg, Mr. Sterling served 26 years with PepsiCo in progressively responsible supply chain positions, most recently as

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Group Vice President of Operations for Frito-Lay since 2005. Prior to that, he served in operations roles in the United States and Mexico.

Alan R. Andrews

Vice President and Corporate Controller

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Mr. Andrews joined Kellogg Company in 1982. He served in various financial roles before relocating to China as general manager of Kellogg China in 1993. He subsequently served in several leadership innovation and finance roles before being promoted to Vice President, International Finance, Kellogg International in 2000. In 2002, he was appointed to Assistant Corporate Controller and assumed his current position in June 2004.

Availability of Reports; Website Access; Other Information. Our internet address is <http://www.kelloggcompany.com>. Through Investor Relations Financials SEC Filings on our home page, we make available free of charge our proxy statements, our annual report on Form 10-K, our quarterly reports on Form 10-Q, our current reports on Form 8-K, SEC Forms 3, 4 and 5 and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission. Our reports filed with the Securities and Exchange Commission are also made available to read and copy at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. You may obtain information about the Public Reference Room by contacting the SEC at 1-800-SEC-0330. Reports filed with the SEC are also made available on its website at www.sec.gov.

Copies of the Corporate Governance Guidelines, the Charters of the Audit, Compensation and Nominating and Governance Committees of the Board of Directors, the Code of Conduct for Kellogg Company directors and Global Code of Ethics for Kellogg Company employees (including the chief executive officer, chief financial officer and corporate controller) can also be found on the Kellogg Company website. Any amendments or waivers to the Global Code of Ethics applicable to the chief executive officer, chief financial officer and corporate controller can also be found in the Investor Relations section of the Kellogg Company website. Shareowners may also request a free copy of these documents from: Kellogg Company, P.O. Box CAMB, Battle Creek, Michigan 49016-9935 (phone: (800) 961-1413), Investor Relations Department at that same address (phone: (269) 961-2800) or investor.relations@kellogg.com.

Forward-Looking Statements. This Report contains forward-looking statements with projections concerning, among other things the acquisition of the *Pringles*[®] business, our strategy, financial principles, and plans; initiatives, improvements and growth; sales, gross margins, advertising, promotion, merchandising, brand building, operating profit, and earnings per share; innovation; investments; capital expenditures; asset write-offs and expenditures and costs related to productivity or efficiency initiatives; the impact of accounting changes and significant accounting estimates; our ability to meet interest and debt principal repayment obligations; minimum contractual obligations; future common stock repurchases or debt reduction; effective income tax rate; cash flow and core working capital improvements; interest expense; commodity and energy prices; and employee benefit plan costs and funding. Forward-looking statements include predictions of future results or activities and may contain the words expect, believe, will, can, anticipate, estimate, project, should, or words or phrases of similar meaning. Forward-looking statements are found in this Item 1 and in several sections of Management's Discussion and Analysis. Our actual results or activities may differ materially from these predictions. Our future results could be affected by a variety of factors, including the ability to complete the acquisition of the *Pringles*[®] business, the impact of competitive conditions; the effectiveness of pricing, advertising, and promotional programs; the success of innovation, renovation and new product introductions; the recoverability of the carrying value of goodwill and other intangibles; the success of productivity improvements and business transitions; commodity and energy prices; labor costs; disruptions or inefficiencies in supply chain; the availability of and interest rates on short-term and long-term financing; actual market performance of benefit plan trust investments; the levels of spending on systems initiatives, properties, business opportunities, integration of acquired businesses, and other general and administrative costs; changes in consumer behavior and preferences; the effect of U.S. and foreign economic conditions on items such as interest rates, statutory tax rates, currency conversion and availability; legal and regulatory factors including changes in food safety, advertising and labeling laws and regulations; the ultimate impact of product recalls; business disruption or other losses from war, terrorist acts, or political unrest; other items; and the risks and uncertainties described in Item 1A below. Forward-looking statements speak only as of the date they were made, and we undertake no obligation to publicly update them.

ITEM 1A. RISK FACTORS

In addition to the factors discussed elsewhere in this Report, the following risks and uncertainties could materially adversely affect our business, financial condition and results of operations. Additional risks and uncertainties not presently known to us or that we currently deem immaterial also may impair our business operations and financial condition.

Our results may be materially and adversely impacted as a result of increases in the price of raw materials, including agricultural commodities, fuel and labor.

Agricultural commodities, including corn, wheat, soybean oil, sugar and cocoa, are the principal raw materials used in our products. Cartonboard, corrugated, and plastic are the principal packaging materials used by us. The cost of such commodities may fluctuate widely due to government policy and regulation, weather conditions, climate change or other unforeseen circumstances. To the extent that any of the foregoing factors affect the prices of such commodities and we are unable to increase our prices or adequately hedge against such changes in prices in a manner that offsets such changes, the results of our operations could be materially and adversely affected. In addition, we use derivatives to hedge price risk associated with forecasted purchases of raw materials. Our hedged price could exceed the spot price on the date of purchase, resulting in an unfavorable impact on both gross margin and net earnings.

Cereal processing ovens at major domestic and international facilities are regularly fueled by natural gas or propane, which are obtained from local utilities or other local suppliers. Short-term stand-by propane storage exists at several plants for use in case of interruption in natural gas supplies. Oil may also be used to fuel certain operations at various plants. In addition, considerable amounts of diesel fuel are used in connection with the distribution of our products. The cost of fuel may fluctuate widely due to economic and political conditions, government policy and regulation, war, or other unforeseen circumstances which could have a material adverse effect on our consolidated operating results or financial condition.

A shortage in the labor pool or other general inflationary pressures or changes in applicable laws and regulations could increase labor cost, which could have a material adverse effect on our consolidated operating results or financial condition.

Additionally, our labor costs include the cost of providing benefits for employees. We sponsor a number of defined benefit plans for employees in the United States and various foreign locations, including pension, retiree health and welfare, active health care, severance and other postemployment benefits. We also participate in a number of multiemployer pension plans for certain of our manufacturing locations. Our major pension plans and U.S. retiree health and welfare plans are funded with trust assets invested in a globally diversified portfolio of equity securities with smaller holdings of bonds, real estate and other investments. The annual cost of benefits can vary significantly from year to year and is materially affected by such factors as changes in the assumed or actual rate of return on major plan assets, a change in the weighted-average discount rate used to measure obligations, the rate or trend of health care cost inflation, and the outcome of collectively-bargained wage and benefit agreements.

Our operations face significant foreign currency exchange rate exposure and currency restrictions which could negatively impact our operating results.

We hold assets and incur liabilities, earn revenue and pay expenses in a variety of currencies other than the U.S. dollar, including the euro, British pound, Australian dollar, Canadian dollar, Mexican peso, Venezuelan bolivar fuerte and Russian ruble. Because our consolidated financial statements are presented in U.S. dollars, we must translate our assets, liabilities, revenue and expenses into U.S. dollars at then-applicable exchange rates. Consequently, changes in the value of the U.S. dollar may unpredictably and negatively affect the value of these items in our consolidated financial statements, even if their value has not changed in their original currency.

Concerns with the safety and quality of food products could cause consumers to avoid certain food products or ingredients.

We could be adversely affected if consumers lose confidence in the safety and quality of certain food products or ingredients, or the food safety system generally. Adverse publicity about these types of concerns, whether or not valid, may discourage consumers from buying our products or cause production and delivery disruptions.

If our food products become adulterated, misbranded or mislabeled, we might need to recall those items and may experience product liability if consumers are injured as a result.

Selling food products involves a number of legal and other risks, including product contamination, spoilage, product tampering, allergens, or other adulteration. We may need to recall some of our products if they become adulterated or misbranded. We may also be liable if the consumption of any of our products causes injury, illness or death. A widespread product recall or market withdrawal could result in significant losses due to their costs, the destruction of product inventory, and lost sales due to the unavailability of product for a period of time. For example, in June 2010, we initiated a recall of certain ready-to-eat cereals due to an odor from waxy resins found in the package liner. We could also suffer losses from a significant product liability judgment against us. A significant product recall or product liability case could also result in adverse publicity, damage to our reputation, and a loss of consumer confidence in our food products, which could have a material adverse effect on our business results and the value of our

brands. Moreover, even if a product liability or consumer fraud claim is meritless, does not prevail or is not pursued, the negative publicity surrounding assertions against our Company and our products or processes could adversely affect our reputation or brands.

Disruption of our supply chain could have an adverse effect on our business, financial condition and results of operations.

Our ability, including manufacturing or distribution capabilities, and that of our suppliers, business partners and contract manufacturers, to make, move and sell products is critical to our success. Damage or disruption to our or their manufacturing or distribution capabilities due to weather, including any potential effects of climate change, natural disaster, fire or explosion, terrorism, pandemics, strikes, repairs or enhancements at our facilities, or other reasons, could impair our ability to manufacture or sell our products. Failure to take adequate steps to mitigate the likelihood or potential impact of such events, or to effectively manage such events if they occur, could adversely affect our business, financial condition and results of operations, as well as require additional resources to restore our supply chain.

Changes in tax, environmental, food quality and safety or other regulations or failure to comply with existing licensing, labeling, trade, food quality and safety and other regulations and laws could have a material adverse effect on our consolidated financial condition.

Our activities, both in and outside of the United States, are subject to regulation by various federal, state, provincial and local laws, regulations and government agencies, including the U.S. Food and Drug Administration, U.S. Federal Trade Commission, the U.S. Departments of Agriculture, Commerce and Labor, as well as similar and other authorities of the European Union, International Accords and Treaties and others, including voluntary regulation by other bodies. The manufacturing, marketing and distribution of food products are subject to governmental regulation that impose additional regulatory requirements. Those regulations control such matters as food quality and safety, ingredients, advertising, labeling, relations with distributors and retailers, health and safety and the environment. We are also regulated with respect to matters such as licensing requirements, trade and pricing practices, tax and environmental matters. The need to comply with new or revised tax, environmental, food quality and safety or other laws or regulations, or new or changed interpretations or enforcement of existing laws or regulations, may have a material adverse effect on our business and results of operations. Further, if we are found to be out of compliance with applicable laws and regulations in these areas, we could be subject to civil remedies, including fines, injunctions, or recalls, as well as potential criminal sanctions, any of which could have a material adverse effect on our business.

If we pursue strategic acquisitions, divestitures or joint ventures, we may not be able to successfully consummate favorable transactions or successfully integrate acquired businesses.

From time to time, we may evaluate potential acquisitions, divestitures or joint ventures that would further our strategic objectives. With respect to acquisitions, we may not be able to identify suitable candidates, consummate a transaction on terms that are favorable to us, or achieve expected returns and other benefits as a result of integration challenges. With respect to proposed divestitures of assets or businesses, we may encounter difficulty in finding acquirers or alternative exit strategies on terms that are favorable to us, which could delay the accomplishment of our strategic objectives, or our divestiture activities may require us to recognize impairment charges. Companies or operations acquired or joint ventures created may not be profitable or may not achieve sales levels and profitability that justify the investments made. Our corporate development activities may present financial and operational risks, including diversion of management attention from existing core businesses, integrating or separating personnel and financial and other systems, and adverse effects on existing business relationships with suppliers and customers. Future acquisitions could also result in potentially dilutive issuances of equity securities, the incurrence of debt, contingent liabilities and/or amortization expenses related to certain intangible assets and increased operating expenses, which could adversely affect our results of operations and financial condition.

Our planned acquisition of the Pringles business may not occur or may not occur in the expected time frame, which may negatively affect the trading prices of our stock and our future business and financial results.

Completion of the planned acquisition of the Pringles business is not assured and is subject to risks and uncertainties, including the risk that the necessary regulatory approvals are not obtained or that other closing conditions are not satisfied. If the acquisition is not completed, or if there are significant delays in completing the acquisition, it could negatively affect the trading prices of our common stock and our future business and financial results.

We may not be able to obtain regulatory clearances and approvals required to complete the Pringles acquisition or, in order to do so, we may be required to accept material restrictions or satisfy material conditions.

The planned acquisition of the Pringles business is subject to review by regulatory authorities, and the closing of the transaction is subject to the condition that all waiting periods under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, have terminated or expired, that the European Commission has issued a decision under the EC Merger Regulation declaring that the acquisition is compatible with the common market, and that all other applicable governmental approvals required under antitrust laws have been obtained. The acquisition is also subject to the condition that there be no preliminary or permanent injunction or other order that would make the acquisition unlawful. We can provide no assurance that these or other closing conditions will be satisfied. Subject to certain limitations, we may be required to take certain actions in connection with obtaining antitrust clearances and other approvals, and we can provide no assurance as to the cost, scope or impact of the actions that may be required. Such actions could be detrimental to us or have the effect of delaying or preventing the acquisition.

Our obligation to complete the Pringles acquisition is not subject to a financing condition.

We intend to finance the acquisition, in part, through debt financing. However, our obligation to complete the acquisition is not subject to a financing condition. Therefore, in the event that we are unable to obtain a portion of the required financing and are not otherwise able to pay the purchase price, we will be in breach of the transaction agreement.

We may not be able to realize the anticipated benefits and synergies of the Pringles acquisition at all or in the expected time frame.

The success of the Pringles acquisition will depend, in part, on our ability to realize the anticipated benefits and synergies from combining and integrating the Pringles business into our existing business. We may not be able to achieve these objectives, or may not be able to achieve these objectives on a timely basis, and the anticipated benefits and synergies therefore may not be realized fully or at all. The acquisition involves challenges and risks, including risks that the transaction does not advance our business strategy or that we will not realize a satisfactory return. Any integration difficulties could decrease or eliminate the anticipated benefits and synergies of the Pringles acquisition and could negatively affect the trading prices of our stock and our future business and financial results.

We may incur substantial costs and liabilities relating to the Pringles acquisition.

In connection with entering into and completing the Pringles acquisition, we may incur substantial costs and liabilities. These include transaction-related costs such as costs and expenses incurred in connection with integration or pursuing synergies, fees to advisors, fees associated with seeking regulatory approvals, and other potential costs and liabilities that, individually or in the aggregate, could be substantial.

Our consolidated financial results and demand for our products are dependent on the successful development of new products and processes.

There are a number of trends in consumer preferences which may impact us and the industry as a whole. These include changing consumer dietary trends and the availability of substitute products.

Our success is dependent on anticipating changes in consumer preferences and on successful new product and process development and product relaunches in response to such changes. We aim to introduce products or new or improved production processes on a timely basis in order to counteract obsolescence and decreases in sales of existing products. While we devote significant focus to the development of new products and to the research, development and technology process functions of our business, we may not be successful in developing new products or our new products may not be commercially successful. Our future results and our ability to maintain or improve our competitive position will depend on our capacity to gauge the direction of our key markets and upon our ability to successfully identify, develop, manufacture, market and sell new or improved products in these changing markets.

We operate in the highly competitive food industry.

We face competition across our product lines, including ready-to-eat cereals and convenience foods, from other companies which have varying abilities to withstand changes in market conditions. Most of our competitors have substantial financial, marketing and other resources, and competition with them in our various markets and product lines could cause us to reduce prices, increase capital, marketing or other expenditures, or lose category share, any of which could have a material adverse effect on our business and financial results. Category share and growth could also be adversely impacted if we are not successful in introducing new products.

Potential liabilities and costs from litigation could adversely affect our business.

There is no guarantee that the Company will be successful in defending itself in civil, criminal or regulatory actions, including under environmental, food quality and safety, and environmental laws and regulations, or in asserting its rights under various laws. In addition, the Company could incur substantial

costs and fees in defending itself or in asserting its rights in these actions or meeting new legal requirements. The costs and other effects of potential and pending litigation and administrative actions against the Company, and new legal requirements, cannot be determined with certainty and may differ from expectations.

We have a substantial amount of indebtedness.

We have indebtedness that is substantial in relation to our shareholders' equity. As of December 31, 2011, we had total debt of approximately \$6.0 billion and total equity of \$1.8 billion and expect to incur an additional \$2.0 billion in debt to consummate our pending acquisition of the *Pringles*[®] business from Procter & Gamble Co.

Our substantial indebtedness could have important consequences, including:

impairing the ability to obtain additional financing for working capital, capital expenditures or general corporate purposes, particularly if the ratings assigned to our debt securities by rating organizations were revised downward.

A downgrade in our credit ratings, particularly our short-term credit rating, would likely reduce the amount of commercial paper we could issue, increase our commercial paper borrowing costs, or both;

restricting our flexibility in responding to changing market conditions or making us more vulnerable in the event of a general downturn in economic conditions or our business;

requiring a substantial portion of the cash flow from operations to be dedicated to the payment of principal and interest on our debt, reducing the funds available to us for other purposes such as expansion through acquisitions, marketing spending and expansion of our product offerings; and

causing us to be more leveraged than some of our competitors, which may place us at a competitive disadvantage.

Our ability to make scheduled payments or to refinance our obligations with respect to indebtedness will depend on our financial and operating performance, which in turn, is subject to prevailing economic conditions, the availability of, and interest rates on, short-term financing, and financial, business and other factors beyond our control.

Our performance is affected by general economic and political conditions and taxation policies.

Customer and consumer demand for our products may be impacted by recession, financial and credit market disruptions, or other economic downturns in the United States or other nations. Our results in the past have been, and in the future may continue to be, materially affected by changes in general economic and political conditions in the United States and other countries, including the interest rate environment in which we conduct business, the financial markets through which we access capital and currency, political unrest and terrorist acts in the United States or other countries in which we carry on business.

Current economic conditions in Europe may delay or reduce purchases by our customers and consumers. This could result in reductions in sales of our products, reduced acceptance of innovations, and increased price competition. Deterioration in economic conditions in any of the countries in which we do business could also cause slower collections on accounts receivable which may adversely impact our liquidity and financial condition. Financial institutions may be negatively impacted by economic conditions and may consolidate or cease to do business which could result in a tightening in the credit markets, a low level of liquidity in many financial markets, and increased volatility in fixed income, credit, currency and equity markets. There could be a number of effects from a financial institution credit crisis on our business, which could include impaired credit availability and financial stability of our customers, including our suppliers, co-manufacturers and distributors. A disruption in financial markets may also have an effect on our derivative counterparties and could also impair our banking partners on which we rely for operating cash management. Any of these events would likely harm our business, results of operations and financial condition.

The enactment of or increases in tariffs, including value added tax, or other changes in the application of existing taxes, in markets in which we are currently active or may be active in the future, or on specific products that we sell or with which our products compete, may have an adverse effect on our business or on our results of operations.

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We may be unable to maintain our profit margins in the face of a consolidating retail environment. In addition, the loss of one of our largest customers could negatively impact our sales and profits.

Our largest customer, Wal-Mart Stores, Inc. and its affiliates, accounted for approximately 20% of consolidated net sales during 2011, comprised principally of sales within the United States. At December 31, 2011, approximately 18% of our consolidated receivables balance and 28% of our U.S. receivables balance was comprised of amounts owed by Wal-Mart Stores, Inc. and its affiliates. No other customer accounted for greater than 10% of net sales in 2011. During 2011, our top five customers, collectively, including Wal-Mart, accounted

for approximately 33% of our consolidated net sales and approximately 46% of U.S. net sales. As the retail grocery trade continues to consolidate and mass marketers become larger, our large retail customers may seek to use their position to improve their profitability through improved efficiency, lower pricing and increased promotional programs. If we are unable to use our scale, marketing expertise, product innovation and category leadership positions to respond, our profitability or volume growth could be negatively affected. The loss of any large customer for an extended length of time could negatively impact our sales and profits.

An impairment of the carrying value of goodwill or other acquired intangibles could negatively affect our consolidated operating results and net worth.

The carrying value of goodwill represents the fair value of acquired businesses in excess of identifiable assets and liabilities as of the acquisition date. The carrying value of other intangibles represents the fair value of trademarks, trade names, and other acquired intangibles as of the acquisition date. Goodwill and other acquired intangibles expected to contribute indefinitely to our cash flows are not amortized, but must be evaluated by management at least annually for impairment. If carrying value exceeds current fair value, the intangible is considered impaired and is reduced to fair value via a charge to earnings. Events and conditions which could result in an impairment include changes in the industries in which we operate, including competition and advances in technology; a significant product liability or intellectual property claim; or other factors leading to reduction in expected sales or profitability. Should the value of one or more of the acquired intangibles become impaired, our consolidated earnings and net worth may be materially adversely affected.

As of December 31, 2011, the carrying value of intangible assets totaled approximately \$5.1 billion, of which \$3.6 billion was goodwill and \$1.5 billion represented trademarks, tradenames, and other acquired intangibles compared to total assets of \$11.9 billion and total equity of \$1.8 billion. An impairment charge of \$20 million was recognized in 2010 representing all of the goodwill from our 2008 acquisition of a business in China.

Economic downturns could limit consumer demand for our products.

Retailers are increasingly offering private label products that compete with our products. Consumers' willingness to purchase our products will depend upon our ability to offer products that appeal to consumers at the right price. It is also important that our products are perceived to be of a higher quality than less expensive alternatives. If the difference in quality between our products and those of store brands narrows, or if such difference in quality is perceived to have narrowed, then consumers may not buy our products. Furthermore, during periods of economic uncertainty, consumers tend to purchase more private label or other economy brands, which could reduce sales volumes of our higher margin products or there could be a shift in our product mix to our lower margin offerings. If we are not able to maintain or improve our brand image, it could have a material effect on our market share and our profitability.

We may not achieve our targeted cost savings and efficiencies from cost reduction initiatives.

Our success depends in part on our ability to be an efficient producer in a highly competitive industry. We have invested a significant amount in capital expenditures to improve our operational facilities. Ongoing operational issues are likely to occur when carrying out major production, procurement, or logistical changes and these, as well as any failure by us to achieve our planned cost savings and efficiencies, could have a material adverse effect on our business and consolidated financial position and on the consolidated results of our operations and profitability.

Technology failures could disrupt our operations and negatively impact our business.

We increasingly rely on information technology systems to process, transmit, and store electronic information. For example, our production and distribution facilities and inventory management utilize information technology to increase efficiencies and limit costs. Furthermore, a significant portion of the communications between our personnel, customers, and suppliers depends on information technology. Like other companies, our information technology systems may be vulnerable to a variety of interruptions, as a result of updating our SAP platform or due to events beyond our control, including, but not limited to, natural disasters, terrorist attacks, telecommunications failures, computer viruses, hackers, and other security issues. We have technology security initiatives and disaster recovery plans in place or in process to mitigate our risk to these vulnerabilities, but these measures may not be adequate.

Our intellectual property rights are valuable, and any inability to protect them could reduce the value of our products and brands.

We consider our intellectual property rights, particularly and most notably our trademarks, but also including patents, trade secrets, copyrights and licensing agreements, to be a significant and valuable aspect of our business. We attempt to protect our intellectual property rights through a combination of patent, trademark, copyright and trade secret laws, as well as licensing agreements, third party nondisclosure

and assignment agreements and policing of third party misuses of our intellectual property. Our failure to obtain or adequately protect our trademarks, products, new features of our products, or our technology, or any change in law or other changes that serve to lessen or remove the current legal protections of our intellectual property, may diminish our competitiveness and could materially harm our business.

We may be unaware of intellectual property rights of others that may cover some of our technology, brands or products. Any litigation regarding patents or other intellectual property could be costly and time-consuming and could divert the attention of our management and key personnel from our business operations. Third party claims of intellectual property infringement might also require us to enter into costly license agreements. We also may be subject to significant damages or injunctions against development and sale of certain products.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our corporate headquarters and principal research and development facilities are located in Battle Creek, Michigan.

We operated, as of February 28, 2012, manufacturing plants and distribution and warehousing facilities totaling more than 30 million square feet of building area in the United States and other countries. Our plants have been designed and constructed to meet our specific production requirements, and we periodically invest money for capital and technological improvements. At the time of its selection, each location was considered to be favorable, based on the location of markets, sources of raw materials, availability of suitable labor, transportation facilities, location of our other plants producing similar products, and other factors. Our manufacturing facilities in the United States include four cereal plants and warehouses located in Battle Creek, Michigan; Lancaster, Pennsylvania; Memphis, Tennessee; and Omaha, Nebraska and other plants or facilities in San Jose, California; Atlanta, Augusta, Columbus, and Rome, Georgia; Chicago, Illinois; Seelyville, Indiana; Kansas City, Kansas; Florence, Louisville, and Pikeville, Kentucky; Grand Rapids and Wyoming, Michigan; Blue Anchor, New Jersey; Cary and Charlotte, North Carolina; Cincinnati, West Jefferson, and Zanesville, Ohio; Muncy, Pennsylvania; Rossville, Tennessee; Clearfield, Utah; and Allyn, Washington.

Outside the United States, we had, as of February 28, 2012, additional manufacturing locations, some with warehousing facilities, in Australia, Brazil, Canada, Colombia, Ecuador, Germany, Great Britain, India, Japan, Mexico, Russia, South Africa, South Korea, Spain, Thailand, and Venezuela.

We generally own our principal properties, including our major office facilities, although some manufacturing facilities are leased, and no owned property is subject to any major lien or other encumbrance. Distribution facilities (including related warehousing facilities) and offices of non-plant locations typically are leased. In general, we consider our facilities, taken as a whole, to be suitable, adequate, and of sufficient capacity for our current operations.

ITEM 3. LEGAL PROCEEDINGS

We are subject to various legal proceedings, claims, and governmental inspections, audits or investigations arising out of our business which cover matters such as general commercial, governmental regulations, antitrust and trade regulations, product liability, environmental, intellectual property, employment and other actions. In the opinion of management, the ultimate resolution of these matters will not have a material adverse effect on our financial position or results of operations.

ITEM 4. MINE SAFETY DISCLOSURE

Not applicable.

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Information on the market for our common stock, number of shareowners and dividends is located in Note 15 within Notes to Consolidated Financial Statements.

On April 23, 2010, the Company's board of directors authorized a \$2.5 billion three-year share repurchase program for 2010 through 2012 for general corporate purposes and to offset issuances for employee benefit programs. During 2011, the Company repurchased 15 million shares for a total of \$793 million. In connection with the announcement of the pending acquisition of the Pringles business, the Company announced that it expects to limit its share repurchases to proceeds received by the Company from employee option exercises for approximately 2 years.

The following table provides information with respect to purchases of common shares under programs authorized by the Company's board of directors during the quarter ended December 31, 2011.

(millions, except per share data)

| Period | (a) Total Number of Shares Purchased | (b) Average Price Paid Per Share | (c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | (d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs |
|--------------------------------|---|--|---|--|
| Month #1: 10/2/11-10/29/11 | | | | \$ 755 |
| Month #2: 10/30/11-11/26/11 | 2.1 | \$ 49.80 | 2.1 | \$ 650 |
| Month #3: 11/27/11-12/31/11 | | | | \$ 650 |
| Total | 2.1 | \$ 49.80 | 2.1 | |

ITEM 6. SELECTED FINANCIAL DATA**Kellogg Company and Subsidiaries****Selected Financial Data**

| (millions, except per share data and number of employees) | 2011 | 2010 | 2009 | 2008 | 2007 |
|---|-----------|-----------|-----------|-----------|-----------|
| Operating trends (a) | | | | | |
| Net sales | \$ 13,198 | \$ 12,397 | \$ 12,575 | \$ 12,822 | \$ 11,776 |
| Gross profit as a % of net sales | 41.3% | 42.7% | 42.9% | 41.9% | 44.0% |
| Depreciation | 367 | 370 | 381 | 374 | 364 |
| Amortization | 2 | 22 | 3 | 1 | 8 |
| Advertising expense | 1,138 | 1,130 | 1,091 | 1,076 | 1,063 |
| Research and development expense | 192 | 187 | 181 | 181 | 179 |
| Operating profit | 1,976 | 1,990 | 2,001 | 1,953 | 1,868 |
| Operating profit as a % of net sales | 15.0% | 16.1% | 15.9% | 15.2% | 15.9% |
| Interest expense | 233 | 248 | 295 | 308 | 319 |
| Net income attributable to Kellogg Company | 1,231 | 1,247 | 1,212 | 1,148 | 1,103 |
| Average shares outstanding: | | | | | |
| Basic | 362 | 376 | 382 | 382 | 396 |
| Diluted | 364 | 378 | 384 | 385 | 400 |
| Per share amounts: | | | | | |
| Basic | 3.40 | 3.32 | 3.17 | 3.01 | 2.79 |
| Diluted | 3.38 | 3.30 | 3.16 | 2.99 | 2.76 |
| Cash flow trends | | | | | |
| Net cash provided by operating activities | \$ 1,595 | \$ 1,008 | \$ 1,643 | \$ 1,267 | \$ 1,503 |
| Capital expenditures | 594 | 474 | 377 | 461 | 472 |
| Net cash provided by operating activities reduced by capital expenditures (b) | 1,001 | 534 | 1,266 | 806 | 1,031 |
| Net cash used in investing activities | (587) | (465) | (370) | (681) | (601) |
| Net cash used in financing activities | (957) | (439) | (1,182) | (780) | (788) |
| Interest coverage ratio (c) | 10.0 | 9.6 | 8.0 | 7.5 | 7.0 |
| Capital structure trends | | | | | |
| Total assets | \$ 11,901 | \$ 11,847 | \$ 11,200 | \$ 10,946 | \$ 11,397 |
| Property, net | 3,281 | 3,128 | 3,010 | 2,933 | 2,990 |
| Short-term debt and current maturities of long-term debt | 995 | 996 | 45 | 1,388 | 1,955 |
| Long-term debt | 5,037 | 4,908 | 4,835 | 4,068 | 3,270 |
| Total Kellogg Company equity (d) | 1,760 | 2,158 | 2,272 | 1,448 | 2,526 |
| Share price trends | | | | | |
| Stock price range | \$ 48-58 | \$ 47-56 | \$ 36-54 | \$ 40-59 | \$ 49-57 |
| Cash dividends per common share | 1.670 | 1.560 | 1.430 | 1.300 | 1.202 |
| Number of employees | 30,671 | 30,645 | 30,949 | 32,394 | 26,494 |

(a) Fiscal year 2008 contained a 53rd week. Refer to Note 1 for further information.

(b) The Company uses this non-GAAP financial measure, which is reconciled above, to focus management and investors on the amount of cash available for debt repayment, dividend distribution, acquisition opportunities, and share repurchase.

(c) Interest coverage ratio is calculated based on net income before interest expense, income taxes, depreciation and amortization, divided by interest expense.

(d) 2008 change due primarily to currency translation adjustments of (\$431) and net experience losses in postretirement and postemployment benefit plans of (\$865).

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Kellogg Company and Subsidiaries

RESULTS OF OPERATIONS**Overview**

The following Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is intended to help the reader understand Kellogg Company, our operations and our present business environment. MD&A is provided as a supplement to, and should be read in conjunction with, our Consolidated Financial Statements and the accompanying notes thereto contained in Item 8 of this report.

Kellogg Company is the world's leading producer of cereal and a leading producer of snacks and frozen food, including cookies, crackers, toaster pastries, cereal bars, fruit-flavored snacks, frozen waffles, and veggie foods. Kellogg products are manufactured and marketed globally.

On February 15, 2012 we announced that we entered into an agreement to acquire Procter & Gamble's *Pringle's*® business for \$2.695 billion which is expected to be funded by international cash and the issuance of approximately \$2 billion of short and long-term debt. The transaction is expected to close in the Summer of 2012, as such, we expect to have *Pringle's*® included in our results for approximately six months.

Beginning in the fourth quarter of 2011, we report results of operations in the following reportable segments: U.S. Morning Foods & Kashi; U.S. Snacks; U.S. Specialty; North America Other; Europe; Latin America; and Asia Pacific. Segment results of prior periods were modified to conform to the current presentation. We currently manage our operations through nine operating segments that are based on product category or geographic location. These operating segments are evaluated for similarity with regards to economic characteristics, products, production processes, types or classes of customers, distribution methods and regulatory environments to determine if they can be aggregated into reportable segments. The reportable segments are discussed in greater detail within Note 16.

We manage our Company for sustainable performance defined by our long-term annual growth targets. These targets are 3 to 4% for internal net sales, mid single-digit (4 to 6%) for internal operating profit, and high single-digit (7 to 9%) for diluted net earnings per share (EPS) on a currency neutral basis. See the Foreign currency translation section for a discussion and reconciliation of currency neutral EPS, a non-GAAP measure.

For our full year 2011, internal net sales increased by 4% and reported net sales was up 6%. Consolidated internal operating profit was down 3% compared to the prior year. Reported operating profit decreased 1%. Diluted EPS was flat on a currency neutral basis. Reported EPS was \$3.38, an increase of 2% over last year's \$3.30.

Consolidated results

(dollars in millions, except per share data)

| | | 2011 | 2010 | 2009 |
|---|--------------|---------------|---------------|--------------|
| Net sales | | \$ 13,198 | \$ 12,397 | \$ 12,575 |
| Net sales growth: | As reported | 6.5% | (1.4)% | (1.9)% |
| | Internal (a) | 4.5% | (1.3)% | 3.0% |
| Operating profit | | \$ 1,976 | \$ 1,990 | \$ 2,001 |
| Operating profit growth: | As reported | (0.7)% | (0.6)% | 2.5% |
| | Internal (a) | (2.9)% | (0.1)% | 10.3% |
| Diluted net earnings per share (EPS) | | \$ 3.38 | \$ 3.30 | \$ 3.16 |
| EPS growth (b) | | 2% | 4% | 6% |
| Currency neutral diluted EPS growth (b) | | % | 6% | 13% |

- (a) Internal net sales and operating profit growth for 2011 and 2010 exclude the impact of currency. Internal net sales and operating profit growth for 2009 exclude the impact of currency and acquisitions. Internal net sales and operating profit growth are non-GAAP financial measures which are further discussed and reconciled to the directly comparable measures in accordance with U.S. GAAP in the Net sales and operating profit section.

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(b) See the section entitled Foreign currency translation for discussion and reconciliation of this non-GAAP financial measure.

Net sales and operating profit

2011 compared to 2010

The following table provides an analysis of net sales and operating profit performance for 2011 versus 2010:

| (dollars in millions) | U.S. | | North | | | | Asia | | Corp- orate | Consoli- dated |
|------------------------------|-----------------------------|----------------|-------------------|------------------|-----------------|------------------|--------------|-----------|-----------------|-------------------|
| | Morning Foods & Kashi | U.S. Snacks | U.S. Specialty | America Other | Europe | Latin America | Pacific | | | |
| 2011 net sales | \$3,635 | \$2,908 | \$ 955 | \$1,375 | \$ 2,334 | \$1,049 | \$942 | \$ | \$13,198 | |
| 2010 net sales | \$3,480 | \$2,745 | \$ 916 | \$1,261 | \$ 2,230 | \$ 923 | \$842 | \$ | \$12,397 | |
| % change 2011 vs. 2010: | | | | | | | | | | |
| Internal business (a) | 4.4% | 6.0% | 4.2% | 6.7% | (.7)% | 10.3% | 4.1% | | 4.5% | |
| Foreign currency impact | % | % | % | 2.4% | 5.3 % | 3.4% | 7.7% | | 2.0% | |
| Total change | 4.4% | 6.0% | 4.2% | 9.1% | 4.6 % | 13.7% | 11.8% | | 6.5% | |

| (dollars in millions) | U.S. | | North | | | Latin | Asia | Corp- | Consoli- |
|------------------------------|--------------------------|----------------|-------------------|------------------|----------------|--------------|--------------|----------------|----------------|
| | Morning Foods & Kashi | U.S. Snacks | U.S. Specialty | America Other | Europe | America | Pacific | orate (b) | dated |
| 2011 operating profit | \$648 | \$431 | \$216 | \$258 | \$338 | \$176 | \$106 | \$(197) | \$1,976 |
| 2010 operating profit | \$630 | \$475 | \$240 | \$220 | \$364 | \$153 | \$74 | \$(166) | \$1,990 |
| % change 2011 vs. 2010: | | | | | | | | | |
| Internal business | 3.0 % | (9.1)% | (10.4)% | 13.9% | (12.5)% | 8.7% | 32.9% | (18.4)% | (2.9)% |
| Foreign currency impact | (.2)% | % | % | 3.4% | 5.4 % | 6.1% | 10.3% | % | 2.2 % |
| Total change | 2.8 % | (9.1)% | (10.4)% | 17.3% | (7.1)% | 14.8% | 43.2% | (18.4)% | (.7)% |

(a) Growth rate includes volume and price/mix.

(b) Research and Development expense totaling \$11 million for 2010 was reallocated to Corporate from the North America businesses. Our consolidated net sales were up 6% on an as reported basis and up 4% on an internal basis behind favorable pricing/mix, approximately flat volume, and strong results from innovations across most markets. Innovations and solid execution contributed to share gains in our core cereal business as well as several other key categories. Additionally, the increased investment in our supply chain that began in 2010 and continued through 2011 is building a stronger foundation for future growth. Pricing was taken selectively throughout 2011 to offset the higher input costs we have experienced on many products across our categories around the world.

Internal net sales for U.S. Morning Foods & Kashi increased 4% as a result of favorable pricing/mix and approximately flat volume. This business has two product groups: cereal and snacks. Cereal's internal net sales increased by 5% resulting from strong innovation launches and reduced reliance on promotional spending. Dollar sales from our innovation in 2011 equaled the dollar sales from innovation introduced by all our competitors combined. Snacks (toaster pastries, Kashi-branded cereal bars, crackers, cookies, Stretch Island fruit snacks, and health and wellness) internal net sales increased by 3% as a result of double-digit growth in health and wellness and continued share gains in our *Pop-Tarts*[®] business.

Internal net sales in U.S. Snacks increased by 6% as a result of favorable pricing/mix and approximately flat volume. This business consists of cookies, crackers, cereal bars, and fruit-flavored snacks. The sales growth was the result of strong crackers consumption behind the launch of *Special K Cracker Chips*[®] and *Cheez-it*[®] innovation which contributed to a solid improvement in our cracker category share. Sales also improved in wholesome snacks as a result of innovations in our *Special K*[®] and *FiberPlus*[®] cereal bars business. Cookies low-single digit sales growth was favorably impacted by the launch of the *Keebler*[®] master brand initiative in the second quarter which aligned pricing, packaging and scale across the *Keebler*[®] brand.

Internal net sales in U.S. Specialty increased by 4% as a result of favorable pricing/mix and approximately flat volume. Sales growth was due to frozen food innovation launches and cereal bar distribution gains.

Internal net sales in North America Other (U.S. Frozen and Canada) increased by 7% due to mid-single-digit volume growth and favorable pricing/mix. Sales growth was the result of our U.S. Frozen business posting double-digit growth for the year while gaining share as a result of

increased brand-building support behind innovation activity.

Our International segments' internal net sales were up 3% compared to the prior year as a result of favorable pricing/mix, partially offset by a decline in volume. Europe's internal net sales declined 1% for the year.

driven by a 3% decline in volume, partially offset by favorable pricing/mix. The operating environment in Europe continued to be difficult as a result of economic conditions and competitive activity. Sales growth in Russia was solid, as we continue to transition from a non-branded to a branded product mix. Latin America's internal net sales growth was 10% due to a slight increase in volume and double-digit increase in pricing/mix. Latin America experienced growth in both cereal and snacks behind a mid-double-digit increase in brand building investment to support innovations. Internal net sales in Asia Pacific grew 4% as a result of favorable pricing/mix and approximately flat volume. Asia Pacific's growth was driven by strong performance across most of Asia, as well as South Africa.

Consolidated operating profit declined by 1% on an as reported basis and was down 3% on an internal basis, when excluding the impact of foreign currency translation. Operating profit for the year was negatively impacted by our supply chain investments, commodity inflation, and the reinstatement of our incentive compensation program as a result of our strong pay-for-performance orientation.

Internal operating profit in U.S. Morning Foods & Kashi increased by 3%, U.S. Snacks declined by 9%, U.S. Specialty declined by 10%, North America Other grew by 14%, Europe declined by 13%, Latin America increased by 9% and Asia Pacific increased by 33%. U.S. Morning Foods & Kashi's increase was attributable to strong sales in cereal and snacks, partially offset by increased incentive compensation expense, increased commodity costs and investments in supply chain. U.S. Snacks' decline was attributable to investments in supply chain and increased incentive compensation expense. U.S. Specialty's decline was attributable to increased commodity costs and incentive compensation expense. Europe's operating profit declined due to lower sales resulting from the continued difficult operating environment and increased commodity costs. The increase in Latin America's operating profit is primarily a result of higher sales partially offset by increased brand-building investment. Asia Pacific's operating profit growth was positively impacted by the prior year impairment charges related to our business in China. Refer to Note 2 within Notes to Consolidated Financial Statements for further information. Corporate was impacted by higher compensation-related expense.

2010 compared to 2009

The following table provides an analysis of net sales and operating profit performance for 2010 versus 2009:

| (dollars in millions) | North | | | | | | | | |
|------------------------------|----------------------------------|----------------|-------------------|------------------|----------------|------------------|-----------------|----------------|-------------------|
| | U.S. Morning Foods & Kashi | U.S. Snacks | U.S. Specialty | America Other | Europe | Latin America | Asia Pacific | Corp- orate | Consoli- dated |
| 2010 net sales | \$3,480 | \$2,745 | \$916 | \$1,261 | \$2,230 | \$923 | \$842 | \$ | \$12,397 |
| 2009 net sales | \$3,587 | \$2,758 | \$913 | \$1,252 | \$2,361 | \$963 | \$741 | \$ | \$12,575 |
| % change 2010 vs. 2009: | | | | | | | | | |
| Internal business (a) | (3.0)% | (.5)% | .3% | (3.4)% | (2.7)% | 4.8 % | 2.0% | | (1.3)% |
| Foreign currency impact | % | % | % | 4.1 % | (2.8)% | (8.9)% | 11.7% | | (.1)% |
| Total change | (3.0)% | (.5)% | .3% | .7 % | (5.5)% | (4.1)% | 13.7% | | (1.4)% |

| (dollars in millions) | U.S. | | | | | | | | |
|------------------------------|----------------------------------|----------------|-------------------|------------------|--------------|------------------|-----------------|--------------------|-------------------|
| | U.S. Morning Foods & Kashi | U.S. Snacks | U.S. Specialty | America Other | Europe | Latin America | Asia Pacific | Corp- orate (b) | Consoli- dated |
| 2010 operating profit | \$630 | \$475 | \$240 | \$220 | \$364 | \$153 | \$74 | \$(166) | \$1,990 |
| 2009 operating profit | \$728 | \$436 | \$190 | \$228 | \$348 | \$179 | \$86 | \$(194) | \$2,001 |
| % change 2010 vs. 2009: | | | | | | | | | |
| Internal business | (13.5)% | 8.8% | 26.3% | (8.5)% | 8.2 % | (2.4)% | (29.5)% | 14.5% | (.1)% |
| Foreign currency impact | .1 % | % | % | 5.0 % | (3.4)% | (12.3)% | 15.2 % | % | (.5)% |
| Total change | (13.4)% | 8.8% | 26.3% | (3.5)% | 4.8 % | (14.7)% | (14.3)% | 14.5% | (.6)% |

(a) Growth rate includes volume and price/mix.

(b) Research and Development expense totaling \$11 million for 2010 and \$13 million for 2009 was reallocated to Corporate from the North America businesses.

Our consolidated net sales were down 1% on both a reported and internal basis, behind a 2% reduction in volume that was partially offset by favorable pricing/mix. There were three major issues that affected our results. First, our categories respond to innovation and brand building. We did not have sufficient cereal innovations in 2010. Rather, we focused on renovating our existing cereal products. We invested in renovation to improve the nutritional profile of our products. Secondly, we experienced supply chain disruptions in our waffle business and had a second quarter recall of select packages of breakfast cereals in our U.S. business. As a result, we increased investment in our supply chain to mitigate potential risks. Next, we experienced weakness in our core cereal businesses due to the competitive environment which drove price deflation into the cereal category. In late 2010 we announced price increases driven by higher input costs on many products across our categories around the world.

Internal net sales for U.S. Morning Foods & Kashi declined 3% as a result of a 2% decline in volume and unfavorable pricing/mix. Cereal's internal net sales declined by 6%. Our consumption was negatively impacted by the cereal recall that occurred in the second quarter of 2010. The brands involved in the recall were the cornerstone of our back-to-school promotions in the third quarter. Promotional pricing drove deflation into the category, but did not drive higher category volumes as would be expected. The U.S. cereal category responds well to innovation. While there were lower levels of innovation across the category in 2010, our innovations performed well. We were also impacted by less support from non-measured channels. Trade inventory levels at the end of 2009 were higher than normal. As a result, our 2010 sales were negatively impacted as retailers sold through their inventory, reducing their purchases from us. Snacks internal net sales increased by 5% primarily driven by *Pop-Tarts*®.

U.S. Snacks' internal net sales declined slightly as a result of a 2% decline in volume, partially offset by favorable pricing/mix. The slight decline was driven by weak performance in cookies and, to a lesser extent, crackers. We were able to maintain our cracker category share in measured channels despite increased competitive promotional activity. Consumption in the cookie category was down for the year. Our cookie performance was also impacted by the loss of shelf space in non-measured channels, which we were able to regain during the fourth quarter of 2010. This decline was partially offset by strong wholesome snack sales including our bar innovations such as *FiberPlus*® and *Special K Fruit Crisps*®.

Internal net sales in North America Other decreased by 3% as a result of a 5% decline in volume, partially offset by favorable pricing/mix. Our sales were negatively impacted during the year due to the waffle supply disruption that began late in 2009. During 2010, we returned to full capacity and introduced new innovations. While the business rebounded slower than expected during 2010 as it took longer to re-supply and reset retailer shelves, we reinstated brand building and the business responded positively. Our veggie business performed well, particularly *Morningstar Farms*® burgers and entrees.

Our International segments' internal net sales were flat compared to the prior year as a result of a 1% improvement in pricing/mix which was offset by reduction in volume. Europe's internal net sales declined 3% for the year which was primarily the result of volume decline. The cereal category (as measured by consumption) declined in our core European countries such as the U.K. Additionally, we saw price deflation in many food categories across Europe, especially in the U.K. Weakness in the Russia snack business due to transition from a non-branded business to a branded business drove lower volumes and contributed to Europe's lower top line results. Latin America's internal net sales growth was 5% resulting from 8% favorable pricing/mix, partially offset by volume decline. The growth in cereal masked the decline in snacks. Our decline in snacks was largely driven by Venezuela where we import some products from Mexico. The imports were impacted by exchange rate controls and it was no longer cost efficient to import goods. Internal net sales in Asia Pacific grew 2% as a result of a 4% increase in volume, partially offset by unfavorable pricing/mix. Asia Pacific's growth was driven by strong performance across most of Asia, as well as South Africa. This was muted by a decline in Australia where the cereal category faced price deflation.

Consolidated operating profit declined by 1% on an as reported basis and was flat on an internal basis, when excluding the impact of foreign currency translation. Operating profit for the year was negatively impacted by the cereal recall, higher than expected commodity inflation and investments in our supply chain. Operating profit benefited from lower incentive compensation expense. Incentive compensation is based upon the Company's actual results compared to our target. Given results were lower than our targets, which were set at the beginning of 2010, incentive compensation decreased significantly compared to the prior year. Despite 2010's operating performance, we recognized the need to invest in advertising. Accordingly, we increased our spending in advertising by 4%, excluding the impact of foreign currency translation.

Internal operating profit in U.S. Morning Foods & Kashi decreased by 14%, U.S. Snacks grew by 9%, U.S. Specialty increased 26%, North America Other declined by 9%, Europe grew by 8%, Latin America declined by 2% and Asia Pacific declined by 30%. U.S. Morning Foods & Kashi's decline was attributable to lower sales in cereal. Competitive activity drove lower

cereal sales as did the second quarter cereal recall. These negative drivers were partially offset by higher sales in snacks primarily due to *Pop-Tarts*[®], lower incentive compensation expense and decreased spending on cost reduction initiatives. U.S. Snacks increase was attributable to lower incentive compensation expense. U.S. Specialty increased due to lower incentive compensation costs and the favorable impact of cost reduction initiatives. Europe's operating profit increased due to lower commodity costs and less spending on cost reduction initiatives. The decline in Latin America's operating profit is primarily a result of higher commodity costs. Asia Pacific's operating profit was negatively impacted by the impairment charges related to our business in China. Refer to Note 2 within Notes to Consolidated Financial Statements for further information. Corporate benefited from lower incentive compensation expense.

Margin performance

Margin performance was as follows:

| | 2011 | 2010 | 2009 | Change vs. prior year (pts.) | |
|------------------|---------|---------|---------|---------------------------------|------|
| | | | | 2011 | 2010 |
| Gross margin (a) | 41.3% | 42.7% | 42.9% | (1.4) | (.2) |
| SGA% (b) | (26.3)% | (26.6)% | (27.0)% | .3 | .4 |
| Operating margin | 15.0% | 16.1% | 15.9% | (1.1) | .2 |

(a) Gross profit as a percentage of net sales. Gross profit is equal to net sales less cost of goods sold.

(b) Selling, general, and administrative expense as a percentage of net sales.

As illustrated in the preceding table, our consolidated gross margin declined by 140 basis points in 2011 due to the expanded investments in our supply chain, and increased cost pressures for fuel, energy, and commodities, which were partially offset by savings from cost reduction initiatives. Our selling, general and administrative (SGA) expense as a percentage of net sales decreased by 30 basis points primarily due to a reduction in brand-building investment as a percent of net sales and decreased costs related to cost reduction initiatives, partially offset by increased incentive compensation expense.

Our consolidated gross margin declined by 20 basis points in 2010 due to the cereal recall, increased cost pressures for fuel, energy, commodities and employee benefits and supply chain investments, which were more than offset by savings from cost reduction initiatives and lower up-front costs recorded in cost of sales (COGS). Our SGA expense as a percentage of net sales decreased by 40 basis points primarily due to a reduction in incentive compensation expense and lower costs for cost reduction initiatives, which more than offset increased advertising investment and an impairment of goodwill.

Foreign currency translation

The reporting currency for our financial statements is the U.S. dollar. Certain of our assets, liabilities, expenses and revenues are denominated in currencies other than the U.S. dollar, primarily in the Euro, British pound, Mexican peso, Australian dollar and Canadian dollar. To prepare our consolidated financial statements, we must translate those assets, liabilities, expenses and revenues into U.S. dollars at the applicable exchange rates. As a result, increases and decreases in the value of the U.S. dollar against these other currencies will affect the amount of these items in our consolidated financial statements, even if their value has not changed in their original currency. This could have significant impact on our results if such increase or decrease in the value of the U.S. dollar is substantial.

Volatility in the foreign exchange markets has limited our ability to forecast future U.S. dollar reported earnings. As such, we are measuring diluted earnings per share growth and providing guidance on future earnings on a currency neutral basis, assuming earnings are translated at the prior year's exchange rates. This non-GAAP financial measure is being used to focus management and investors on local currency business results, thereby providing visibility to the underlying trends of the Company. Management believes that excluding the impact of foreign currency from EPS provides a useful measurement of comparability given the volatility in foreign exchange markets.

Below is a reconciliation of reported EPS to currency neutral EPS for the fiscal years 2011, 2010 and 2009:

| | | | |
|----------------------|------|------|------|
| Consolidated results | 2011 | 2010 | 2009 |
|----------------------|------|------|------|

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| | | | |
|--------------------------------------|---------|---------|---------|
| Diluted net earnings per share (EPS) | \$ 3.38 | \$ 3.30 | \$ 3.16 |
| Translational impact (a) | (0.08) | 0.04 | 0.22 |
| Currency neutral EPS | \$ 3.30 | \$ 3.34 | \$ 3.38 |
| Currency neutral EPS growth (b) | % | 6% | 13% |

(a) Translation impact is the difference between reported EPS and the translation of current year net profits at prior year exchange rates, adjusted for gains (losses) on translational hedges, if applicable.

(b) Calculated as a percentage of growth from the prior year's reported EPS.

Interest expense

Annual interest expense for the 2009 to 2011 periods has trended downward. The decline in 2010 was due primarily to charges of approximately \$35 million in 2009 for early redemption of long-term debt and lower interest rates on our long-term debt. Interest income (recorded in other income (expense), net) was (in millions), 2011-\$11; 2010-\$6; 2009-\$4.

Income taxes

Our reported effective tax rates for 2011, 2010 and 2009 were 29.0%, 28.8% and 28.2% respectively. The impact of discrete adjustments and the cost of remitted and unremitted foreign earnings reduced our effective income tax rate by 3 percentage points for 2011. For 2010 and 2009 the impact was a reduction of 3 and 2 percentage points, respectively. Refer to Note 11 within Notes to Consolidated Financial Statements for further information. Fluctuations in foreign currency exchange rates could impact the expected effective income tax rate as it is dependent upon U.S. dollar earnings of foreign subsidiaries doing business in various countries with differing statutory tax rates. Additionally, the rate could be impacted if pending uncertain tax matters, including tax positions that could be affected by planning initiatives, are resolved more or less favorably than we currently expect.

Product withdrawal

Refer to Note 13 within Notes to Consolidated Financial Statements.

LIQUIDITY AND CAPITAL RESOURCES

Our principal source of liquidity is operating cash flows supplemented by borrowings for major acquisitions and other significant transactions. Our cash-generating capability is one of our fundamental strengths and provides us with substantial financial flexibility in meeting operating and investing needs.

We believe that our operating cash flows, together with our credit facilities and other available debt financing, will be adequate to meet our operating, investing and financing needs in the foreseeable future. However, there can be no assurance that volatility and/or disruption in the global capital and credit markets will not impair our ability to access these markets on terms acceptable to us, or at all.

On February 15, 2012 we announced that we entered into an agreement to acquire Procter & Gamble's *Pringle*® business for \$2.695 billion which is expected to be funded by international cash and the issuance of approximately \$2 billion of short and long term debt. The transaction is expected to close in the Summer of 2012, as such, we expect to have the *Pringles*® business included in our results for approximately six months. We plan to decrease our share repurchase program while we pay down debt, but we are likely to repurchase shares to the extent of stock option exercise to offset the dilution effect. We also expect to maintain a strong investment-grade rating and are committed to reducing debt levels to rebuild our financial flexibility.

The following table sets forth a summary of our cash flows:

| (dollars in millions) | 2011 | 2010 | 2009 |
|---|--------------|---------------|--------------|
| Net cash provided by (used in): | | | |
| Operating activities | \$ 1,595 | \$ 1,008 | \$ 1,643 |
| Investing activities | (587) | (465) | (370) |
| Financing activities | (957) | (439) | (1,182) |
| Effect of exchange rates on cash and cash equivalents | (35) | 6 | (12) |
| Net increase in cash and cash equivalents | \$ 16 | \$ 110 | \$ 79 |
| Operating activities | | | |

The principal source of our operating cash flows is net earnings, meaning cash receipts from the sale of our products, net of costs to manufacture and market our products.

Our net cash provided by operating activities for 2011 amounted to \$1,595 million, an increase of \$587 million compared with 2010. The increase in net cash provided by operating activities was primarily attributable to lower pension and postretirement benefit plan contributions and lower payments for incentive compensation partially offset by a marginal increase in core working capital in 2011. Our net cash provided by operating activities for 2010 amounted to \$1,008 million, a decrease of \$635 million compared with 2009, reflecting higher pension and postretirement benefit plan contributions and increased payments for advertising and promotion in 2010.

Our cash conversion cycle (defined as days of inventory and trade receivables outstanding less days of trade payables outstanding, based on a trailing 12 month average) is relatively short, equating to approximately 24 days for 2011, and 23 days for each of 2010 and 2009. Core working capital in 2011 averaged 6.9% of net sales, compared to 6.6% in 2010 and 6.5% in 2009. During 2011, core working capital was negatively

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impacted by higher days of inventory and higher days of trade receivables. Higher days of inventory was necessary to support our new product introductions and to maintain appropriate levels of service while investing in our supply chain infrastructure. Higher days of trade receivables resulted from strong sales at year-end due to our innovation launches and *Special K*® New Year's resolution programs. During 2010, core working capital was negatively impacted by higher days of inventory needed to improve order fill levels, which was compounded by the impact of lower reported sales.

Our total pension and postretirement benefit plan funding amounted to \$192 million, \$643 million and \$100 million, in 2011, 2010 and 2009, respectively. During the fourth quarter of 2010, we made incremental contributions to our pension and

postretirement benefit plans amounting to \$563 million (\$467 million, net of tax).

The Pension Protection Act (PPA), and subsequent regulations, determines defined benefit plan minimum funding requirements in the United States. We believe that we will not be required to make any contributions under PPA requirements until 2014 or beyond. Our projections concerning timing of PPA funding requirements are subject to change primarily based on general market conditions affecting trust asset performance, future discount rates based on average yields of high quality corporate bonds and our decisions regarding certain elective provisions of the PPA.

We currently project that we will make total U.S. and foreign benefit plan contributions in 2012 of approximately \$50 million. Actual 2012 contributions could be different from our current projections, as influenced by our decision to undertake discretionary funding of our benefit trusts versus other competing investment priorities, future changes in government requirements, trust asset performance, renewals of union contracts, or higher-than-expected health care claims cost experience.

We measure cash flow as net cash provided by operating activities reduced by expenditures for property additions. We use this non-GAAP financial measure of cash flow to focus management and investors on the amount of cash available for debt repayment, dividend distributions, acquisition opportunities, and share repurchases. Our cash flow metric is reconciled to the most comparable GAAP measure, as follows:

| (dollars in millions) | 2011 | 2010 | 2009 |
|---|--------------|----------------|----------|
| Net cash provided by operating activities | \$ 1,595 | \$ 1,008 | \$ 1,643 |
| Additions to properties | (594) | (474) | (377) |
| Cash flow | \$ 1,001 | \$ 534 | \$ 1,266 |
| <i>year-over-year change</i> | <i>87.5%</i> | <i>(57.8)%</i> | |

Year-over-year changes in cash flow (as defined) were driven by variations in both the amount of contributions to our pension and postretirement benefit plans and core working capital as well as changes in the level of capital expenditures during the three-year period.

Investing activities

Our net cash used in investing activities for 2011 amounted to \$587 million, an increase of \$122 million compared with 2010 due to a higher level of capital expenditures in 2011.

Capital spending in 2011 included investments in our supply chain infrastructure and to support capacity requirements in certain markets. In addition, we continued the investment in our information technology infrastructure related to the reimplementation and upgrade of our SAP platform. In 2010, we spent capital on our SAP platform and invested in our supply chain. In 2009, we invested in a new facility to manufacture ready-to-eat cereal in Mexico and completed the expansion of our global research center, one of the key incubators of innovation for our business, located in Battle Creek, Michigan.

Net cash used in investing activities of \$465 million in 2010 increased by \$95 million compared with 2009, reflecting capital projects for our reimplementation and upgrade of our SAP platform and investments in our supply chain.

Cash paid for additions to properties as a percentage of net sales has grown to 4.5% in 2011, from 3.8% in 2010, and 3.0% in 2009.

Financing activities

Our net cash used in financing activities for 2011, 2010 and 2009 amounted to \$957 million, \$439 million, and \$1,182 million, respectively.

Total debt was \$6.0 billion at year-end 2011 and \$5.9 billion at year-end 2010.

In April 2011, we repaid \$945 million ten-year 6.60% U.S. Dollar Notes at maturity with commercial paper.

In May 2011, we issued \$400 million of seven-year 3.25% fixed rate U.S. Dollar Notes, using the proceeds of \$397 million for general corporate purposes and repayment of commercial paper. During 2011, the Company entered into interest rate swaps with notional amounts totaling \$400 million, which effectively converted these Notes from a fixed rate to a floating rate obligation through maturity. The effective interest rate on these Notes, reflecting issuance discount and interest rate swaps was 2.31% in December 2011.

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In November 2011, we issued \$500 million of five-year 1.875% fixed rate U. S. Dollar Notes, using the proceeds of \$498 million for general corporate purposes and repayment of commercial paper. The effective interest rate on these Notes, reflecting issuance discount and hedge settlement was 1.98% in December 2011.

In December 2010, we issued \$1.0 billion of ten-year 4.0% fixed rate U.S. Dollar Notes, using a portion of the \$987 million net proceeds to make incremental pension and postretirement benefit plan contributions. The proceeds were also used to retire commercial paper. The effective interest rate on these Notes, reflecting issuance discount and hedge settlement was 3.42% in December 2011.

In November 2009, we issued \$500 million of ten-year 4.15% fixed rate U.S. Dollar Notes, and used proceeds of \$496 million to retire a portion of our 6.6% U.S. Dollar Notes due 2011. We retired \$482 million of the 2011 debt, which had an effective interest rate of 7.08%, through a tender offer. In connection with the debt retirement, we recognized \$35 million of interest expense and an acceleration of \$3 million loss on an interest rate swap, which was previously recorded in accumulated other comprehensive income. These charges were included in 2009 cash flows from operating activities.

In May 2009, we issued \$750 million of seven-year 4.45% fixed rate U.S. Dollar Notes, and used proceeds of \$745 million to pay down commercial paper. In May 2009, we also entered into interest rate swaps on \$1,150 million of our debt. Interest rate swaps with notional amounts totaling \$750 million effectively converted our 5.125% U.S. Dollar Notes due 2012 from a fixed rate to a floating rate obligation for the remainder of the five-year term. In addition, interest rate swaps with notional amounts totaling \$400 million effectively converted a portion of our 6.6% U.S. Dollar Notes due 2011 from a fixed rate to a floating rate obligation for the remaining term.

In April 2010, our board of directors approved a share repurchase program authorizing us to repurchase shares of our common stock amounting to \$2.5 billion during 2010 through 2012. This three year authorization replaced previous share buyback programs which had authorized stock repurchases of up to \$1.1 billion for 2010 and \$650 million for 2009.

Under these programs, we repurchased approximately 15 million, 21 million and 4 million shares of common stock for \$793 million, \$1.1 billion and \$187 million during 2011, 2010 and 2009, respectively.

We paid quarterly dividends to shareholders totaling \$1.67 per share in 2011, \$1.56 per share in 2010 and \$1.43 per share in 2009. Total cash paid for dividends increased by 3.4% in 2011 and 7.0% in 2010.

In March 2011, we entered into an unsecured Four-Year Credit Agreement to replace our existing unsecured Five-Year Credit Agreement which would have expired in November 2011. The Four-Year Credit Agreement allows us to borrow, on a revolving credit basis, up to \$2.0 billion.

Our long-term debt agreements contain customary covenants that limit the Company and some of its subsidiaries from incurring certain liens or from entering into certain sale and lease-back transactions. Some agreements also contain change in control provisions. However, they do not contain acceleration of maturity clauses that are dependent on credit ratings. A change in the Company's credit ratings could limit our access to the U.S. short-term debt market and/or increase the cost of refinancing long-term debt in the future. However, even under these circumstances, we would continue to have access to our Four-Year Credit Agreement, which expires in March 2015. This source of liquidity is unused and available on an unsecured basis, although we do not currently plan to use it.

We plan to use a combination of commercial paper and future issuances of term debt to refinance our \$750 million of debt maturing in the fourth quarter of 2012.

Capital and credit markets, including commercial paper markets, continued to experience instability and disruption as the U.S. and global economies underwent a period of extreme uncertainty. Throughout this period of uncertainty, we continued to have access to the U.S. and Canadian commercial paper markets. Our commercial paper and term debt credit ratings were not affected by the changes in the credit environment.

We monitor the financial strength of our third-party financial institutions, including those that hold our cash and cash equivalents as well as those who serve as counterparties to our credit facilities, our derivative financial instruments, and other arrangements.

We continue to believe that we will be able to meet our interest and principal repayment obligations and maintain our debt covenants for the foreseeable future, while still meeting our operational needs, including the pursuit of selected bolt-on acquisitions. This will be accomplished through our strong cash flow, our short-term borrowings, and our maintenance of credit facilities on a global basis.

OFF-BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL OBLIGATIONS**Off-balance sheet arrangements**

As of December 31, 2011 and January 1, 2011 we did not have any material off-balance sheet arrangements.

Contractual obligations

The following table summarizes our contractual obligations at December 31, 2011:

| Contractual obligations (millions) | Payments due by period | | | | | | |
|---------------------------------------|------------------------|-----------------|-----------------|---------------|---------------|-----------------|-----------------|
| | Total | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 and beyond |
| Long-term debt: | | | | | | | |
| Principal | \$ 5,763 | \$ 750 | \$ 752 | \$ 8 | \$ 1 | \$ 1,251 | \$ 3,001 |
| Interest (a) | 2,802 | 297 | 243 | 229 | 230 | 217 | 1,586 |
| Capital leases (b) | 5 | 1 | 1 | 1 | 1 | | 1 |
| Operating leases (c) | 589 | 150 | 123 | 93 | 69 | 59 | 95 |
| Purchase obligations (d) | 999 | 832 | 73 | 44 | 35 | 15 | |
| Uncertain tax positions (e) | 15 | 15 | | | | | |
| Other long-term obligations (f) | 1,008 | 90 | 68 | 91 | 191 | 326 | 242 |
| Total | \$ 11,181 | \$ 2,135 | \$ 1,260 | \$ 466 | \$ 527 | \$ 1,868 | \$ 4,925 |

- (a) Includes interest payments on our long-term debt and payments on our interest rate swaps. Interest calculated on our variable rate debt was forecasted using the LIBOR forward rate curve as of December 31, 2011.
- (b) The total expected cash payments on our capital leases include interest expense totaling approximately \$1 million over the periods presented above.
- (c) Operating leases represent the minimum rental commitments under non-cancelable operating leases.
- (d) Purchase obligations consist primarily of fixed commitments for raw materials to be utilized in the normal course of business and for marketing, advertising and other services. The amounts presented in the table do not include items already recorded in accounts payable or other current liabilities at year-end 2011, nor does the table reflect cash flows we are likely to incur based on our plans, but are not obligated to incur. Therefore, it should be noted that the exclusion of these items from the table could be a limitation in assessing our total future cash flows under contracts.
- (e) As of December 31, 2011, our total liability for uncertain tax positions was \$66 million, of which \$15 million, is expected to be paid in the next twelve months. We are not able to reasonably estimate the timing of future cash flows related to the remaining \$51 million.
- (f) Other long-term obligations are those associated with noncurrent liabilities recorded within the Consolidated Balance Sheet at year-end 2011 and consist principally of projected commitments under deferred compensation arrangements, multiemployer plans, and supplemental employee retirement benefits. The table also includes our current estimate of minimum contributions to defined benefit pension and postretirement benefit plans through 2017 as follows: 2012-\$50; 2013-\$38; 2014-\$76; 2015-\$173; 2016-\$294; 2017-\$89.

CRITICAL ACCOUNTING ESTIMATES**Promotional expenditures**

Our promotional activities are conducted either through the retail trade or directly with consumers and include activities such as in-store displays and events, feature price discounts, consumer coupons, contests and loyalty programs. The costs of these activities are generally recognized at the time the related revenue is recorded, which normally precedes the actual cash expenditure. The recognition of these costs therefore requires management judgment regarding the volume of promotional offers that will be redeemed by either the retail trade or consumer. These estimates are made using various techniques including historical data on performance of similar promotional programs. Differences between estimated expense and actual redemptions are normally insignificant and recognized as a change in management estimate in a subsequent period. On a full-year basis, these subsequent period adjustments generally represent less than 0.5% of our Company's net sales. However, our Company's total promotional expenditures (including amounts classified as a revenue reduction) represented approximately 40% of 2011 net sales; therefore, it is likely that our results would be materially different if different assumptions or conditions were to prevail.

Property

Long-lived assets such as property, plant and equipment are tested for impairment when conditions indicate that the carrying value may not be recoverable. Management evaluates several conditions, including, but not limited to, the following: a significant decrease in the market price of an asset or an asset group; a significant adverse change in the extent or manner in which a long-lived asset is being used, including an extended period of idleness; and a current expectation

that, more likely than not, a long-lived asset or asset group will be sold or otherwise disposed of significantly before the end of its previously estimated useful life. For assets to be held and used, we project the expected future undiscounted cash flows generated by the long-lived asset or asset group over the remaining useful life of the primary asset. If the cash flow analysis yields an amount less than the carrying amount we determine the fair value of the asset or asset group by using comparable market data. There are inherent uncertainties associated with the judgments and estimates we use in these analyses.

At December 31, 2011, we have property, plant and equipment of \$3.3 billion, net of accumulated depreciation, on our balance sheet. Included in this amount are approximately \$68 million of idle assets. The largest individual idle asset is a facility outside the United States which we tested for impairment on a held and used basis. The estimated future undiscounted cash flows exceeded the net book value of the facility as of December 31, 2011. Management estimates the plant will be deployed within the next several years. Should management's plan for deployment change, this could result in an impairment charge of up to \$46 million based on the carrying value as of December 31, 2011.

Goodwill and other intangible assets

We perform an impairment evaluation of goodwill and intangible assets with indefinite useful lives at least annually during the fourth quarter of each year in conjunction with our annual budgeting process. During the fourth quarter of 2011 we changed our reporting structure which altered the composition of the reporting units within the U.S. Morning Foods and Kashi operating segment. The changes resulted in the reassignment of the assets and liabilities to the reporting units impacted. The goodwill was allocated to the reporting units impacted using the relative fair value approach.

Goodwill impairment testing first requires a comparison between the carrying value and fair value of a reporting unit with associated goodwill. Carrying value is based on the assets and liabilities associated with the operations of that reporting unit, which often requires allocation of shared or corporate items among reporting units. For the 2011 goodwill impairment test, the fair value of the reporting units was estimated based on market multiples. Our approach employs market multiples based on earnings before interest, taxes, depreciation and amortization (EBITDA), earnings for companies comparable to our reporting units and discounted cash flows. Management believes the assumptions used for the impairment test are consistent with those utilized by a market participant performing similar valuations for our reporting units.

Similarly, impairment testing of indefinite-lived intangible assets requires a comparison of carrying value to fair value of that particular asset. Fair values of non-goodwill intangible assets are based primarily on projections of future cash flows to be generated from that asset. For instance, cash flows related to a particular trademark would be based on a projected royalty stream attributable to branded product sales discounted at rates consistent with rates used by market participants.

These estimates are made using various inputs including historical data, current and anticipated market conditions, management plans, and market comparables.

We also evaluate the useful life over which a non-goodwill intangible asset with a finite life is expected to contribute directly or indirectly to the cash flows of the Company. Reaching a determination on useful life requires significant judgments and assumptions regarding the future effects of obsolescence, demand, competition, other economic factors (such as the stability of the industry, known technological advances, legislative action that results in an uncertain or changing regulatory environment, and expected changes in distribution channels), the level of required maintenance expenditures, and the expected lives of other related groups of assets.

At December 31, 2011, goodwill and other intangible assets amounted to \$5.1 billion, consisting primarily of goodwill and trademarks associated with the 2001 acquisition of Keebler Foods Company. Within this total, approximately \$1.4 billion of non-goodwill intangible assets were classified as indefinite-lived, comprised principally of Keebler trademarks. We currently believe that the fair value of our goodwill and other intangible assets exceeds their carrying value and that those intangibles so classified will contribute indefinitely to the cash flows of the Company. At December 31, 2011, the fair value of our U.S. Snacks reporting unit exceeded its book value by \$2.1 billion. However, if we had used materially different assumptions, which we do not believe are reasonably possible, regarding the future performance of our business or a different weighted-average cost of capital in the valuation, this could have resulted in significant impairment losses. Additionally, we have \$57 million of goodwill related to our 2008 acquisition of United Bakers in Russia. The percentage of excess fair value over carrying value of the Russian reporting unit was approximately 30% in both 2011 and 2010. If we used modestly different assumptions regarding sales multiples and EBITDA in the valuation, this could have resulted in an impairment loss. For example, if our projection of EBITDA margins had been lower by 200 basis points, this change in assumption may have resulted in impairment of some or all of the goodwill in the Russian reporting unit. Management will continue to monitor the situation closely.

Retirement benefits

Our Company sponsors a number of U.S. and foreign defined benefit employee pension plans and also provides retiree health care and other welfare benefits in the United States and Canada. Plan funding strategies are influenced by tax regulations and asset return performance. A substantial majority of plan assets are invested in a globally diversified portfolio of equity securities with smaller holdings of debt securities and other investments. We recognize the cost of benefits provided during retirement over the employees' active working life to determine the obligations and expense related to our retiree benefit plans. Inherent in this concept is the requirement to use various actuarial assumptions to predict and measure costs and obligations many years prior to the settlement date. Major actuarial assumptions that require significant management judgment and have a material impact on the measurement of our consolidated benefits expense and accumulated obligation include the long-term rates of return on plan assets, the health care cost trend rates, and the interest rates used to discount the obligations for our major plans, which cover employees in the United States, United Kingdom and Canada.

To conduct our annual review of the long-term rate of return on plan assets, we model expected returns over a 20-year investment horizon with respect to the specific investment mix of each of our major plans. The return assumptions used reflect a combination of rigorous historical performance analysis and forward-looking views of the financial markets including consideration of current yields on long-term bonds, price-earnings ratios of the major stock market indices, and long-term inflation. Our U.S. plan model, corresponding to approximately 71% of our trust assets globally, currently incorporates a long-term inflation assumption of 2.5% and an active management premium of 1% (net of fees) validated by historical analysis. Although we review our expected long-term rates of return annually, our benefit trust investment performance for one particular year does not, by itself, significantly influence our evaluation. Our expected rates of return are generally not revised, provided these rates continue to fall within a more likely than not corridor of between the 25th and 75th percentile of expected long-term returns, as determined by our modeling process. Our assumed rate of return for U.S. plans in 2011 of 8.9% equated to approximately the 62nd percentile expectation of our 2011 model. Similar methods are used for various foreign plans with invested assets, reflecting local economic conditions. Foreign trust investments represent approximately 29% of our global benefit plan assets.

Based on consolidated benefit plan assets at December 31, 2011, a 100 basis point reduction in the assumed rate of return would increase 2012 benefits expense by approximately \$49 million. Correspondingly, a 100 basis point shortfall between the assumed and actual rate of return on plan assets for 2012 would result in a similar amount of arising experience loss. Any arising asset-related experience gain or loss is recognized in the calculated value of plan assets over a five-year period. Once recognized, experience gains and losses are amortized using a declining-balance method over the average remaining service period of active plan participants, which for U.S. plans is presently about 12 years. Under this recognition method, a 100 basis point shortfall in actual versus assumed performance of all of our plan assets in 2012 would reduce pre-tax earnings by approximately \$1.8 million in 2013, increasing to approximately \$9.0 million in 2017. For each of the three fiscal years, our actual return on plan assets exceeded (was less than) the recognized assumed return by the following amounts (in millions): 2011-\$ (478); 2010 \$208; 2009 \$507.

To conduct our annual review of health care cost trend rates, we model our actual claims cost data over a five-year historical period, including an analysis of pre-65 versus post-65 age groups and other important demographic components in our covered retiree population. This data is adjusted to eliminate the impact of plan changes and other factors that would tend to distort the underlying cost inflation trends. Our initial health care cost trend rate is reviewed annually and adjusted as necessary to remain consistent with recent historical experience and our expectations regarding short-term future trends. In comparison to our actual five-year compound annual claims cost growth rate of approximately 5.0%, our initial trend rate for 2012 of 6.1% reflects the expected future impact of faster-growing claims experience for certain demographic groups within our total employee population. Our initial rate is trended downward by 0.5% per year, until the ultimate trend rate of 4.5% is reached. The ultimate trend rate is adjusted annually, as necessary, to approximate the current economic view on the rate of long-term inflation plus an appropriate health care cost premium. Based on consolidated obligations at December 31, 2011, a 100 basis point increase in the assumed health care cost trend rates would increase 2012 benefits expense by approximately \$17 million. A 100 basis point excess of 2012 actual health care claims cost over that calculated from the assumed trend rate would result in an arising experience loss of approximately \$8 million. Any arising health care claims cost-related experience gain or loss is recognized in the calculated amount of claims experience over a four-year period. Once recognized, experience gains and losses are amortized using a straight-line method over 15 years. The net experience gain arising from recognition of 2011 claims experience and adoption of an Employer Group Waiver Plan (EGWP) design for prescription drug costs was approximately \$161 million.

To conduct our annual review of discount rates, we selected the discount rate based on a cash-flow matching analysis using Towers Watson's proprietary RATE:Link tool and projections of the future benefit payments constituting the projected benefit obligation for the plans. RATE:Link establishes the uniform discount rate that produces the same present value of the estimated future benefit payments, as is generated by discounting each year's benefit payments by a spot rate applicable to that year. The spot rates used in this process are derived from a yield curve created from yields on the 40th to 90th percentile of U.S. high quality bonds. A similar methodology is applied in Canada and Europe, except the smaller bond markets imply that yields between the 10th and 90th percentiles are preferable. The measurement dates for our defined benefit plans are consistent with our fiscal year end. Accordingly, we select discount rates to measure our benefit obligations that are consistent with market indices during December of each year.

Based on consolidated obligations at December 31, 2011, a 25 basis point decline in the weighted-average discount rate used for benefit plan measurement purposes would increase 2012 benefits expense by approximately \$16 million. All obligation-related experience gains and losses are amortized using a straight-line method over the average remaining service period of active plan participants.

Despite the previously-described rigorous policies for selecting major actuarial assumptions, we periodically experience material differences between assumed and actual experience. As of December 31, 2011, we had consolidated unamortized prior service cost and net experience losses of approximately \$2.3 billion, compared to approximately \$1.7 billion at January 1, 2011. Of the total unamortized amounts at December 31, 2011, approximately \$1.9 billion was related to asset losses that occurred during 2008 and 2011, offset by \$0.7 billion in asset gains during 2009 and 2010, with the remainder largely related to discount rate reductions and health care claims experience. For 2012, we currently expect total amortization of prior service cost and net experience losses to be approximately \$34 million higher than the actual 2011 amount of approximately \$142 million. Total employee benefit expense for 2012 is expected to be higher than 2011 due to lower discount rates, phase in of the 2008 and 2011 investment losses, offset by better than expected 2009 and 2010 investment performance.

During 2011 we made contributions in the amount of \$180 million to Kellogg's global tax-qualified pension programs. This amount was mostly discretionary. Additionally we contributed \$12 million to our retiree medical programs.

Assuming actual future experience is consistent with our current assumptions, annual amortization of accumulated prior service cost and net experience losses during each of the next several years would increase versus the 2011 amount.

Income taxes

Our consolidated effective income tax rate is influenced by tax planning opportunities available to us in the various jurisdictions in which we operate. The calculation of our income tax provision and deferred income tax assets and liabilities is complex and requires the use of estimates and judgment. Income taxes are provided on the portion of foreign earnings that is expected to be remitted to and taxable in the United States.

We recognize tax benefits associated with uncertain tax positions when, in our judgment, it is more likely than not that the positions will be sustained upon examination by a taxing authority. For tax positions that meet the more likely than not recognition threshold, we initially and subsequently measure the tax benefits as the largest amount that we judge to have a greater than 50% likelihood of being realized upon ultimate settlement. Our liability associated with unrecognized tax benefits is adjusted periodically due to changing circumstances, such as the progress of tax audits, new or emerging legislation and tax planning. The tax position will be derecognized when it is no longer more likely than not of being sustained. Significant adjustments to our liability for unrecognized tax benefits impacting our effective tax rate are separately presented in the rate reconciliation table of Note 11 within Notes to Consolidated Financial Statements.

ACCOUNTING STANDARDS TO BE ADOPTED IN FUTURE PERIODS

Presentation of Comprehensive Income

In June 2011, the Financial Accounting Standards Board (FASB) issued a new accounting standard requiring most entities to present items of net income and other comprehensive income either in one continuous statement referred to as the statement of comprehensive income or in two separate, but consecutive, statements of net income and other comprehensive income. The update does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The new standard included a requirement to present reclassification adjustments out of accumulated other comprehensive income by component on the face of the financial statements. In December, 2011, the reclassification requirement within the new standard was indefinitely deferred. The new standard is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011 and should be applied

retrospectively. Early adoption is permitted. We will adopt the new standard at the beginning of our 2012 fiscal year.

Goodwill impairment testing

In September 2011, the FASB issued an updated accounting standard allowing entities the option to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. Under the updated standard an entity would not be required to calculate the fair value of a reporting unit unless the entity determines, based on a qualitative assessment, that it is more likely than not that its fair value is less than its carrying amount. The updated standard is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. We will adopt the updated standard in connection with our annual goodwill impairment evaluation in the fourth quarter of 2012.

FUTURE OUTLOOK

On February 15, 2012 we announced that we entered into an agreement to acquire Procter & Gamble's *Pringle*® business for \$2.695 billion which is expected to be funded by international cash and the issuance of approximately \$2 billion of short and long term debt. The transaction is expected to close in the Summer of 2012, as such we expect having Pringle's included in our results for approximately six months.

We anticipate in 2012 we will continue to set the foundation for future growth as a result of price realization and mix improvement driven by innovation and supported by increased investment in brand building. Earnings per share on a currency-neutral basis is expected to grow by 2 to 4 percent, prior to the impact of the *Pringles*® acquisition which is expected to be dilutive to 2012 earnings per share by \$0.11 to 0.16 including one-time costs and changes to the share repurchase program.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our Company is exposed to certain market risks, which exist as a part of our ongoing business operations. We use derivative financial and commodity instruments, where appropriate, to manage these risks. As a matter of policy, we do not engage in trading or speculative transactions. Refer to Note 12 within Notes to Consolidated Financial Statements for further information on our derivative financial and commodity instruments.

Foreign exchange risk

Our Company is exposed to fluctuations in foreign currency cash flows related primarily to third-party purchases, intercompany transactions, and when applicable, nonfunctional currency denominated third-party debt. Our Company is also exposed to fluctuations in the value of foreign currency investments in subsidiaries and cash flows related to repatriation of these investments. Additionally, our Company is exposed to volatility in the translation of foreign currency denominated earnings to U.S. dollars. Primary exposures include the U.S. dollar versus the euro, British pound, Australian dollar, Canadian dollar, and Mexican peso, and in the case of inter-subsidary transactions, the British pound versus the euro. We assess foreign currency risk based on transactional cash flows and translational volatility and may enter into forward contracts, options, and currency swaps to reduce fluctuations in long or short currency positions. Forward contracts and options are generally less than 18 months duration. Currency swap agreements may be established in conjunction with the term of underlying debt issuances.

The total notional amount of foreign currency derivative instruments at year-end 2011 was \$1,265 million, representing a settlement obligation of \$7 million. The total notional amount of foreign currency derivative instruments at year-end 2010 was \$1,075 million, representing a settlement obligation of \$20 million. All of these derivatives were hedges of anticipated transactions, translational exposure, or existing assets or liabilities, and mature within 18 months. Assuming an unfavorable 10% change in year-end exchange rates, the settlement obligation would have increased by approximately \$127 million at year-end 2011 and \$108 million at year-end 2010. These unfavorable changes would generally have been offset by favorable changes in the values of the underlying exposures.

Venezuela was designated as a highly inflationary economy as of the beginning of our 2010 fiscal year. Gains and losses resulting from the translation of the financial statements of subsidiaries operating in highly inflationary economies are recorded in earnings. As of the end of our 2009 fiscal year, we used the parallel rate to translate our Venezuelan subsidiary's financial statements to U.S. dollars. In May 2010, the Venezuelan government effectively eliminated the parallel market. In June 2010, several large Venezuelan commercial banks began operating the Transaction System for Foreign Currency Denominated Securities (SITME). Accordingly, we began using the SITME rate as of January 1, 2011 to translate our Venezuelan subsidiary's financial statements to U.S. dollars. During 2010, we recorded a \$3 million foreign exchange gain in other income (expense), net, associated with the translation of our subsidiary's financials into U.S. dollars, with no impact during 2011. On a consolidated basis, Venezuela represents less than 2% of our business; therefore, any ongoing impact is expected to be immaterial.

Interest rate risk

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Our Company is exposed to interest rate volatility with regard to future issuances of fixed rate debt and existing and future issuances of variable rate debt.

Primary exposures include movements in U.S. Treasury rates, London Interbank Offered Rates (LIBOR), and commercial paper rates. We periodically use interest rate swaps and forward interest rate contracts to reduce interest rate volatility and funding costs associated with certain debt issues, and to achieve a desired proportion of variable versus fixed rate debt, based on current and projected market conditions.

During 2011 and 2009, we entered into interest rate swaps in connection with certain U.S. Dollar Notes. Refer to disclosures contained in Note 6 within Notes to Consolidated Financial Statements. The total notional amount of interest rate swaps at year-end 2011 was \$600 million, representing a settlement receivable of \$23 million. The total notional amount of interest rate swaps at year-end 2010 was \$1.9 billion, representing a settlement receivable of \$74 million. Assuming average variable rate debt levels during the year, a one percentage point increase in interest rates would have increased interest expense by approximately \$18 million at year-end 2011 and \$21 million at year-end 2010.

Price risk

Our Company is exposed to price fluctuations primarily as a result of anticipated purchases of raw and packaging materials, fuel, and energy. Primary exposures include corn, wheat, soybean oil, sugar, cocoa, cartonboard, natural gas, and diesel fuel. We have historically used the combination of long-term contracts with suppliers, and exchange-traded futures and option contracts to reduce price fluctuations in a desired percentage of forecasted raw material purchases over a duration of generally less than 18 months. During 2006, we entered into two separate 10-year over-the-counter commodity swap transactions to reduce fluctuations in the price of natural gas used principally in our manufacturing processes. The notional amount of the swaps totaled \$104 million as of December 31, 2011 and equates to approximately 50% of our North America manufacturing needs over the remaining hedge period. At year-end January 1, 2011 the notional amount was \$125 million.

The total notional amount of commodity derivative instruments at year-end 2011, including the North America natural gas swaps, was \$175 million, representing a settlement obligation of approximately \$48 million. The total notional amount of commodity derivative instruments at year-end 2010, including the natural gas swaps, was \$379 million, representing a settlement obligation of approximately \$16 million. Assuming a 10% decrease in year-end commodity prices, the settlement obligation would have increased by approximately \$12 million at year-end 2011, and \$36 million at year-end 2010, generally offset by a reduction in the cost of the underlying commodity purchases.

In some instances the Company has reciprocal collateralization agreements with counterparties regarding fair value positions in excess of certain thresholds. These agreements call for the posting of collateral in the form of cash, treasury securities or letters of credit if a net liability position to the Company or our counterparties exceeds a certain amount. As of December 31, 2011, we had posted collateral of \$2 million in the form of cash, which was reflected as an increase in accounts receivable, net on the Consolidated Balance Sheet. There was no collateral balance requirement at January 1, 2011.

In addition to the commodity derivative instruments discussed above, we use long-term contracts with suppliers to manage a portion of the price exposure associated with future purchases of certain raw materials, including rice, sugar, cartonboard, and corrugated boxes. It should be noted the exclusion of these contracts from the analysis above could be a limitation in assessing the net market risk of our Company.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF INCOME

| (millions, except per share data) | 2011 | 2010 | 2009 |
|---|------------------|-----------|-----------|
| Net sales | \$ 13,198 | \$ 12,397 | \$ 12,575 |
| Cost of goods sold | 7,750 | 7,108 | 7,184 |
| Selling, general and administrative expense | 3,472 | 3,299 | 3,390 |
| Operating profit | \$ 1,976 | \$ 1,990 | \$ 2,001 |
| Interest expense | 233 | 248 | 295 |
| Other income (expense), net | (11) | | (22) |
| Income before income taxes | 1,732 | 1,742 | 1,684 |
| Income taxes | 503 | 502 | 476 |
| Net income | \$ 1,229 | \$ 1,240 | \$ 1,208 |
| Net loss attributable to noncontrolling interests | (2) | (7) | (4) |
| Net income attributable to Kellogg Company | \$ 1,231 | \$ 1,247 | \$ 1,212 |
| Per share amounts: | | | |
| Basic | \$ 3.40 | \$ 3.32 | \$ 3.17 |
| Diluted | \$ 3.38 | \$ 3.30 | \$ 3.16 |
| Dividends per share | \$ 1.670 | \$ 1.560 | \$ 1.430 |

Refer to Notes to Consolidated Financial Statements.

Kellogg Company and Subsidiaries

CONSOLIDATED BALANCE SHEET

| (millions, except share data) | 2011 | 2010 |
|---|------------------|------------------|
| Current assets | | |
| Cash and cash equivalents | \$ 460 | \$ 444 |
| Accounts receivable, net | 1,188 | 1,190 |
| Inventories | 1,132 | 1,056 |
| Other current assets | 247 | 225 |
| Total current assets | 3,027 | 2,915 |
| Property, net | 3,281 | 3,128 |
| Goodwill | 3,623 | 3,628 |
| Other intangibles, net | 1,454 | 1,456 |
| Other assets | 516 | 720 |
| Total assets | \$ 11,901 | \$ 11,847 |
| Current liabilities | | |
| Current maturities of long-term debt | \$ 761 | \$ 952 |
| Notes payable | 234 | 44 |
| Accounts payable | 1,189 | 1,149 |
| Other current liabilities | 1,129 | 1,039 |
| Total current liabilities | 3,313 | 3,184 |
| Long-term debt | 5,037 | 4,908 |
| Deferred income taxes | 637 | 697 |
| Pension liability | 560 | 265 |
| Other liabilities | 592 | 639 |
| Commitments and contingencies | | |
| Equity | | |
| Common stock, \$.25 par value, 1,000,000,000 shares authorized | | |
| Issued: 419,484,087 shares in 2011 and 419,272,027 shares in 2010 | 105 | 105 |
| Capital in excess of par value | 522 | 495 |
| Retained earnings | 6,721 | 6,122 |
| Treasury stock, at cost | | |
| 62,182,500 shares in 2011 and 53,667,635 shares in 2010 | (3,130) | (2,650) |
| Accumulated other comprehensive income (loss) | (2,458) | (1,914) |
| Total Kellogg Company equity | 1,760 | 2,158 |
| Noncontrolling interests | 2 | (4) |
| Total equity | 1,762 | 2,154 |
| Total liabilities and equity | \$ 11,901 | \$ 11,847 |

Refer to Notes to Consolidated Financial Statements.

Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF EQUITY

| (millions) | Common stock | | Capital in excess of par value | Retained earnings | Treasury stock | | Accumulated other comprehensive income (loss) | Total Kellogg Company equity | Non-controlling interests | Total equity | Total comprehensive income (loss) |
|--|--------------|---------------|--------------------------------|-------------------|----------------|-------------------|---|------------------------------|---------------------------|-----------------|-----------------------------------|
| | shares | amount | | | shares | amount | | | | | |
| Balance, January 3, 2009 | 419 | \$ 105 | \$ 438 | \$ 4,836 | 37 | \$ (1,790) | \$ (2,141) | \$ 1,448 | \$ 7 | \$ 1,455 | \$ (168) |
| Common stock repurchases | | | | | 4 | (187) | | (187) | | (187) | |
| Net income (loss) | | | | 1,212 | | | | 1,212 | (4) | 1,208 | 1,208 |
| Dividends | | | | (546) | | | | (546) | | (546) | |
| Other comprehensive income | | | | | | | 175 | 175 | | 175 | 175 |
| Stock compensation | | | 37 | | | | | 37 | | 37 | |
| Stock options exercised and other | | | (3) | (21) | (3) | 157 | | 133 | | 133 | |
| Balance, January 2, 2010 | 419 | \$ 105 | \$ 472 | \$ 5,481 | 38 | \$ (1,820) | \$ (1,966) | \$ 2,272 | \$ 3 | \$ 2,275 | \$ 1,383 |
| Common stock repurchases | | | | | 21 | (1,057) | | (1,057) | | (1,057) | |
| Net income (loss) | | | | 1,247 | | | | 1,247 | (7) | 1,240 | 1,240 |
| Dividends | | | | (584) | | | | (584) | | (584) | |
| Other comprehensive income | | | | | | | 52 | 52 | | 52 | 52 |
| Stock compensation | | | 19 | | | | | 19 | | 19 | |
| Stock options exercised and other | | | 4 | (22) | (5) | 227 | | 209 | | 209 | |
| Balance, January 1, 2011 | 419 | \$ 105 | \$ 495 | \$ 6,122 | 54 | \$ (2,650) | \$ (1,914) | \$ 2,158 | \$ (4) | \$ 2,154 | \$ 1,292 |
| Common stock repurchases | | | | | 15 | (793) | | (793) | | (793) | |
| Acquisition of noncontrolling interest | | | (8) | | | | | (8) | 8 | | |
| Net income (loss) | | | | 1,231 | | | | 1,231 | (2) | 1,229 | 1,229 |
| Dividends | | | | (604) | | | | (604) | | (604) | |
| Other comprehensive loss | | | | | | | (544) | (544) | | (544) | (544) |
| Stock compensation | | | 26 | | | | | 26 | | 26 | |
| Stock options exercised and other | | | 9 | (28) | (7) | 313 | | 294 | | 294 | |
| Balance, December 31, 2011 | 419 | \$ 105 | \$ 522 | \$ 6,721 | 62 | \$ (3,130) | \$ (2,458) | \$ 1,760 | \$ 2 | \$ 1,762 | \$ 685 |

Refer to Notes to Consolidated Financial Statements.

Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF CASH FLOWS

| (millions) | 2011 | 2010 | 2009 |
|--|-----------------|-----------------|-------------------|
| Operating activities | | | |
| Net income | \$ 1,229 | \$ 1,240 | \$ 1,208 |
| Adjustments to reconcile net income to operating cash flows: | | | |
| Depreciation and amortization | 369 | 392 | 384 |
| Deferred income taxes | 84 | 266 | (40) |
| Other | (22) | 97 | 13 |
| Postretirement benefit plan contributions | (192) | (643) | (100) |
| Changes in operating assets and liabilities: | | | |
| Trade receivables | (100) | 59 | (75) |
| Inventories | (76) | (146) | (13) |
| Accounts payable | 40 | 72 | (59) |
| Accrued income taxes | 132 | (192) | 112 |
| Accrued interest expense | (7) | 9 | (5) |
| Accrued and prepaid advertising, promotion and trade allowances | 4 | (12) | 91 |
| Accrued salaries and wages | 89 | (169) | 42 |
| All other current assets and liabilities | 45 | 35 | 85 |
| Net cash provided by operating activities | \$ 1,595 | \$ 1,008 | \$ 1,643 |
| Investing activities | | | |
| Additions to properties | \$ (594) | \$ (474) | \$ (377) |
| Other | 7 | 9 | 7 |
| Net cash used in investing activities | \$ (587) | \$ (465) | \$ (370) |
| Financing activities | | | |
| Net increase (reduction) of notes payable, with maturities less than or equal to 90 days | \$ 189 | \$ (1) | \$ (1,284) |
| Issuances of notes payable, with maturities greater than 90 days | | | 10 |
| Reductions of notes payable, with maturities greater than 90 days | | | (70) |
| Issuances of long-term debt | 895 | 987 | 1,241 |
| Reductions of long-term debt | (945) | (1) | (482) |
| Net issuances of common stock | 291 | 204 | 131 |
| Common stock repurchases | (798) | (1,052) | (187) |
| Cash dividends | (604) | (584) | (546) |
| Other | 15 | 8 | 5 |
| Net cash used in financing activities | \$ (957) | \$ (439) | \$ (1,182) |
| Effect of exchange rate changes on cash and cash equivalents | (35) | 6 | (12) |
| Increase in cash and cash equivalents | \$ 16 | \$ 110 | \$ 79 |
| Cash and cash equivalents at beginning of period | 444 | 334 | 255 |
| Cash and cash equivalents at end of period | \$ 460 | \$ 444 | \$ 334 |

Refer to Notes to Consolidated Financial Statements.

Kellogg Company and Subsidiaries

Notes to Consolidated Financial Statements

NOTE 1

ACCOUNTING POLICIES

Basis of presentation

The consolidated financial statements include the accounts of Kellogg Company and its majority-owned subsidiaries (Kellogg or the Company). Intercompany balances and transactions are eliminated.

The Company's fiscal year normally ends on the Saturday closest to December 31 and as a result, a 53rd week is added approximately every sixth year. The Company's 2011, 2010 and 2009 fiscal years each contained 52 weeks and ended on December 31, 2011, January 1, 2011 and January 2, 2010, respectively. The next fiscal year which will contain a 53rd week for the Company will be 2014, ending on January 3, 2015.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods reported. Actual results could differ from those estimates.

Cash and cash equivalents

Highly liquid investments with remaining stated maturities of three months or less when purchased are considered cash equivalents and recorded at cost.

Accounts receivable

Accounts receivable consists principally of trade receivables, which are recorded at the invoiced amount, net of allowances for doubtful accounts and prompt payment discounts. Trade receivables do not bear interest. The allowance for doubtful accounts represents management's estimate of the amount of probable credit losses in existing accounts receivable, as determined from a review of past due balances and other specific account data. Account balances are written off against the allowance when management determines the receivable is uncollectible. The Company does not have off-balance sheet credit exposure related to its customers.

Inventories

Inventories are valued at the lower of cost or market. Cost is determined on an average cost basis.

Property

The Company's property consists mainly of plants and equipment used for manufacturing activities. These assets are recorded at cost and depreciated over estimated useful lives using straight-line methods for financial reporting and accelerated methods, where permitted, for tax reporting. Major property categories are depreciated over various periods as follows (in years): manufacturing machinery and equipment 5-20; office equipment 4-5; computer equipment and capitalized software 3-7; building components 15-25; building structures 50. Cost includes interest associated with significant capital projects. Plant and equipment are reviewed for impairment when conditions indicate that the carrying value may not be recoverable. Such conditions include an extended period of idleness or a plan of disposal. Assets to be disposed of at a future date are depreciated over the remaining period of use. Assets to be sold are written down to realizable value at the time the assets are being actively marketed for sale and a sale is expected to occur within one year. As of year-end 2011 and 2010, the carrying value of assets held for sale was insignificant.

Goodwill and other intangible assets

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Goodwill and indefinite-lived intangibles are not amortized, but are tested at least annually for impairment. An intangible asset with a finite life is amortized on a straight-line basis over the estimated useful life.

For the goodwill impairment test, the fair value of the reporting units are estimated based on market multiples. This approach employs market multiples based on earnings before interest, taxes, depreciation and amortization, earnings for companies that are comparable to the Company's reporting units and discounted cash flow. The assumptions used for the impairment test are consistent with those utilized by a market participant performing similar valuations for the Company's reporting units.

Similarly, impairment testing of other intangible assets requires a comparison of carrying value to fair value of that particular asset. Fair values of non-goodwill intangible assets are based primarily on projections of future cash flows to be generated from that asset. For instance, cash flows related to a particular trademark would be based on a projected royalty stream attributable to branded product sales, discounted at rates consistent with rates used by market participants.

These estimates are made using various inputs including historical data, current and anticipated market conditions, management plans, and market comparables.

Revenue recognition

The Company recognizes sales upon delivery of its products to customers. Revenue, which includes shipping and handling charges billed to the customer, is reported net of applicable provisions for discounts, returns, allowances, and various government withholding taxes. Methodologies for determining these provisions are dependent on local customer pricing and promotional practices, which range from contractually fixed percentage price reductions to reimbursement based on actual occurrence or performance. Where applicable, future reimbursements are estimated based on a combination of historical patterns and future expectations regarding specific in-market product performance.

Advertising and promotion

The Company expenses production costs of advertising the first time the advertising takes place. Advertising expense is classified in selling, general and administrative (SGA) expense.

The Company classifies promotional payments to its customers, the cost of consumer coupons, and other cash redemption offers in net sales. The cost of promotional package inserts is recorded in cost of goods sold (COGS). Other types of consumer promotional expenditures are recorded in SGA expense.

Research and development

The costs of research and development (R&D) are expensed as incurred and are classified in SGA expense. R&D includes expenditures for new product and process innovation, as well as significant technological improvements to existing products and processes. The Company's R&D expenditures primarily consist of internal salaries, wages, consulting, and supplies attributable to time spent on R&D activities. Other costs include depreciation and maintenance of research facilities and equipment, including assets at manufacturing locations that are temporarily engaged in pilot plant activities.

Stock-based compensation

The Company uses stock-based compensation, including stock options, restricted stock and executive performance shares, to provide long-term performance incentives for its global workforce.

The Company classifies pre-tax stock compensation expense principally in SGA expense within its corporate operations. Expense attributable to awards of equity instruments is recorded in capital in excess of par value in the Consolidated Balance Sheet.

Certain of the Company's stock-based compensation plans contain provisions that accelerate vesting of awards upon retirement, disability, or death of eligible employees and directors. A stock-based award is considered vested for expense attribution purposes when the employee's retention of the award is no longer contingent on providing subsequent service. Accordingly, the Company recognizes compensation cost immediately for awards granted to retirement-eligible individuals or over the period from the grant date to the date retirement eligibility is achieved, if less than the stated vesting period.

The Company recognizes compensation cost for stock option awards that have a graded vesting schedule on a straight-line basis over the requisite service period for the entire award.

Corporate income tax benefits realized upon exercise or vesting of an award in excess of that previously recognized in earnings (windfall tax benefit) is recorded in other financing activities in the Consolidated Statement of Cash Flows. Realized windfall tax benefits are credited to capital in excess of par value in the Consolidated Balance Sheet. Realized shortfall tax benefits (amounts which are less than that previously recognized in earnings) are first offset against the cumulative balance of windfall tax benefits, if any, and then charged directly to income tax expense. The Company currently has sufficient cumulative windfall tax benefits to absorb arising shortfalls, such that earnings were not affected during the periods presented. Correspondingly, the Company includes the impact of pro forma deferred tax assets (i.e., the "as if" windfall or shortfall) for purposes of determining assumed proceeds in the treasury stock calculation of diluted earnings per share.

Pension benefits, nonpension postretirement and postemployment benefits

The Company sponsors a number of U.S. and foreign plans to provide pension, health care, and other welfare benefits to retired employees, as well as salary continuance, severance, and long-term disability to former or inactive employees.

The recognition of benefit expense is based on actuarial assumptions, such as discount rate, long-term rate of compensation increase, long-term rate of return on plan assets and health care cost trend rate, and is reported in COGS and SGA expense on the Consolidated Statement of

Income.

Pension and nonpension postretirement benefits. Variances between the expected and actual rates of return on plan assets are recognized in the calculated value of plan assets over a five-year period. Once recognized, experience gains and losses are amortized using a declining-balance method over the average remaining service period of active plan participants. Management reviews the Company's expected long-term rates of return annually; however, the benefit trust investment performance for one

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particular year does not, by itself, significantly influence this evaluation. The expected rates of return are not revised provided these rates fall between the 25th and 75th percentile of expected long-term returns, as determined by the Company's modeling process.

Pension obligation related experience gains or losses are amortized using a straight-line method over the average remaining service period of active plan participants. Health care claims cost related experience gains or losses are recognized in the calculated amount of claims experience over a four year period and once recognized, are amortized using a straight-line method over 15 years.

For defined benefit pension and postretirement plans, the Company records the net overfunded or underfunded position as a pension asset or pension liability on the Consolidated Balance Sheet. The change in funded status for the year is reported as a component of other comprehensive income (loss), net of tax, in equity.

Postemployment benefits. The Company recognizes an obligation for postemployment benefit plans that vest or accumulate with service. Obligations associated with the Company's postemployment benefit plans, which are unfunded, are included in other current liabilities and other liabilities on the Consolidated Balance Sheet. All gains and losses are recognized over the average remaining service period of active plan participants.

Postemployment benefits that do not vest or accumulate with service or benefits to employees in excess of those specified in the respective plans are expensed as incurred.

Income taxes

The Company recognizes uncertain tax positions based on a benefit recognition model. Provided that the tax position is deemed more likely than not of being sustained, the Company recognizes the largest amount of tax benefit that is greater than 50 percent likely of being ultimately realized upon settlement. The tax position is derecognized when it is no longer more likely than not of being sustained. The Company classifies income tax-related interest and penalties as interest expense and SGA expense, respectively, on the Consolidated Statement of Income. The current portion of the Company's unrecognized tax benefits is presented in the Consolidated Balance Sheet in other current assets and other current liabilities, and the amounts expected to be settled after one year are recorded in other assets and other liabilities.

Income taxes are provided on the portion of foreign earnings that is expected to be remitted to and taxable in the United States.

Derivative Instruments

The fair value of derivative instruments is recorded in other current assets, other assets, other current liabilities or other liabilities. Gains and losses representing either hedge ineffectiveness, hedge components excluded from the assessment of effectiveness, or hedges of translational exposure are recorded in the Consolidated Statement of Income in other income (expense), net. In the Consolidated Statement of Cash Flows, settlements of cash flow and fair value hedges are classified as an operating activity; settlements of all other derivative instruments, including instruments for which hedge accounting has been discontinued, are classified consistent with the nature of the instrument.

Cash flow hedges. Qualifying derivatives are accounted for as cash flow hedges when the hedged item is a forecasted transaction. Gains and losses on these instruments are recorded in other comprehensive income until the underlying transaction is recorded in earnings. When the hedged item is realized, gains or losses are reclassified from accumulated other comprehensive income (loss) (AOCI) to the Consolidated Statement of Income on the same line item as the underlying transaction.

Fair value hedges. Qualifying derivatives are accounted for as fair value hedges when the hedged item is a recognized asset, liability, or firm commitment. Gains and losses on these instruments are recorded in earnings, offsetting gains and losses on the hedged item.

Net investment hedges. Qualifying derivative and nonderivative financial instruments are accounted for as net investment hedges when the hedged item is a nonfunctional currency investment in a subsidiary. Gains and losses on these instruments are included in foreign currency translation adjustments in AOCI.

Other contracts. The Company also periodically enters into foreign currency forward contracts and options to reduce volatility in the translation of foreign currency earnings to U.S. dollars. Gains and losses on these instruments are recorded in other income (expense), net, generally reducing the exposure to translation volatility during a full-year period.

Foreign currency exchange risk. The Company is exposed to fluctuations in foreign currency cash flows related primarily to third-party purchases, intercompany transactions and when applicable, nonfunctional currency denominated third-party debt. The Company is also exposed to fluctuations in the value of foreign currency investments in subsidiaries and cash flows related to repatriation of these investments. Additionally, the Company is exposed to volatility in the translation of foreign currency denominated earnings to U.S. dollars. Management

assesses foreign currency risk based on transactional cash flows and translational volatility and may enter into forward contracts, options, and currency swaps to reduce fluctuations in long or short currency positions. Forward contracts and options are generally less than 18 months duration. Currency swap agreements are established in conjunction with the term of underlying debt issues.

For foreign currency cash flow and fair value hedges, the assessment of effectiveness is generally based on changes in spot rates. Changes in time value are reported in other income (expense), net.

Interest rate risk. The Company is exposed to interest rate volatility with regard to future issuances of fixed rate debt and existing and future issuances of variable rate debt. The Company periodically uses interest rate swaps, including forward-starting swaps, to reduce interest rate volatility and funding costs associated with certain debt issues, and to achieve a desired proportion of variable versus fixed rate debt, based on current and projected market conditions.

Fixed-to-variable interest rate swaps are accounted for as fair value hedges and the assessment of effectiveness is based on changes in the fair value of the underlying debt, using incremental borrowing rates currently available on loans with similar terms and maturities.

Price risk. The Company is exposed to price fluctuations primarily as a result of anticipated purchases of raw and packaging materials, fuel, and energy. The Company has historically used the combination of long-term contracts with suppliers, and exchange-traded futures and option contracts to reduce price fluctuations in a desired percentage of forecasted raw material purchases over a duration of generally less than 18 months.

Commodity contracts are accounted for as cash flow hedges. The assessment of effectiveness for exchange-traded instruments is based on changes in futures prices. The assessment of effectiveness for over-the-counter transactions is based on changes in designated indices.

New accounting standards

Multiemployer pension and postretirement benefit plans. In September 2011, the Financial Accounting Standards Board (FASB) amended the Accounting Standards Codification (ASC) to provide more information about an employer's financial obligations to multiemployer pension and post retirement benefit plans. Previously, employers were only required to disclose their total contributions to all multiemployer plans in which they participate and certain year-to-year changes in circumstances. The enhanced disclosures required under the revised guidance provide additional information regarding the overall financial health of the plan and the level of the employer's participation in the plan. The revised guidance is effective for fiscal year end 2011. Refer to Note 10 for disclosures regarding multiemployer plans in which the Company participates.

NOTE 2

GOODWILL AND OTHER INTANGIBLE ASSETS

For the periods presented, the Company's intangible assets consisted of the following:

Intangible assets subject to amortization

| (millions) | Gross carrying amount | | Accumulated amortization | |
|--------------------------|-----------------------|-------|--------------------------|-------|
| | 2011 | 2010 | 2011 | 2010 |
| Trademarks | \$ 19 | \$ 19 | \$ 17 | \$ 16 |
| Other | 41 | 41 | 32 | 31 |
| Total | \$ 60 | \$ 60 | \$ 49 | \$ 47 |
| | | | 2011 | 2010 |
| Amortization expense (a) | | | \$ 2 | \$ 2 |

(a) The currently estimated aggregate amortization expense for each of the next five succeeding fiscal periods is approximately \$2 million per year.

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Intangible assets not subject to amortization

| | Total carrying amount | |
|------------|-----------------------|----------|
| (millions) | 2011 | 2010 |
| Trademarks | \$ 1,443 | \$ 1,443 |

Changes in the carrying amount of goodwill

| (millions) | U.S. Morning Foods & Kashi | U.S. Snacks | U.S. Specialty | North America Other | Europe | Latin America | Asia Pacific | Corp- orate | Consoli- dated |
|---------------------------------|--|-----------------|-------------------|---------------------------|--------------|------------------|-----------------|----------------|-------------------|
| January 2, 2010 | \$ 80 | \$ 3,257 | \$ | \$ 202 | \$ 62 | \$ | \$ 42 | \$ | \$ 3,643 |
| Impairment charge | | | | | | | (20) | | (20) |
| Currency translation adjustment | | | | | | | 5 | | 5 |
| January 1, 2011 | \$ 80 | \$ 3,257 | \$ | \$ 202 | \$ 62 | \$ | \$ 27 | \$ | \$ 3,628 |
| Currency translation adjustment | | | | | (5) | | | | (5) |
| December 31, 2011 | \$ 80 | \$ 3,257 | \$ | \$ 202 | \$ 57 | \$ | \$ 27 | \$ | \$ 3,623 |

Impairment charges

In 2008, the Company acquired a majority interest in the business of Zhenghang Food Company Ltd. (Navigable Foods), a manufacturer of cookies and crackers in the northern and northeastern regions of China. The Company also obtained the option to purchase the noncontrolling interest of Navigable Foods beginning June 30, 2011 and the noncontrolling interest holder obtained the option to cause the Company to purchase its remaining interest. The options, which had similar terms, included an exercise price that approximated fair value on the date of exercise. During 2011, the Company exercised its option and acquired the noncontrolling interest for no consideration. A portion of the original purchase price aggregating \$5 million is payable in 2012 and is recorded on the Company's Consolidated Balance Sheet in other current liabilities.

In 2010, the Company recorded impairment charges totaling \$29 million in connection with Navigable Foods, which included \$20 million of goodwill. The China business generated operating losses since the acquisition and that trend was expected to continue. As a result, management determined in 2010 the current business has not proven to be the right vehicle for entry into the Chinese marketplace and began exploring various strategic alternatives to reduce operating losses in the future. The impairment charge was recorded in SGA expense in the Asia Pacific operating segment.

Prior to assessing the goodwill for impairment, the Company determined that the long-lived assets of the China reporting unit were impaired and should be written down to their estimated fair value of \$10 million. This resulted in a fixed asset impairment charge of \$9 million in 2010 that was recorded in the Asia Pacific operating segment, of which \$8 million was recorded in COGS, and \$1 million was recorded in SGA expense.

Subsequent to December 31, 2011, the Company sold the net assets of Navigable Foods for proceeds of \$11 million which approximated carrying value.

NOTE 3

EXIT OR DISPOSAL ACTIVITIES

The Company views its continued spending on cost-reduction initiatives 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.

Summary of activities

During 2011, the Company recorded \$24 million of costs associated with exit or disposal activities. \$7 million represented severance, \$12 million was for pension costs, \$2 million for other cash costs including relocation of assets and employees and \$3 million for asset write-offs. \$10 million of the charges were recorded in cost of goods sold (COGS) in the European reportable segment. \$14 million of the charges were recorded in selling, general and administrative (SGA) expense in the following reportable segments (in millions): U.S. Snacks \$13; and Europe \$1.

The Company recorded \$19 million of costs in 2010 associated with exit or disposal activities. \$6 million represented severance, \$7 million for other cash costs including relocation of assets and employees, \$5 million was for pension costs and \$1 million for asset write offs. \$4 million of the charges were recorded in COGS in the European reportable segment. \$15 million of the charges were recorded in SGA expense in the following reportable segments (in millions): U.S. Morning Foods and Kashi \$2; U.S. Snacks \$8; North America Other \$1; Europe \$2; and Asia Pacific \$2.

For 2009, the Company recorded charges of \$65 million associated with exit or disposal activities. \$42 million represented severance, \$3 million was for pension costs, \$6 million for asset write offs, and \$14 million for other cash costs including relocation of assets and employees. \$40 million of the charges were recorded in COGS in the following reportable segments (in millions): U.S. Morning Foods and Kashi \$4; U.S. Snacks \$9; North America Other \$1; Europe \$16; Latin America \$9; and Asia Pacific \$1. \$25 million of the charges were recorded in SGA expense in the following reportable segments (in millions): U.S. Morning Foods and Kashi \$4; U.S. Snacks \$3; U.S. Specialty \$2; North America Other \$1; Europe \$13; Latin America \$1; and Asia Pacific \$1.

At December 31, 2011, exit cost reserves were \$1 million, related to severance payments which will be made in 2012. Exit cost reserves at January 1, 2011 were \$5 million related to severance payments.

Cost summary

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During 2011, the Company incurred costs related to two ongoing programs which will result in COGS and SGA expense savings. The COGS program seeks to optimize the Company's global manufacturing network, reduce waste, and develop best practices on a global basis. The SGA programs focus on improvements in the efficiency and effectiveness of various global support functions. The Company commenced the COGS and the various SGA programs in 2009.

The following table presents the total program costs incurred for these programs through December 31, 2011.

| (millions) | Employee severance | Other cash costs (a) | Asset write-offs | Retirement benefits (b) | Total |
|---------------------------------------|-----------------------|-------------------------------|---------------------|-------------------------------|-------|
| For the year ended, January 2, 2010 | \$ 32 | \$ 14 | \$ | \$ 3 | \$ 49 |
| For the year ended, January 1, 2011 | 6 | 7 | 1 | 5 | 19 |
| For the year ended, December 31, 2011 | 7 | 2 | 3 | 12 | 24 |
| Total program costs | \$ 45 | \$ 23 | \$ 4 | \$ 20 | \$ 92 |

(a) Includes cash costs for equipment removal and relocation.

(b) Pension plan curtailment losses and special termination benefits.

The above costs impacted the reportable segments, as follows (in millions): U.S. Morning Foods and Kashi \$10; U.S. Snacks \$33; U.S. Specialty \$2; North America Other \$3; Europe \$39; Asia Pacific \$4; and Latin America \$1. The cost and cash outlay in 2012 for these programs is estimated to be an additional \$7 million.

The following table presents a reconciliation of the severance reserve for these programs.

| (millions) | Beginning of period | Accruals | Payments | End of period |
|--|------------------------|----------|----------|------------------|
| For the year ended, January 2, 2010 | \$ | \$ 32 | \$ (14) | \$ 18 |
| For the year ended, January 1, 2011 | \$ 18 | 6 | (19) | \$ 5 |
| For the year ended, December 31, 2011 | \$ 5 | 7 | (11) | \$ 1 |
| Total project to date | | \$ 45 | \$ (44) | |
| Prior year activities | | | | |

During 2009, in addition to the COGS and SGA programs above, the Company incurred costs related to a European manufacturing optimization program in Bremen, Germany and a supply chain network rationalization program in Latin America.

The Company incurred \$7 million of costs representing cash payments for severance, related to a manufacturing optimization program in Bremen, Germany. The program resulted in cash savings through the elimination of employee positions and was recorded within COGS in the European reportable segment. The program was substantially complete in 2009. Severance reserves were \$7 million as of January 2, 2010 and were paid during 2010.

The Company incurred \$9 million of costs related to a supply chain rationalization in Latin America which resulted in the closing of a plant in Guatemala. The charges represent \$3 million of cash payments for severance and other cash costs associated with the elimination of employee positions and \$6 million for asset removal and relocation costs as well as non-cash asset write offs. Efficiencies gained in other plants in the Latin America network allow the Company to service the Guatemala market from those plants. The costs were recorded in COGS in the Latin America reportable segment and there were no severance reserves as of January 2, 2010.

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

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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:

| (millions, except per share data) | Net income attributable to Kellogg Company | Average shares outstanding | Earnings per share |
|-----------------------------------|---|----------------------------------|--------------------------|
| 2011 | | | |
| Basic | \$ 1,231 | 362 | \$ 3.40 |
| Dilutive potential common shares | | 2 | (0.02) |
| Diluted | \$ 1,231 | 364 | \$ 3.38 |
| 2010 | | | |
| Basic | \$ 1,247 | 376 | \$ 3.32 |
| Dilutive potential common shares | | 2 | (0.02) |
| Diluted | \$ 1,247 | 378 | \$ 3.30 |
| 2009 | | | |
| Basic | \$ 1,212 | 382 | \$ 3.17 |
| Dilutive potential common shares | | 2 | (0.01) |
| Diluted | \$ 1,212 | 384 | \$ 3.16 |

The total number of anti-dilutive potential common shares excluded from the reconciliation for each period was (in millions): 2011-4.2; 2010-4.9; 2009-12.2.

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): 2011 7; 2010 5; 2009 3. The Company issued shares totaling less than

one million in each of the years presented under *Kellogg DirectTM*, a direct stock purchase and dividend reinvestment plan for U.S. shareholders.

On April 23, 2010, the Company's board of directors authorized a \$2.5 billion three-year share repurchase program for 2010 through 2012. During 2011, the Company repurchased 15 million shares of common stock for a total of \$793 million. During 2010, the Company repurchased 21 million shares of common stock for a total of \$1,057 million, of which \$1,052 was paid during the year and \$5 million was payable at January 1, 2011. During 2009, the Company repurchased 4 million shares of common stock at a total cost of \$187 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 for all years presented 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. In 2011, other comprehensive income also includes fair value adjustments associated with net investment hedges of foreign subsidiaries.

During 2011, the Company's postretirement and postemployment plans incurred net experience losses totaling \$492 million, net of tax, due primarily to losses on plan assets and discount rate reductions. During 2010, the Company amended its U.S. postretirement healthcare benefit plan, which resulted in a \$17 million decrease of a deferred tax asset and is included in tax expense with prior service credit (cost) arising during the period.

| (millions) | Pre-tax amount | Tax (expense) or benefit | After-tax amount |
|---|-------------------|--------------------------------|---------------------|
| 2011 | | | |
| Net income | | | \$ 1,229 |
| Other comprehensive loss: | | | |
| Foreign currency translation adjustments | \$ (105) | \$ (2) | (107) |
| Cash flow hedges: | | | |
| Unrealized gain (loss) on cash flow hedges | (51) | 18 | (33) |
| Reclassification to net earnings | (2) | 1 | (1) |
| Postretirement and postemployment benefits: | | | |
| Amounts arising during the period: | | | |
| Net experience gain (loss) | (728) | 236 | (492) |
| Prior service credit (cost) | (3) | 1 | (2) |
| Reclassification to net earnings: | | | |
| Net experience loss | 131 | (47) | 84 |
| Prior service cost | 11 | (4) | 7 |
| | \$ (747) | \$ 203 | (544) |
| Total comprehensive income | | | \$ 685 |
| 2010 | | | |
| Net income | | | \$ 1,240 |
| Other comprehensive income: | | | |
| Foreign currency translation adjustments | \$ (18) | \$ | (18) |
| Cash flow hedges: | | | |
| Unrealized gain (loss) on cash flow hedges | 51 | (21) | 30 |
| Reclassification to net earnings | 34 | (9) | 25 |
| Postretirement and postemployment benefits: | | | |
| Amounts arising during the period: | | | |
| Net experience gain (loss) | (71) | 30 | (41) |
| Prior service credit (cost) | (8) | (13) | (21) |
| Reclassification to net earnings: | | | |
| Net experience loss | 102 | (32) | 70 |
| Prior service cost | 11 | (4) | 7 |
| | \$ 101 | \$ (49) | 52 |
| Total comprehensive income | | | \$ 1,292 |
| 2009 | | | |
| Net income | | | \$ 1,208 |
| Other comprehensive income: | | | |
| Foreign currency translation adjustments | \$ 65 | \$ | 65 |
| Cash flow hedges: | | | |
| Unrealized gain (loss) on cash flow hedges | (6) | 3 | (3) |
| Reclassification to net earnings | (3) | | (3) |
| Postretirement and postemployment benefits: | | | |

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| | | | |
|------------------------------------|--------|---------|----------|
| Amounts arising during the period: | | | |
| Net experience gain (loss) | 161 | (72) | 89 |
| Prior service credit (cost) | (33) | 11 | (22) |
| Reclassification to net earnings: | | | |
| Net experience loss | 63 | (21) | 42 |
| Prior service cost | 11 | (4) | 7 |
| | \$ 258 | \$ (83) | 175 |
| Total comprehensive income | | | \$ 1,383 |

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Accumulated other comprehensive income (loss) as of December 31, 2011 and January 1, 2011 consisted of the following:

| (millions) | December 31, 2011 | January 1, 2011 |
|---|----------------------|--------------------|
| Foreign currency translation adjustments | \$ (896) | \$ (789) |
| Cash flow hedges unrealized net gain (loss) | (9) | 25 |
| Postretirement and postemployment benefits: | | |
| Net experience loss | (1,483) | (1,075) |
| Prior service cost | (70) | (75) |
| Total accumulated other comprehensive income (loss) | \$ (2,458) | \$ (1,914) |

NOTE 5

LEASES AND OTHER COMMITMENTS

The Company's leases are generally for equipment and warehouse space. Rent expense on all operating leases was (in millions): 2011-\$166; 2010-\$154; 2009-\$150. The Company did not enter into any material capital lease agreements during 2009, 2010 or 2011.

At December 31, 2011, future minimum annual lease commitments under non-cancelable operating and capital leases were as follows:

| (millions) | Operating leases | Capital leases |
|--|---------------------|-------------------|
| 2012 | \$ 150 | \$ 1 |
| 2013 | 123 | 1 |
| 2014 | 93 | 1 |
| 2015 | 69 | 1 |
| 2016 | 59 | |
| 2017 and beyond | 95 | 1 |
| Total minimum payments | \$ 589 | \$ 5 |
| Amount representing interest | | (1) |
| Obligations under capital leases | | 4 |
| Obligations due within one year | | (1) |
| Long-term obligations under capital leases | | \$ 3 |

The Company has provided various standard indemnifications in agreements to sell and purchase business assets and lease facilities over the past several years, related primarily to pre-existing tax, environmental, and employee benefit obligations. Certain of these indemnifications are limited by agreement in either amount and/or term and others are unlimited. The Company has also provided various hold harmless provisions within certain service type agreements. Because the Company is not currently aware of any actual exposures associated with these indemnifications, management is unable to estimate the maximum potential future payments to be made. At December 31, 2011, the Company had not recorded any liability related to these indemnifications.

NOTE 6

DEBT

The following table presents the components of notes payable at year end December 31, 2011 and January 1, 2011:

| (millions) | 2011 | | 2010 | |
|-----------------------|---------------------|----------------------------|---------------------|----------------------------|
| | Principal amount | Effective interest rate | Principal amount | Effective interest rate |
| U.S. commercial paper | \$ 216 | 0.24% | \$ | % |
| Bank borrowings | 18 | | 44 | |
| Total | \$ 234 | | \$ 44 | |

Long-term debt at year end consisted primarily of issuances of U.S. Dollar Notes, as follows:

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| (millions) | 2011 | 2010 |
|---|----------|----------|
| (a) 7.45% U.S. Dollar Debentures due 2031 | \$ 1,090 | \$ 1,090 |
| (b) 4.0% U.S. Dollar Notes due 2020 | 992 | 991 |
| (c) 4.25% U.S. Dollar Notes due 2013 | 772 | 800 |
| (d) 4.45% U.S. Dollar Notes due 2016 | 763 | 748 |
| (e) 5.125% U.S. Dollar Notes due 2012 | 760 | 768 |
| (f) 1.875% U.S. Dollar Notes due 2016 | 499 | |
| (g) 4.15% U.S. Dollar Notes due 2019 | 499 | 498 |
| (h) 3.25% U.S. Dollar Notes due 2018 | 409 | |
| (a) 6.6% U.S. Dollar Notes due 2011 | | 951 |
| Other | 14 | 14 |
| | 5,798 | 5,860 |
| Less current maturities | (761) | (952) |
| Balance at year end | \$ 5,037 | \$ 4,908 |

- (a) In March 2001, the Company issued \$4.6 billion of long-term debt instruments, primarily to finance the acquisition of Keebler Foods Company. The preceding table reflects the remaining principal amounts outstanding as of year-end 2011 and 2010. The debt securities contain standard events of default and covenants. The Notes due 2011 and the Debentures due 2031 could be redeemed in whole or in part by the Company at any time at prices determined under a formula (but not less than 100% of the principal amount plus unpaid interest to the redemption date). The effective interest rate on the Debentures due 2031, reflecting issuance discount and hedge settlement, was 7.62%. In May 2009, the Company entered into interest rate swaps with notional amounts totaling \$400 million, which effectively converted a portion of the Notes due 2011 from a fixed rate to a floating rate obligation for the remainder of the ten-year term. These derivative instruments were designated as fair value hedges of the debt obligation. The Company redeemed \$72 million of the Notes due 2011 in December 2007, an additional \$482 million in December 2009, and the remainder in April 2011. The Company incurred \$35 million of interest expense and \$3 million of accelerated losses on interest rate swaps previously recorded in accumulated other comprehensive income in connection with the 2009 redemption.
- (b) On December 8, 2010, the Company issued \$1.0 billion of ten-year 4.0% fixed rate U.S. Dollar Notes, using net proceeds from these Notes for incremental pension and postretirement

benefit plan contributions and to retire a portion of its commercial paper. The effective interest rate on these Notes, reflecting issuance discount and hedge settlement, was 3.42%. 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. The customary covenants also contain a change of control provision.

- (c) On March 6, 2008, the Company issued \$750 million of five-year 4.25% fixed rate U.S. Dollar Notes, using the proceeds from these Notes to retire a portion of its U.S. commercial paper. The effective interest rate on these Notes, reflecting issuance discount, hedge settlement and interest rate swaps was 1.733% at December 31, 2011. 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. The customary covenants also contain a change of control provision. In conjunction with this debt issuance, the Company entered into interest rate swaps with notional amounts totaling \$750 million, which effectively converted this debt from a fixed rate to a floating rate obligation. These derivative instruments were designated as fair value hedges of the debt obligation. During 2011, the Company transferred a portion of the interest rate swaps to another counterparty and subsequently terminated all the interest rate swaps. The resulting unamortized gain of \$22 million at December 31, 2011 will be amortized to interest expense over the remaining term of the Notes.
- (d) On May 18, 2009, the Company issued \$750 million of seven-year 4.45% fixed rate U.S. Dollar Notes, using net proceeds from these Notes to retire a portion of its commercial paper. The effective interest rate as of December 31, 2011 on these Notes, reflecting issuance discount, hedge settlement and interest rate swaps, was 3.89%. 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. The customary covenants also contain a change of control provision. In February 2011, the Company entered into interest rate swaps with notional amounts totaling \$200 million, which effectively converted a portion of these Notes from a fixed rate to a floating rate obligation for the remainder of the seven-year term. These derivative instruments were designated as fair value hedges of the debt obligation. The fair value adjustment for the interest rate swaps was \$14 million, and was recorded as an increase in the hedged debt balance at December 31, 2011.
- (e) In December 2007, the Company issued \$750 million of five-year 5.125% fixed rate U.S. Dollar Notes, using the proceeds from these Notes to replace a portion of its U.S. commercial paper. The effective interest rate on these Notes, reflecting issuance discount, hedge settlement and interest rate swaps was 3.632% at December 31, 2011. 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. The customary covenants also contain a change of control provision. In May 2009, the Company entered into interest rate swaps with notional amounts totaling \$750 million, which effectively converted these Notes from a fixed rate to a floating rate obligation. These derivative instruments were designated as fair value hedges of the debt obligation. In August 2011, the Company terminated the interest rate swaps. The unamortized gain of \$10 million at December 31, 2011 will be amortized to interest expense over the remaining term of the Notes.
- (f) On November 14, 2011, the Company issued \$500 million of five-year 1.875% fixed rate U.S. Dollar Notes, using net proceeds from these Notes for general corporate purposes including repayment of a portion of its commercial paper. The effective interest rate on these Notes, reflecting issuance discount and hedge settlement, was 1.98%. 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. The customary covenants also contain a change of control provision.
- (g) On November 15, 2009, the Company issued \$500 million of ten-year 4.15% fixed rate U.S. Dollar Notes, using net proceeds from these Notes to retire a portion of its 6.6% U.S. Dollar Notes due 2011. The effective interest rate on these Notes, reflecting issuance discount and hedge settlement, was 4.23%. 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. The customary covenants also contain a change of control provision.
- (h) On May 16, 2011, the Company issued \$400 million of seven-year 3.25% fixed rate U.S. Dollar Notes, using net proceeds from these Notes for general corporate purposes including repayment of a portion of its commercial paper. The effective interest rate as of December 31, 2011 on these Notes, reflecting issuance discount, hedge settlement and interest rate swaps, was 2.31%. 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. The customary covenants also contain a change of control provision. In October 2011, the Company entered into interest rate swaps with notional amounts totaling \$400 million, which effectively converted these Notes from a fixed rate to a floating rate obligation for the remainder of the seven-year term. These derivative instruments were designated as fair value hedges of the debt obligation. The fair value adjustment for the interest rate swaps was \$10 million, and was recorded as an increase in the hedged debt balance at December 31, 2011.

In February 2007, the Company and two of its subsidiaries (the Issuers) established a program under which the Issuers may issue euro-commercial paper notes up to a maximum aggregate amount outstanding at any time of \$750 million or its equivalent in alternative currencies. The notes may have maturities ranging up to 364 days and will be senior unsecured obligations of the applicable Issuer. Notes issued by subsidiary Issuers will be guaranteed by the Company. The notes may be issued at a discount or may bear fixed or floating rate interest or a coupon calculated by reference to an index or formula. As of December 31, 2011 and January 1, 2011, no notes were outstanding under this program.

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At December 31, 2011, the Company had \$2.2 billion of short-term lines of credit, virtually all of which were unused and available for borrowing on an unsecured basis. These lines were comprised principally of an unsecured Four-Year Credit Agreement, which the Company entered into in March 2011 and expires in 2015, replacing the Company's unsecured Five-Year

Credit Agreement, which would have expired in November 2011. The Four-Year Credit Agreement allows the Company to borrow, on a revolving credit basis, up to \$2.0 billion, to obtain letters of credit in an aggregate amount up to \$75 million, U.S. swingline loans in an aggregate amount up to \$200 million and European swingline loans in an aggregate amount up to \$400 million and to provide a procedure for lenders to bid on short-term debt of the Company. The agreement contains customary covenants and warranties, including specified restrictions on indebtedness, liens, sale and leaseback transactions, and a specified interest coverage ratio. If an event of default occurs, then, to the extent permitted, the administrative agent may terminate the commitments under the credit facility, accelerate any outstanding loans under the agreement, and demand the deposit of cash collateral equal to the lender's letter of credit exposure plus interest.

Scheduled principal repayments on long-term debt are (in millions): 2012 \$750; 2013 \$752; 2014 \$8; 2015 \$1; 2016 \$1,251; 2017 and beyond \$3,001.

Interest paid was (in millions): 2011 \$249; 2010 \$244; 2009 \$302. Interest expense capitalized as part of the construction cost of fixed assets was (in millions): 2011 \$5; 2010 \$2; 2009 \$3.

NOTE 7

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, and to a lesser extent, executive performance shares and restricted stock grants. 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. These awards are administered through several plans, as described within this Note.

The 2009 Long-Term Incentive Plan (2009 Plan), approved by shareholders in 2009, permits awards to employees and officers in the form of incentive and non-qualified stock options, performance units, restricted stock or restricted stock units, and stock appreciation rights. The 2009 Plan, which replaced the 2003 Long-Term Incentive Plan (2003 Plan), authorizes the issuance of a total of (a) 27 million shares; plus (b) the total number of shares as to which awards granted under the 2009 Plan or the 2003 or 2001 Incentive Plans expire or are forfeited, terminated or settled in cash. No more than 5 million shares can be issued in satisfaction of performance units, performance-based restricted shares and other awards (excluding stock options and stock appreciation rights). There are additional annual limitations on awards or payments to individual participants. Options granted under the 2009 Plan generally vest over three years. At December 31, 2011, there were 16 million remaining authorized, but unissued, shares under the 2009 Plan.

The Non-Employee Director Stock Plan (2009 Director Plan) was approved by shareholders in 2009 and allows each eligible non-employee director to receive shares of the Company's common stock annually. The number of shares granted pursuant to each annual award will be determined by the Nominating and Governance Committee of the Board of Directors. The 2009 Director Plan, which replaced the 2000 Non-Employee Director Stock Plan (2000 Director Plan), reserves 500,000 shares for issuance, plus the total number of shares as to which awards granted under the 2009 Director Plan or the 2000 Director Plans expire or are forfeited, terminated or settled in cash. Under both the 2009 and 2000 Director Plans, shares (other than stock options) are placed in the Kellogg Company Grantor Trust for Non-Employee Directors (the Grantor Trust). Under the terms of the Grantor Trust, shares are available to a director only upon termination of service on the Board. Under the 2009 Director Plan, awards were as follows (number of shares): 2011-24,850; 2010-26,000; 2009-32,510.

The 2002 Employee Stock Purchase Plan was approved by shareholders in 2002 and permits eligible employees to purchase Company stock at a discounted price. This plan allows for a maximum of 2.5 million shares of Company stock to be issued at a purchase price equal to 95% of the fair market value of the stock on the last day of the quarterly purchase period. Total purchases through this plan for any employee are limited to a fair market value of \$25,000 during any calendar year. At December 31, 2011, there were approximately 0.7 million remaining authorized, but unissued, shares under this plan. Shares were purchased by employees under this plan as follows (approximate number of shares): 2011 110,000; 2010 123,000; 2009 159,000. Options granted to employees to purchase discounted stock under this plan are included in the option activity tables within this note.

Additionally, during 2002, an international subsidiary of the Company established a stock purchase plan for its employees. Subject to limitations, employee contributions to this plan are matched 1:1 by the Company. Under this plan, shares were granted by the Company to match an equal number of shares purchased by employees as follows (approximate number of shares): 2011 68,000; 2010 66,000; 2009 74,000.

Compensation expense for all types of equity-based programs and the related income tax benefit recognized were as follows:

| (millions) | 2011 | 2010 | 2009 |
|------------------------------|-------|-------|-------|
| Pre-tax compensation expense | \$ 37 | \$ 29 | \$ 48 |
| Related income tax benefit | \$ 13 | \$ 10 | \$ 17 |

As of December 31, 2011, total stock-based compensation cost related to non-vested awards not yet recognized was \$42 million and the weighted-average period over which this amount is expected to be recognized was 2 years.

Cash flows realized upon exercise or vesting of stock-based awards in the periods presented are included in the following table. Tax benefits realized upon exercise or vesting of stock-based awards generally represent the tax benefit of the difference between the exercise price and the strike price of the option.

Cash used by the Company to settle equity instruments granted under stock-based awards was insignificant.

| (millions) | 2011 | 2010 | 2009 |
|---|--------|--------|--------|
| Total cash received from option exercises and similar instruments | \$ 291 | \$ 204 | \$ 131 |
| Tax benefits realized upon exercise or vesting of stock-based awards: | | | |
| Windfall benefits classified as financing cash flow | 11 | 8 | 4 |
| Other amounts classified as operating cash flow | 25 | 20 | 12 |
| Total | \$ 36 | \$ 28 | \$ 16 |

Shares used to satisfy stock-based awards are normally issued out of treasury stock, although management is authorized to issue new shares to the extent permitted by respective plan provisions. Refer to Note 4 for information on shares issued during the periods presented to employees and directors under various long-term incentive plans and share repurchases under the Company's stock repurchase authorizations. The Company does not currently have a policy of repurchasing a specified number of shares issued under employee benefit programs during any particular time period.

Stock options

During the periods presented, non-qualified stock options were granted to eligible employees under the 2009 Plan with exercise prices equal to the fair market value of the Company's stock on the grant date, a contractual term of ten years, and a three-year graded vesting period.

Management estimates the fair value of each annual stock option award on the date of grant using a lattice-based option valuation model. Composite assumptions are presented in the following table. Weighted-average values are disclosed for certain inputs which incorporate a range of assumptions. Expected volatilities are based principally on historical volatility of the Company's stock, and to a lesser extent, on implied volatilities from traded options on the Company's stock. Historical volatility corresponds to the contractual term of the options granted. The Company uses historical data to estimate option exercise and employee termination within the valuation models; separate groups of employees that have similar historical exercise behavior are considered separately for valuation purposes. The expected term of options granted represents the period of time that options granted are expected to be outstanding; the weighted-average expected term for all employee groups is presented in the following table. The risk-free rate for periods within the contractual life of the options is based on the U.S. Treasury yield curve in effect at the time of grant.

| Stock option valuation model assumptions for grants within the year ended: | 2011 | 2010 | 2009 |
|--|---------|---------|---------|
| Weighted-average expected volatility | 17.00% | 20.00% | 24.00% |
| Weighted-average expected term (years) | 6.99 | 4.94 | 5.00 |
| Weighted-average risk-free interest rate | 3.06% | 2.54% | 2.10% |
| Dividend yield | 3.10% | 2.80% | 3.40% |
| Weighted-average fair value of options granted | \$ 7.59 | \$ 7.90 | \$ 6.33 |

A summary of option activity for the year ended December 31, 2011 is presented in the following table:

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| Employee and director stock options | Shares (millions) | Weighted-average exercise price | Weighted-average remaining contractual term (yrs.) | Aggregate intrinsic value (millions) |
|-------------------------------------|-------------------|---------------------------------|--|--------------------------------------|
| Outstanding, beginning of year | 26 | \$ 47 | | |
| Granted | 5 | 53 | | |
| Exercised | (6) | 45 | | |
| Forfeitures and expirations | (1) | 52 | | |
| Outstanding, end of year | 24 | \$ 48 | 6.2 | \$ 80 |
| Exercisable, end of year | 16 | \$ 47 | 5.0 | \$ 69 |

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Additionally, option activity for the comparable prior year periods is presented in the following table:

| (millions, except per share data) | 2010 | 2009 |
|-----------------------------------|-------|-------|
| Outstanding, beginning of year | 26 | 26 |
| Granted | 4 | 4 |
| Exercised | (4) | (3) |
| Forfeitures and expirations | | (1) |
| Outstanding, end of year | 26 | 26 |
| Exercisable, end of year | 20 | 22 |
| Weighted-average exercise price: | | |
| Outstanding, beginning of year | \$ 45 | \$ 45 |
| Granted | 53 | 40 |
| Exercised | 43 | 41 |
| Forfeitures and expirations | | 48 |
| Outstanding, end of year | \$ 47 | \$ 45 |
| Exercisable, end of year | \$ 46 | \$ 45 |

The total intrinsic value of options exercised during the periods presented was (in millions): 2011 \$63; 2010 \$45; 2009 \$25.

Other stock-based awards

During the periods presented, other stock-based awards consisted principally of executive performance shares and restricted stock granted under the 2009 Plan.

In 2011, 2010 and 2009, the Company made performance share awards to a limited number of senior executive-level employees, which entitles these employees to receive a specified number of shares of the Company's common stock on the vesting date, provided cumulative three-year targets are achieved. The cumulative three-year targets involved operating profit and internal net sales growth for the 2011 and 2010 grants, and cost savings for the 2009 grant. Management estimates the fair value of performance share awards based on the market price of the underlying stock on the date of grant, reduced by the present value of estimated dividends foregone during the performance period. The 2011, 2010 and 2009 target grants (as revised for non-vested forfeitures and other adjustments) currently correspond to approximately 224,000, 198,000 and 168,000 shares, respectively, with a grant-date fair value of \$48, \$48, and \$36 per share. The actual number of shares issued on the vesting date could range from zero to 200% of target, depending on actual performance achieved. Based on the market price of the Company's common stock at year-end 2011, the maximum future value that could be awarded on the vesting date was (in millions): 2011 award \$23; 2010 award \$20; and 2009 award \$7. The 2008 performance share award, payable in stock, was settled at 69% of target in February 2011 for a total dollar equivalent of \$6 million.

The Company also periodically grants restricted stock and restricted stock units to eligible employees under the 2009 Plan. Restrictions with respect to sale or transferability generally lapse after three years and the grantee is normally entitled to receive shareholder dividends during the vesting period. Management estimates the fair value of restricted stock grants based on the market price of the underlying stock on the date of grant. A summary of restricted stock activity for the year ended December 31, 2011, is presented in the following table:

| Employee restricted stock and restricted stock units | Shares (thousands) | Weighted-average grant-date fair value |
|--|-----------------------|--|
| Non-vested, beginning of year | 304 | \$ 49 |
| Granted | 102 | 51 |
| Vested | (145) | 47 |
| Forfeited | (5) | 47 |
| Non-vested, end of year | 256 | \$ 50 |

Grants of restricted stock and restricted stock units for comparable prior-year periods were: 2010 121,000; 2009 68,000.

The total fair value of restricted stock and restricted stock units vesting in the periods presented was (in millions): 2011 \$7; 2010 \$3; 2009 \$3.

NOTE 8

PENSION BENEFITS

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The Company sponsors a number of U.S. and foreign pension plans to provide retirement benefits for its employees. The majority of these plans are funded or unfunded defined benefit plans, although the Company does participate in a limited number of multiemployer or other defined contribution plans for certain employee groups. See Note 10 for more information regarding the Company's participation in multiemployer plans. Defined benefits for salaried employees are generally based on salary and years of service, while union employee benefits are generally a negotiated amount for each year of service.

Obligations and funded status

The aggregate change in projected benefit obligation, plan assets, and funded status is presented in the following tables.

| (millions) | 2011 | 2010 |
|--|----------|----------|
| Change in projected benefit obligation | | |
| Beginning of year | \$ 3,930 | \$ 3,605 |
| Service cost | 96 | 88 |
| Interest cost | 209 | 200 |
| Plan participants' contributions | 2 | 2 |
| Amendments | 3 | 8 |
| Actuarial loss | 365 | 241 |
| Benefits paid | (220) | (203) |
| Foreign currency adjustments | (18) | (11) |
| End of year | \$ 4,367 | \$ 3,930 |
| Change in plan assets | | |
| Fair value beginning of year | \$ 3,967 | \$ 3,323 |
| Actual return on plan assets | (33) | 480 |
| Employer contributions | 180 | 350 |
| Plan participants' contributions | 2 | 2 |
| Benefits paid | (173) | (177) |
| Foreign currency adjustments | (12) | (11) |
| Fair value end of year | \$ 3,931 | \$ 3,967 |
| Funded status | \$ (436) | \$ 37 |
| Amounts recognized in the Consolidated Balance Sheet consist of | | |
| Other assets | \$ 150 | \$ 333 |
| Other current liabilities | (26) | (43) |
| Other liabilities | (560) | (253) |
| Net amount recognized | \$ (436) | \$ 37 |
| Amounts recognized in accumulated other comprehensive income consist of | | |
| Net experience loss | \$ 1,907 | \$ 1,277 |
| Prior service cost | 85 | 96 |
| Net amount recognized | \$ 1,992 | \$ 1,373 |

The accumulated benefit obligation for all defined benefit pension plans was \$4.0 billion and \$3.6 billion at December 31, 2011 and January 1, 2011, respectively. Information for pension plans with accumulated benefit obligations in excess of plan assets were:

| (millions) | 2011 | 2010 |
|--------------------------------|----------|--------|
| Projected benefit obligation | \$ 3,077 | \$ 248 |
| Accumulated benefit obligation | \$ 2,882 | \$ 207 |
| Fair value of plan assets | \$ 2,505 | \$ 11 |

Expense

The components of pension expense are presented in the following table. Pension expense for defined contribution plans relates to certain foreign-based defined contribution plans and multiemployer plans in the United States in which the Company participates on behalf of certain unionized workforces.

| (millions) | 2011 | 2010 | 2009 |
|--|--------|-------|-------|
| Service cost | \$ 96 | \$ 88 | \$ 79 |
| Interest cost | 209 | 200 | 196 |
| Expected return on plan assets | (369) | (316) | (315) |
| Amortization of unrecognized prior service cost | 14 | 14 | 13 |
| Recognized net loss | 106 | 81 | 46 |
| Curtailed and special termination benefits' net loss | 16 | | 6 |
| Pension expense: | | | |
| Defined benefit plans | 72 | 67 | 25 |
| Defined contribution plans | 35 | 32 | 38 |
| Total | \$ 107 | \$ 99 | \$ 63 |

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The estimated net experience loss and prior service cost for defined benefit pension plans that will be amortized from accumulated other comprehensive income into pension expense over the next fiscal year are approximately \$144 million and \$14 million, respectively.

The Company and certain of its subsidiaries sponsor 401(k) or similar savings plans for active employees. Expense related to these plans was \$36 million in 2011 and \$37 million 2010 and 2009. These amounts are not included in the preceding expense table. Company contributions to these savings plans approximate annual expense. Company contributions to multiemployer and other defined contribution pension plans approximate the amount of annual expense presented in the preceding table.

Beginning in 2010, new U.S. salaried and non-union hourly employees were not eligible to participate in the defined benefit pension plan. These employees are eligible to participate in an enhanced defined contribution plan. The change does not impact employees with a hire date before December 31, 2009. Related expense is included within 401(k) costs noted above.

Assumptions

The worldwide weighted-average actuarial assumptions used to determine benefit obligations were:

| | 2011 | 2010 | 2009 |
|---|------|------|------|
| Discount rate | 4.8% | 5.4% | 5.7% |
| Long-term rate of compensation increase | 4.2% | 4.2% | 4.1% |

The worldwide weighted-average actuarial assumptions used to determine annual net periodic benefit cost were:

| | 2011 | 2010 | 2009 |
|---|------|------|------|
| Discount rate | 5.4% | 5.7% | 6.2% |
| Long-term rate of compensation increase | 4.2% | 4.1% | 4.2% |
| Long-term rate of return on plan assets | 8.9% | 8.9% | 8.9% |

To determine the overall expected long-term rate of return on plan assets, the Company models expected returns over a 20-year investment horizon with respect to the specific investment mix of its major plans. The return assumptions used reflect a combination of rigorous historical performance analysis and forward-looking views of the financial markets including consideration of current yields on long-term bonds, price-earnings ratios of the major stock market indices, and long-term inflation. The U.S. model, which corresponds to approximately 71% of consolidated pension and other postretirement benefit plan assets, incorporates a long-term inflation assumption of 2.5% and an active management premium of 1% (net of fees) validated by historical analysis. Similar methods are used for various foreign plans with invested assets, reflecting local economic conditions. The expected rate of return for 2011 of 8.9% equated to approximately the 62nd percentile expectation. Refer to Note 1.

To conduct the annual review of discount rates, the Company selected the discount rate based on a cash-flow matching analysis using Towers Watson's proprietary RATE:Link tool and projections of the future benefit payments that constitute the projected benefit obligation for the plans. RATE:Link establishes the uniform discount rate that produces the same present value of the estimated future benefit payments, as is generated by discounting each year's benefit payments by a spot rate applicable to that year. The spot rates used in this process are derived from a yield curve created from yields on the 40th to 90th percentile of U.S. high quality bonds. A similar methodology is applied in Canada and Europe, except the smaller bond markets imply that yields between the 10th and 90th percentiles are preferable. The measurement dates for the defined benefit plans are consistent with the Company's fiscal year end. Accordingly, the Company selected discount rates to measure our benefit obligations consistent with market indices during December of each year.

Plan assets

The Company categorized Plan assets within a three level fair value hierarchy described as follows:

Investments stated at fair value as determined by quoted market prices (Level 1) include:

Cash and cash equivalents: Value based on cost, which approximates fair value.

Corporate stock, common: Value based on the last sales price on the primary exchange.

Investments stated at estimated fair value using significant observable inputs (Level 2) include:

Cash and cash equivalents: Institutional short-term investment vehicles valued daily.

Mutual funds: Valued at the net asset value of shares held by the Plan at year end.

Collective trusts: Value based on the net asset value of units held at year end.

Bonds: Value based on matrices or models from pricing vendors.

Investments stated at estimated fair value using significant unobservable inputs (Level 3) include:

Real Estate: Value based on the net asset value of units held at year end. The fair value of real estate holdings is based on market data including earnings capitalization, discounted cash flow analysis, comparable sales transactions or a combination of these methods.

Bonds: Value based on matrices or models from brokerage firms. A limited number of the investments are in default.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

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The Company's practice regarding the timing of transfers between levels is to measure transfers in at the beginning of the month and transfers out at the end of the month. For the year ended December 31, 2011, the Company had no transfers between Levels 1 and 2.

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The fair value of Plan assets as of December 31, 2011 summarized by level within the fair value hierarchy are as follows:

| (millions) | Total Level 1 | Total Level 2 | Total Level 3 | Total |
|---------------------------|------------------|------------------|------------------|-----------------|
| Cash and cash equivalents | \$ 96 | \$ 22 | \$ | \$ 118 |
| Corporate stock, common: | | | | |
| Domestic | 563 | | | 563 |
| International | 185 | | | 185 |
| Mutual funds: | | | | |
| Domestic equity | | 31 | | 31 |
| International equity | | 380 | | 380 |
| Collective trusts: | | | | |
| Domestic equity | | 696 | | 696 |
| International equity | | 841 | | 841 |
| Eurozone sovereign debt | | 13 | | 13 |
| Other international debt | | 242 | | 242 |
| Bonds, corporate | | 298 | 1 | 299 |
| Bonds, government | | 396 | | 396 |
| Bonds, other | | 55 | | 55 |
| Real estate | | | 105 | 105 |
| Other | 6 | (5) | 6 | 7 |
| Total | \$ 850 | \$ 2,969 | \$ 112 | \$ 3,931 |

The fair value of Plan assets at January 1, 2011 are summarized as follows:

| (millions) | Total Level 1 | Total Level 2 | Total Level 3 | Total |
|---------------------------|---------------------|---------------------|------------------|-----------------|
| Cash and cash equivalents | \$ 169 | \$ 38 | \$ | \$ 207 |
| Corporate stock, common | | | | |
| Domestic | 645 | | | 645 |
| International | 185 | | | 185 |
| Mutual funds: | | | | |
| Domestic equity | | 44 | | 44 |
| International equity | | 419 | | 419 |
| Collective trusts: | | | | |
| Domestic equity | | 600 | | 600 |
| International equity | | 959 | | 959 |
| Domestic debt | | 13 | | 13 |
| International debt | | 275 | | 275 |
| Bonds, corporate | | 350 | 1 | 351 |
| Bonds, government | | 180 | | 180 |
| Bonds, other | | 29 | | 29 |
| Real estate | | | 58 | 58 |
| Other | | (5) | 7 | 2 |
| Total | \$ 999 | \$ 2,902 | \$ 66 | \$ 3,967 |

There were no unfunded commitments to purchase investments at December 31, 2011 or January 1, 2011.

The Company's investment strategy for its major defined benefit plans is to maintain a diversified portfolio of asset classes with the primary goal of meeting long-term cash requirements as they become due. Assets are invested in a prudent manner to maintain the security of funds while maximizing returns within the Plan's investment policy. The investment policy specifies the type of investment vehicles appropriate for the Plan, asset allocation guidelines, criteria for the selection of investment managers, procedures to monitor overall investment performance as well as investment manager performance. It also provides guidelines enabling Plan fiduciaries to fulfill their responsibilities.

The current weighted-average target asset allocation reflected by this strategy is: equity securities 74%; debt securities 23%; other 3%. Investment in Company common stock represented 1.3% of consolidated plan assets at December 31, 2011 and January 1, 2011. Plan funding strategies are influenced by tax regulations and funding requirements. The Company currently expects to contribute approximately \$33 million to its defined benefit pension plans during 2012.

Level 3 gains and losses

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Changes in the fair value of the Plan's Level 3 assets are summarized as follows:

| (millions) | Bonds, corporate | Bonds, other | Real estate | Other | Total |
|------------------------------|---------------------|-----------------|----------------|-------------|---------------|
| January 2, 2010 | \$ 3 | \$ 4 | \$ 32 | \$ (2) | \$ 37 |
| Purchases | | 1 | 19 | 6 | 26 |
| Sales | (2) | (5) | | | (7) |
| Realized and unrealized gain | | | 7 | 1 | 8 |
| Transfer out | | | | 2 | 2 |
| January 1, 2011 | \$ 1 | \$ | \$ 58 | \$ 7 | \$ 66 |
| Purchases | 1 | | 50 | 2 | 53 |
| Sales | (1) | | (7) | (3) | (11) |
| Realized and unrealized gain | | | 4 | | 4 |
| December 31, 2011 | \$ 1 | \$ | \$ 105 | \$ 6 | \$ 112 |

The net change in Level 3 assets includes a gain attributable to the change in unrealized holding gains or losses related to Level 3 assets held at December 31, 2011 and January 1, 2011 totaling \$4 million and \$7 million, respectively.

Benefit payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid (in millions): 2012 \$217; 2013 \$205; 2014 \$213; 2015 \$219; 2016 \$244; 2017 to 2021 \$1,286.

NOTE 9

NONPENSION POSTRETIREMENT AND POSTEMPLOYMENT BENEFITS

Postretirement

The Company sponsors a number of plans to provide health care and other welfare benefits to retired employees in the United States and Canada, who have met certain age and service requirements. The majority of these plans are funded or unfunded defined benefit plans, although the Company does participate in a limited number of multiemployer or other defined contribution plans for certain employee

groups. The Company contributes to voluntary employee benefit association (VEBA) trusts to fund certain U.S. retiree health and welfare benefit obligations.

In the first quarter of 2010, the Patient Protection and Affordable Care Act (PPACA) was signed into law. There are various provisions which will impact the Company, however, the Act did not have a material impact on the accumulated benefit obligation as of January 1, 2011 for nonpension postretirement benefit plans.

Obligations and funded status

The aggregate change in accumulated postretirement benefit obligation, plan assets, and funded status is presented in the following tables.

| (millions) | 2011 | 2010 |
|--|----------|----------|
| Change in accumulated benefit obligation | | |
| Beginning of year | \$ 1,224 | \$ 1,162 |
| Service cost | 23 | 20 |
| Interest cost | 62 | 64 |
| Actuarial (gain) loss | (86) | 36 |
| Benefits paid | (67) | (60) |
| Foreign currency adjustments | (1) | 2 |
| End of year | \$ 1,155 | \$ 1,224 |
| Change in plan assets | | |
| Fair value beginning of year | \$ 1,008 | \$ 672 |
| Actual return on plan assets | 12 | 108 |
| Employer contributions | 12 | 293 |
| Benefits paid | (67) | (65) |
| Fair value end of year | \$ 965 | \$ 1,008 |
| Funded status | \$ (190) | \$ (216) |
| Amounts recognized in the Consolidated Balance Sheet consist of | | |
| Other current liabilities | \$ (2) | \$ (2) |
| Other liabilities | (188) | (214) |
| Net amount recognized | \$ (190) | \$ (216) |
| Amounts recognized in accumulated other comprehensive income consist of | | |
| Net experience loss | \$ 281 | \$ 315 |
| Prior service credit | (6) | (9) |
| Net amount recognized | \$ 275 | \$ 306 |
| Expense | | |

Components of postretirement benefit expense were:

| (millions) | 2011 | 2010 | 2009 |
|---|-------|-------|-------|
| Service cost | \$ 23 | \$ 20 | \$ 18 |
| Interest cost | 62 | 64 | 65 |
| Expected return on plan assets | (88) | (64) | (68) |
| Amortization of unrecognized prior service credit | (3) | (3) | (2) |
| Recognized net loss | 20 | 17 | 13 |
| Postretirement benefit expense: | | | |
| Defined benefit plans | 14 | 34 | 26 |
| Defined contribution plans | 14 | 14 | 14 |
| Total | \$ 28 | \$ 48 | \$ 40 |

The estimated net experience loss for defined benefit plans that will be amortized from accumulated other comprehensive income into nonpension postretirement benefit expense over the next fiscal year is expected to be approximately \$16 million, partially offset by amortization of prior service credit of \$3 million.

Assumptions

The weighted-average actuarial assumptions used to determine benefit obligations were:

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| | 2011 | 2010 | 2009 |
|---------------|------|------|------|
| Discount rate | 4.6% | 5.3% | 5.7% |

The weighted-average actuarial assumptions used to determine annual net periodic benefit cost were:

| | 2011 | 2010 | 2009 |
|---|------|------|------|
| Discount rate | 5.3% | 5.7% | 6.1% |
| Long-term rate of return on plan assets | 8.9% | 8.9% | 8.9% |

The Company determines the overall discount rate and expected long-term rate of return on VEBA trust obligations and assets in the same manner as that described for pension trusts in Note 8.

The assumed health care cost trend rate is 6.1% for 2012, decreasing gradually to 4.5% by the year 2015 and remaining at that level thereafter. These trend rates reflect the Company's historical experience and management's expectations regarding future trends. A one percentage point change in assumed health care cost trend rates would have the following effects:

| (millions) | One percentage point increase | One percentage point decrease |
|---|-------------------------------|-------------------------------|
| Effect on total of service and interest cost components | \$ 9 | \$ (7) |
| Effect on postretirement benefit obligation | 122 | (96) |

Plan assets

The fair value of Plan assets as of December 31, 2011 summarized by level within fair value hierarchy described in Note 8, are as follows:

| (millions) | Total Level 1 | Total Level 2 | Total Level 3 | Total |
|---------------------------|---------------|---------------|---------------|--------|
| Cash and cash equivalents | \$ 11 | \$ 15 | \$ | \$ 26 |
| Corporate stock, common: | | | | |
| Domestic | 181 | | | 181 |
| International | 20 | | | 20 |
| Mutual funds: | | | | |
| Domestic equity | | 53 | | 53 |
| International equity | | 76 | | 76 |
| Domestic debt | | 87 | | 87 |
| Collective trusts: | | | | |
| Domestic equity | | 185 | | 185 |
| International equity | | 135 | | 135 |
| Bonds, corporate | | 90 | | 90 |
| Bonds, government | | 98 | | 98 |
| Bonds, other | | 12 | | 12 |
| Other | 2 | | | 2 |
| Total | \$ 214 | \$ 751 | \$ | \$ 965 |

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The fair value of Plan assets at January 1, 2011 are summarized as follows:

| (millions) | Total Level 1 | Total Level 2 | Total Level 3 | Total |
|---------------------------|------------------|------------------|------------------|----------|
| Cash and cash equivalents | \$ 17 | \$ 31 | \$ | \$ 48 |
| Corporate stock, common | | | | |
| Domestic | 184 | | | 184 |
| International | 12 | | | 12 |
| Mutual funds: | | | | |
| Domestic equity | | 76 | | 76 |
| International equity | | 97 | | 97 |
| Domestic debt | | 73 | | 73 |
| Collective trusts: | | | | |
| Domestic equity | | 241 | | 241 |
| International equity | | 137 | | 137 |
| Bonds, corporate | | 99 | | 99 |
| Bonds, government | | 34 | | 34 |
| Bonds, other | | 7 | | 7 |
| Total | \$ 213 | \$ 795 | \$ | \$ 1,008 |

The Company's asset investment strategy for its VEBA trusts is consistent with that described for its pension trusts in Note 8. The current target asset allocation is 75% equity securities and 25% debt securities. The Company currently expects to contribute approximately \$17 million to its VEBA trusts during 2012.

Level 3 gains and losses

The change in the fair value of the Plan's Level 3 assets is summarized as follows:

| (millions) | Bonds, other |
|--------------------------|-----------------|
| January 2, 2010 | \$ 1 |
| Purchases | |
| Sales | (1) |
| January 1, 2011 | \$ |
| Purchases | |
| Sales | |
| December 31, 2011 | \$ |

Postemployment

Under certain conditions, the Company provides benefits to former or inactive employees, including salary continuance, severance, and long-term disability, in the United States and several foreign locations. The Company's postemployment benefit plans are unfunded. Actuarial assumptions used are generally consistent with those presented for pension benefits in Note 8. The aggregate change in accumulated postemployment benefit obligation and the net amount recognized were:

| (millions) | 2011 | 2010 |
|--|----------------|----------------|
| Change in accumulated benefit obligation | | |
| Beginning of year | \$ 85 | \$ 74 |
| Service cost | 6 | 6 |
| Interest cost | 4 | 4 |
| Actuarial loss | 6 | 8 |
| Benefits paid | (8) | (7) |
| End of year | \$ 93 | \$ 85 |
| Funded status | \$ (93) | \$ (85) |
| Amounts recognized in the Consolidated Balance Sheet consist of | | |
| Other current liabilities | \$ (9) | \$ (8) |
| Other liabilities | (84) | (77) |
| Net amount recognized | \$ (93) | \$ (85) |

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Amounts recognized in accumulated other comprehensive income consist of

| | | |
|-----------------------|-------|-------|
| Net experience loss | \$ 44 | \$ 43 |
| Net amount recognized | \$ 44 | \$ 43 |

Components of postemployment benefit expense were:

| (millions) | 2011 | 2010 | 2009 |
|--------------------------------|-------|-------|-------|
| Service cost | \$ 6 | \$ 6 | \$ 6 |
| Interest cost | 4 | 4 | 4 |
| Recognized net loss | 5 | 4 | 4 |
| Postemployment benefit expense | \$ 15 | \$ 14 | \$ 14 |

The estimated net experience loss that will be amortized from accumulated other comprehensive income into postemployment benefit expense over the next fiscal year is approximately \$5 million.

Benefit payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

| (millions) | Postretirement | Postemployment |
|------------|----------------|----------------|
| 2012 | \$ 66 | \$ 9 |
| 2013 | 68 | 9 |
| 2014 | 70 | 10 |
| 2015 | 71 | 10 |
| 2016 | 72 | 11 |
| 2017-2021 | 383 | 63 |

NOTE 10

MULTIEMPLOYER PENSION AND POSTRETIREMENT PLANS

The Company contributes to multiemployer defined contribution pension and postretirement benefit plans under the terms of collective-bargaining agreements that cover certain unionized employee groups in the United States. Contributions to these plans are included in total pension and postretirement benefit expense as reported in Notes 8 and 9, respectively.

Pension Benefits

The risks of participating in multiemployer pension plans are different from single-employer plans. Assets contributed to a multiemployer plan by one employer may be used to provide benefits to employees of other participating employers. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.

The Company's participation in multiemployer pension plans for the year ended December 31, 2011, is outlined in the table below. The EIN/PN column provides the Employee Identification Number (EIN) and the three-digit plan number (PN). The most recent Pension Protection Act (PPA) zone status available for 2011 and 2010 is for the plan year-ends as indicated below. The zone status is based on information that the Company received from the plan and is certified by the plan's actuary. Among other factors, plans in the red zone are generally less than 65 percent funded, plans in the yellow zone are between 65 percent and 80 percent funded, and plans in the green zone are at least 80 percent funded. The FIP/RP Status Pending/Implemented column indicates plans for which a financial improvement plan (FIP) or a rehabilitation plan (RP) is either pending or has been implemented. In addition to regular plan contributions, the Company may be subject to a surcharge if the plan is in the red zone. The Surcharge Imposed column indicates whether a surcharge has been imposed on contributions to the plan. The last column lists the expiration date(s) of the collective-bargaining agreement(s) (CBA) to which the plans are subject.

| Pension Trust Fund | EIN/PN | PPA Zone Status | | FIP/RP Status | Contributions by the Company (millions) | | | Surcharge Imposed | Expiration Date of CBA |
|--|------------------|--------------------|---------------------|---------------------|---|----------------|----------------|-------------------|-------------------------|
| | | 2011 | 2010 | Pending/Implemented | 2011 | 2010 | 2009 | | |
| Bakery and Confectionary Union and Industry International Pension Fund (a) | 52-6118572 / 001 | Green - 12/31/2010 | Yellow - 12/31/2009 | N/A | \$ 4.3 | \$ 3.8 | \$ 3.8 | No | 6/30/2012 to 11/1/2016 |
| Central States, Southeast and Southwest Areas Pension Fund (b) | 36-6044243 / 001 | Red - 12/31/2011 | Red - 12/31/2010 | Implemented | 4.1 | 3.6 | 3.6 | Yes | 1/31/2012 to 10/31/2014 |
| Western Conference of Teamsters Pension Trust (c) | 91-6145047 / 001 | Green - 12/31/2010 | Green - 12/31/2009 | N/A | 1.2 | 1.2 | 1.1 | No | 1/31/2012 to 3/29/2013 |
| Philadelphia Bakery Employers and Food Driver Salesmen's Union, Local 463 and the Teamsters Union Local 676 Pension Fund (d) | 23-6537145 / 001 | Green - 7/31/2011 | Yellow - 7/31/2010 | N/A | | 0.3 | 0.4 | N/A | N/A |
| Hagerstown Motor Carriers and Teamsters Pension Fund | 52-6045424 / 001 | Red - 6/30/2012 | Red - 6/30/2011 | Implemented | 0.4 | 0.3 | 0.3 | No | 10/3/2015 |
| Twin Cities Bakery Drivers Pension Plan | 41-6172265 / 001 | Red - 12/31/2011 | Red - 12/31/2010 | Implemented | 0.2 | 0.2 | 0.2 | Yes | 5/31/2012 |
| Other Plans | | | | | 2.4 | 2.2 | 2.3 | | |
| Total Contributions: | | | | | \$ 12.6 | \$ 11.6 | \$ 11.7 | | |

(a) The Company is party to multiple CBAs requiring contributions to this fund, each with its own expiration date. Over 70 percent of the Company's participants in this fund are covered by a single CBA that expires on 5/5/2013.

(b)

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The Company is party to multiple CBAs requiring contributions to this fund, each with its own expiration date. Over 40 percent of the Company's participants in this fund are covered by a single CBA that expires on 7/27/2014.

- (c) The Company is party to multiple CBAs requiring contributions to this fund, each with its own expiration date. Over 40 percent of the Company's participants in this fund are covered by a single CBA that expires on 3/24/2012.
- (d) Effective in November 2010, the Company ceased participation in the plan and accordingly made no contributions in 2011.

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The Company was listed in the Forms 5500 of the following plans as of the following plan year ends as providing more than 5 percent of total contributions:

| Pension Trust Fund | Contributions to the plan exceeded more than 5% of total contributions (as of the Plan's year end) |
|--|---|
| Philadelphia Bakery Employers and Food Driver Salesmen's Union, Local 463 and the Teamsters Union Local 676 Pension Fund | 7/31/2009 |
| Hagerstown Motor Carriers and Teamsters Pension Fund | 6/30/2011 and 6/30/2010 |
| Twin Cities Bakery Drivers Pension Plan | 12/31/2010 and 12/31/2009 |
| At the date the Company's financial statements were issued, Forms 5500 were not available for the plan years ending after June 30, 2011. | |

In addition to regular contributions, the Company could be obligated to pay additional amounts, known as a withdrawal liability, if a multiemployer pension plan has unfunded vested benefits and the Company decreases or ceases participation in that plan. The Company has recognized estimated withdrawal liability expense related to curtailment and special termination benefits associated with our withdrawal from certain multiemployer plans aggregating (in millions): 2011 \$12; 2010 \$5; 2009 \$12.

During 2011, the withdrawal liabilities recorded in 2010 and 2009 were settled for approximately \$3 million and \$8 million, respectively. The final calculation of the withdrawal liability recognized in 2011 is pending the finalization of certain plan year-related data and is therefore subject to adjustment. The associated cash obligation is payable over a maximum 20 year period; management has not determined the actual period over which the payments will be made.

Postretirement Benefits

Multiemployer postretirement benefit plans provide health care and other welfare benefits to active and retired employees who have met certain age and service requirements. Contributions to multiemployer postretirement benefit plans were (in millions): 2011 \$14; 2010 \$14; 2009 \$14.

NOTE 11

INCOME TAXES

The components of income before income taxes and the provision for income taxes were as follows:

| (millions) | 2011 | 2010 | 2009 |
|-----------------------------------|---------------|----------|----------|
| Income before income taxes | | | |
| United States | \$ 1,267 | \$ 1,271 | \$ 1,207 |
| Foreign | 465 | 471 | 477 |
| | 1,732 | 1,742 | 1,684 |
| Income taxes | | | |
| Currently payable | | | |
| Federal | 285 | 97 | 331 |
| State | 26 | 10 | 39 |
| Foreign | 108 | 129 | 146 |
| | 419 | 236 | 516 |
| Deferred | | | |
| Federal | 56 | 239 | (8) |
| State | 13 | 26 | (3) |
| Foreign | 15 | 1 | (29) |
| | 84 | 266 | (40) |
| Total income taxes | \$ 503 | \$ 502 | \$ 476 |

The difference between the U.S. federal statutory tax rate and the Company's effective income tax rate was:

| 2011 | 2010 | 2009 |
|------|------|------|
|------|------|------|

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| | | | |
|--|--------------|-------|-------|
| U.S. statutory income tax rate | 35.0% | 35.0% | 35.0% |
| Foreign rates varying from 35% | (4.2) | (4.1) | (4.2) |
| State income taxes, net of federal benefit | 1.5 | 1.4 | 1.4 |
| Cost (benefit) of remitted and unremitted foreign earnings | (1.3) | 0.9 | (0.8) |
| Tax audit activity | (0.4) | (1.6) | (0.9) |
| Net change in valuation allowances | 0.6 | 0.5 | 0.4 |
| Statutory rate changes, deferred tax impact | (0.4) | | |
| U.S. deduction for qualified production activities | (1.3) | (1.1) | (1.6) |
| Other | (0.5) | (2.2) | (1.1) |
| Effective income tax rate | 29.0% | 28.8% | 28.2% |

As presented in the preceding table, the Company's 2011 consolidated effective tax rate was 29.0%, as compared to 28.8% in 2010 and 28.2% in 2009. The 2011 effective income tax rate benefited from an international legal restructuring reflected in the cost (benefit) of remitted and unremitted foreign earnings. During the third quarter of 2011, the Company recorded a benefit of \$7 million from the decrease in the statutory rate in the United Kingdom.

As of December 31, 2011, the Company had recorded a deferred tax liability of \$25 million related to \$325 million of earnings. Accumulated foreign earnings of approximately \$1.7 billion, primarily in Europe, were considered indefinitely reinvested. Accordingly, deferred income taxes have not been provided on these earnings and it is not practical to estimate the deferred tax impact of those earnings.

The 2010 effective income tax rate was impacted primarily by the remeasurement of liabilities for uncertain tax positions. Authoritative guidance related to liabilities for uncertain tax positions requires the Company to remeasure its liabilities for uncertain tax positions based on information obtained during the period, including interactions with tax authorities. Based on these interactions with tax authorities in various state and foreign jurisdictions, we reduced certain liabilities for uncertain tax positions by \$42 million and increased others by \$13 million in 2010. The other line item contains the benefit from an immaterial correction of an item related to prior years that was booked in the first quarter of 2010, as well as the U.S. research and development tax credit.

The 2009 effective tax rate reflected the favorable impact of various audit settlements as well as a U.S. deduction for qualified production activities as defined by the Internal Revenue Code. The deduction is based on U.S. manufacturing activities. During 2009, the Company finalized its assessment of foreign earnings and capital to be repatriated under the prior year repatriation plan resulting in a favorable impact to the cost of remitted and unremitted foreign earnings.

Changes in valuation allowances on deferred tax assets and the corresponding impacts on the effective income tax rate result from management's assessment of the Company's ability to utilize certain future tax deductions, operating losses and tax credit carryforwards prior to expiration. Valuation allowances were recorded to reduce deferred tax assets to an amount that will, more likely than not, be realized in the future. The total tax benefit of carryforwards at year-end 2011 and 2010 were \$41 million and \$60 million, respectively, with related valuation allowances at year-end 2011 and 2010 of \$38 and \$35 million. Of the total carryforwards at year-end 2011, \$4 million expire in 2014; \$2 million in 2015; \$4 million in 2016 and the remainder expiring thereafter.

The following table provides an analysis of the Company's deferred tax assets and liabilities as of year-end 2011 and 2010. Operating loss and credit carryforwards decreased in 2011 due to the utilization of net operating losses and tax credit carryforwards. Deferred tax assets on employee benefits increased in 2011 due to losses on plan assets and discount rate reductions associated with the Company's pension and postretirement plans recorded in Other Comprehensive Income, net of tax. Additionally, the deferred tax liability for unremitted foreign earnings decreased by \$32 million; \$24 million of this change is attributable to the benefit recorded in 2011's consolidated effective income tax rate, while \$8 million relates to remeasurement for foreign currency changes.

| (millions) | Deferred tax assets | | Deferred tax liabilities | |
|---|---------------------|------------|--------------------------|--------------|
| | 2011 | 2010 | 2011 | 2010 |
| U.S. state income taxes | \$ 8 | \$ 7 | \$ 85 | \$ 77 |
| Advertising and promotion-related | 22 | 24 | | 3 |
| Wages and payroll taxes | 29 | 25 | | |
| Inventory valuation | 26 | 28 | | |
| Employee benefits | 312 | 187 | | 65 |
| Operating loss and credit carryforwards | 41 | 60 | | |
| Hedging transactions | 3 | 1 | | 16 |
| Depreciation and asset disposals | | 25 | 365 | 311 |
| Capitalized interest | | 7 | 2 | 9 |
| Trademarks and other intangibles | | | 477 | 472 |
| Deferred compensation | 39 | 48 | | |
| Stock options | 48 | 52 | | |
| Unremitted foreign earnings | | | 25 | 57 |
| Other | 53 | 51 | | 8 |
| | 581 | 515 | 954 | 1,018 |
| Less valuation allowance | (46) | (36) | | |
| Total deferred taxes | \$ 535 | \$ 479 | \$ 954 | \$ 1,018 |
| Net deferred tax asset (liability) | \$ (419) | \$ (539) | | |
| Classified in balance sheet as: | | | | |
| Other current assets | \$ 149 | \$ 110 | | |
| Other current liabilities | (7) | (13) | | |
| Other assets | 76 | 61 | | |
| Other liabilities | (637) | (697) | | |
| Net deferred tax asset (liability) | \$ (419) | \$ (539) | | |

The change in valuation allowance reducing deferred tax assets was:

| (millions) | 2011 | 2010 | 2009 |
|---|-------|-------|-------|
| Balance at beginning of year | \$ 36 | \$ 28 | \$ 22 |
| Additions charged to income tax expense | 12 | 11 | 14 |

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| | | | |
|---|-------|-------|-------|
| Reductions credited to income tax expense | (1) | (2) | (7) |
| Currency translation adjustments | (1) | (1) | (1) |
| Balance at end of year | \$ 46 | \$ 36 | \$ 28 |

Cash paid for income taxes was (in millions): 2011 \$271; 2010 \$409; 2009 \$409. Income tax benefits realized from stock option exercises and deductibility of other equity-based awards are presented in Note 7.

Uncertain tax positions

The Company is subject to federal income taxes in the U.S. as well as various state, local, and foreign jurisdictions. The Company's annual provision for U.S. federal income taxes represents approximately 70% of the Company's consolidated income tax provision. The Company was chosen to participate in the Internal Revenue Service (IRS) Compliance Assurance Program (CAP) beginning with the 2008 tax year. As a result, with limited exceptions, the Company is no longer subject to U.S. federal examinations by the IRS for years prior to 2011. The Company is under examination for income and non-income tax filings in various state and foreign jurisdictions, most notably Spain for years 2005 to 2006.

As of December 31, 2011, the Company has classified \$15 million of unrecognized tax benefits as a current liability. Management's estimate of reasonably possible changes in unrecognized tax benefits during the next twelve months is comprised of the 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 as of the years ended December 31, 2011, January 1, 2011 and January 2, 2010. For the 2011 year, approximately \$49 million represents the amount that, if recognized, would affect the Company's effective income tax rate in future periods.

| (millions) | 2011 | 2010 | 2009 |
|--|--------|--------|--------|
| Balance at beginning of year | \$ 104 | \$ 130 | \$ 132 |
| Tax positions related to current year: | | | |
| Additions | 7 | 12 | 17 |
| Tax positions related to prior years: | | | |
| Additions | 8 | 13 | 4 |
| Reductions | (19) | (42) | (9) |
| Settlements | (27) | (6) | (8) |
| Lapses in statutes of limitation | (7) | (3) | (6) |
| Balance at end of year | \$ 66 | \$ 104 | \$ 130 |

For the year ended December 31, 2011, the Company recognized a decrease of \$3 million of tax-related interest and penalties and had \$16 million accrued at year end. For the year ended January 1, 2011, the Company recognized an increase of \$2 million of tax-related interest and penalties and had approximately \$26 million accrued at January 1, 2011. For the year ended January 2, 2010, the Company recognized a reduction of \$1 million of tax-related interest and penalties and had approximately \$25 million accrued at January 2, 2010.

NOTE 12

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 and must be designated as a hedge at the inception of the contract.

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 December 31, 2011 and January 1, 2011 were as follows:

| (millions) | 2011 | 2010 |
|-------------------------------------|----------|----------|
| Foreign currency exchange contracts | \$ 1,265 | \$ 1,075 |
| Interest rate contracts | 600 | 1,900 |
| Commodity contracts | 175 | 379 |
| Total | \$ 2,040 | \$ 3,354 |

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 December 31, 2011 and January 1, 2011, measured on a recurring basis.

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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.

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 December 31, 2011 or January 1, 2011.

The following table presents assets and liabilities that were measured at fair value in the Consolidated Balance Sheet on a recurring basis as of December 31, 2011 and January 1, 2011:

| (millions) | Level 1 | | Level 2 | | Total | |
|---|---------------|--------------|----------------|----------------|----------------|----------------|
| | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 |
| Derivatives designated as hedging instruments: | | | | | | |
| Assets: | | | | | | |
| Foreign currency exchange contracts: | | | | | | |
| Other current assets | \$ | \$ | \$ 11 | \$ 7 | \$ 11 | \$ 7 |
| Interest rate contracts: | | | | | | |
| Other current assets | | | | 5 | | 5 |
| Other assets | | | 23 | 69 | 23 | 69 |
| Commodity contracts: | | | | | | |
| Other current assets | 2 | 23 | | | 2 | 23 |
| Total assets | \$ 2 | \$ 23 | \$ 34 | \$ 81 | \$ 36 | \$ 104 |
| Liabilities: | | | | | | |
| Foreign currency exchange contracts: | | | | | | |
| Other current liabilities | \$ | \$ | \$ (18) | \$ (27) | \$ (18) | \$ (27) |
| Commodity contracts: | | | | | | |
| Other current liabilities | (4) | | (12) | (10) | (16) | (10) |
| Other liabilities | | | (34) | (29) | (34) | (29) |
| Total liabilities | \$ (4) | \$ | \$ (64) | \$ (66) | \$ (68) | \$ (66) |

The fair value of non designated hedging instruments as of December 31, 2011 and January 1, 2011 was immaterial.

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The effect of derivative instruments on the Consolidated Statement of Income for the years ended December 31, 2011 and January 1, 2011 were as follows:

| Derivatives in fair value hedging relationships (millions) | Location of gain (loss) recognized in income | Gain (loss) recognized in income (a) | |
|---|--|--------------------------------------|----------------|
| | | 2011 | 2010 |
| Foreign currency exchange contracts | Other income (expense), net | \$ (12) | (\$ 51) |
| Interest rate contracts | Interest expense | \$ (1) | \$ |
| Total | | \$ (13) | \$ (51) |

(a) Includes the ineffective portion and amount excluded from effectiveness testing.

| Derivatives in cash flow hedging relationships (millions) | Gain (loss) recognized in AOCI | | Location of gain (loss) reclassified from AOCI | Gain (loss) reclassified from AOCI into income | | Location of gain (loss) recognized in income (a) | Gain (loss) recognized in income (a) | |
|--|--------------------------------|-------------|--|--|---------------|--|--------------------------------------|---------------|
| | 2011 | 2010 | | 2011 | 2010 | | 2011 | 2010 |
| Foreign currency exchange contracts | \$ | \$(19) | COGS | \$(3) | \$(25) | Other income (expense), net | \$ (2) | \$(1) |
| Foreign currency exchange contracts | 1 | | SGA expense | | (1) | Other income (expense), net | | |
| Interest rate contracts | (15) | 67 | Interest expense | 4 | (4) | N/A | | |
| Commodity contracts | (37) | 3 | COGS | 1 | (4) | Other income (expense), net | | (1) |
| Total | \$(51) | \$51 | | \$2 | \$(34) | | \$ (2) | \$ (2) |

(a) Includes the ineffective portion and amount excluded from effectiveness testing.

During the next 12 months, the Company expects \$8 million of net deferred losses reported in AOCI at December 31, 2011 to be reclassified to income, assuming market rates remain constant through contract maturities.

| Derivatives in net investment hedging relationships (millions) | Gain (loss) recognized in AOCI | |
|---|--------------------------------|-----------|
| | 2011 | 2010 |
| Foreign currency exchange contracts | \$ 6 | \$ |
| Total | \$ 6 | \$ |

| Derivatives not designated as hedging instruments (millions) | Location of gain (loss) recognized in income | Gain (loss) recognized in income | |
|---|--|----------------------------------|-----------|
| | | 2011 | 2010 |
| Foreign currency exchange contracts | Other income (expense), net | \$(1) | \$ |
| Interest rate contracts | Interest expense | \$ (1) | \$ |
| Total | | \$ (2) | \$ |

Certain of the Company's derivative instruments contain provisions requiring the Company to post collateral on those derivative instruments that are in a liability position if the Company's credit rating falls below BB+ (S&P), or Baa1 (Moody's). The fair value of all derivative instruments

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with credit-risk-related contingent features in a liability position on December 31, 2011 was \$46 million. If the credit-risk-related contingent features were triggered as of December 31, 2011, the Company would be required to post additional collateral of \$44 million. In addition, certain derivative instruments contain provisions that would be triggered in the event the Company defaults on its debt agreements. There were no collateral posting requirements as of December 31, 2011 triggered by credit-risk-related contingent features, however, there was \$2 million of collateral posted under the reciprocal collateralization agreements as discussed under counterparty credit risk concentration below.

Other fair value measurements

Level 3 assets measured on a nonrecurring basis at January 1, 2011 consisted of long-lived assets and goodwill.

The Company's calculation of the fair value of long-lived assets is based on market comparables, market trends and the condition of the assets. Long-lived assets with a carrying amount of \$19 million were written down to their fair value of \$10 million at January 1, 2011, resulting in an impairment charge of \$9 million, which was included in earnings for the period.

Goodwill with a carrying amount of \$20 million was written off at January 1, 2011 to reflect its implied fair value, resulting in an impairment charge of \$20 million, which was included in earnings for the period. Please refer to the impairment discussion in Note 2.

The following table presents assets that were measured at fair value on the Consolidated Balance Sheet on a nonrecurring basis as of January 1, 2011:

| (millions) | Fair Value | Level 3 | Total Loss |
|-------------------|------------|---------|------------|
| Description: | | | |
| Long-lived assets | \$ 10 | \$ 10 | \$ (9) |
| Goodwill | | | (20) |
| Total | \$ 10 | \$ 10 | \$ (29) |

Financial instruments

The carrying values of the Company's short-term items, including cash, cash equivalents, accounts receivable, accounts payable and notes payable approximate fair value. The fair value of the Company's long-term debt is calculated based on broker quotes and was as follows at December 31, 2011:

| (millions) | Fair Value | Carrying Value |
|--------------------------------------|------------|----------------|
| Current maturities of long-term debt | \$ 778 | \$ 761 |
| Long-term debt | 5,893 | 5,037 |
| Total | \$ 6,671 | \$ 5,798 |

Counterparty credit risk concentration

The Company is exposed to credit loss in the event of nonperformance by counterparties on derivative financial and commodity contracts. Management believes a concentration of credit risk with respect to derivative counterparties is limited due to the credit ratings and use of master netting and reciprocal collateralization agreements with the counterparties and the use of exchange-traded commodity contracts.

Master netting agreements apply in situations where the Company executes multiple contracts with the same counterparty. There were no counterparties representing a concentration of credit risk to the Company at December 31, 2011.

For certain derivative contracts, reciprocal collateralization agreements with counterparties call for the posting of collateral in the form of cash, treasury securities or letters of credit if a fair value loss position to the Company or its counterparties exceeds a certain amount. As of December 31, 2011, the Company had posted collateral of \$2 million in the form of cash, which was reflected as an increase in accounts receivable, net on the Consolidated Balance Sheet.

Management believes concentrations of credit risk with respect to accounts receivable is limited due to the generally high credit quality of the Company's major customers, as well as the large number and geographic dispersion of smaller customers. However, the Company conducts a disproportionate amount of business with a small number of large multinational grocery retailers, with the five largest accounts encompassing approximately 31% of consolidated trade receivables at December 31, 2011.

Refer to Note 1 for disclosures regarding the Company's accounting policies for derivative instruments.

NOTE 13

PRODUCT RECALLS

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During 2010 and 2009, the Company recorded charges in connection with product recalls. The Company recorded estimated customer returns and consumer rebates as a reduction of net sales, costs associated with returned product and the disposal and write-off of inventory as COGS, and other recall costs as SGA expense.

On June 25, 2010, the Company announced a recall of select packages of Kellogg's cereal primarily in the U.S. due to an odor from waxy resins found in the package liner.

On January 16, 2009, the Company announced a recall of certain *Austin* and *Keebler* branded peanut butter sandwich crackers and certain *Famous Amos* and *Keebler* branded peanut butter cookies. The recall was expanded in February 2009 to include certain *Bear Naked*, *Kashi* and *Special K* products. The decision to recall the products was made following an investigation by the United States Food and Drug Administration concerning a salmonella outbreak thought to be caused by tainted peanut related products. The products subject to the recall contained peanut based ingredients manufactured by the Peanut Corporation of America whose Blakely, Georgia plant was found to contain salmonella. Charges associated with the recall were incurred during the Company's 2009 and 2008 fiscal years and reduced operating profit by a total of \$65 million.

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The following table presents a summary of recall related charges for the years ended January 1, 2011 and January 2, 2010:

| (millions, except per share amount) | 2010 | 2009 |
|--------------------------------------|-----------|-----------|
| Reduction of net sales | \$ 29 | \$ 12 |
| COGS | 16 | 18 |
| SGA expense | 1 | 1 |
| Total | \$ 46 | \$ 31 |
| Impact on earnings per diluted share | \$ (0.09) | \$ (0.06) |

In addition to charges recorded in connection with the recalls, the Company also lost sales of the impacted products that are not included in the table above.

NOTE 14

CONTINGENCIES

The Company is subject to various legal proceedings, claims, and governmental inspections or investigations in the ordinary course of business covering matters such as general commercial, governmental regulations, antitrust and trade regulations, product liability, environmental, intellectual property, workers' compensation, employment and other actions. These matters are subject to uncertainty and the outcome is not predictable with assurance. The Company uses a combination of insurance and self-insurance for a number of risks, including workers' compensation, general liability, automobile liability and product liability.

The Company has established accruals for certain matters where losses are deemed probable and reasonably estimable. There are other claims and legal proceedings pending against the Company for which accruals have not been established. It is reasonably possible that some of these matters could result in an unfavorable judgment against the Company and could require payment of claims in amounts that cannot be estimated at December 31, 2011. Based upon current information, management does not expect any of the claims or legal proceedings pending against the Company to have a material impact on the Company's consolidated financial statements.

NOTE 15

QUARTERLY FINANCIAL DATA (unaudited)

| (millions, except per share data) | Net sales | | Gross profit | |
|-----------------------------------|-----------|-----------|--------------|----------|
| | 2011 | 2010 | 2011 | 2010 |
| | First | \$ 3,485 | \$ 3,318 | \$ 1,421 |
| Second | 3,386 | 3,062 | 1,443 | 1,305 |
| Third | 3,312 | 3,157 | 1,350 | 1,369 |
| Fourth | 3,015 | 2,860 | 1,234 | 1,190 |
| | \$ 13,198 | \$ 12,397 | \$ 5,448 | \$ 5,289 |

| | Net income attributable to Kellogg Company | | Per share amounts | | | |
|--------|--|----------|-------------------|---------|---------|---------|
| | 2011 | 2010 | 2011 | | 2010 | |
| | | | Basic | Diluted | Basic | Diluted |
| First | \$ 366 | \$ 418 | \$ 1.00 | \$ 1.00 | \$ 1.10 | \$ 1.09 |
| Second | 343 | 302 | .94 | .94 | .80 | .79 |
| Third | 290 | 338 | .81 | .80 | .91 | .90 |
| Fourth | 232 | 189 | .65 | .64 | .51 | .51 |
| | \$ 1,231 | \$ 1,247 | | | | |

The principal market for trading Kellogg shares is the New York Stock Exchange (NYSE). At year-end 2011, the closing price (on the NYSE) was \$50.57 and there were 39,730 shareholders of record.

Dividends paid per share and the quarterly price ranges on the NYSE during the last two years were:

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| 2011 Quarter | Dividend | Stock price | |
|--------------|-----------|-------------|----------|
| | per share | High | Low |
| First | \$.4050 | \$ 55.41 | \$ 49.99 |
| Second | .4050 | 57.70 | 53.45 |
| Third | .4300 | 56.39 | 50.38 |
| Fourth | .4300 | 55.30 | 48.10 |
| | \$ 1.6700 | | |
| 2010 Quarter | | | |
| First | \$.3750 | \$ 55.45 | \$ 51.70 |
| Second | .3750 | 56.00 | 49.75 |
| Third | .4050 | 52.58 | 47.28 |
| Fourth | .4050 | 51.62 | 48.51 |
| | \$ 1.5600 | | |

NOTE 16

REPORTABLE SEGMENTS

Kellogg Company is the world's leading producer of cereal and a leading producer of snacks and frozen foods, including cookies, crackers, toaster pastries, cereal bars, fruit-flavored snacks, frozen waffles, and veggie foods. Kellogg products are manufactured and marketed globally. Principal markets for these products include the United States and United Kingdom.

Beginning in the fourth quarter of 2011, the Company now has the following reportable segments: U.S. Morning Foods and Kashi; U.S. Snacks; U.S. Specialty; North America Other; Europe; Latin America; and Asia Pacific. Segment results of prior periods were recast to conform to the current presentation. The Company currently manages its operations through nine operating segments that are based on product category or geographic location. These operating segments are evaluated for similarity with regards to economic characteristics, products, production processes, types or classes of customers, distribution methods and regulatory environments to determine if they can be aggregated into reportable segments. The reportable segments are discussed in greater detail below:

U.S. Morning Foods and Kashi aggregates the U.S. Morning Foods and U.S. Kashi operating segments. The U.S. Morning Foods operating segment includes cereal, toaster pastries, and health and wellness business generally marketed under the Kellogg's name. The U.S. Kashi operating segment represents Kashi branded cereal, cereal bars, crackers, cookies and Stretch Island fruit snacks.

U.S. Snacks represents the U.S. snacks business which includes products such as cookies, crackers, cereal bars and fruit-flavored snacks.

U.S. Specialty primarily represents the food service and Girl Scouts business. The food service business is mostly non-commercial, and services schools, hospitals and prisons.

North America Other represents the U.S. Frozen and Canada operating segments. As these operating segments are not considered economically similar enough to aggregate with other operating segments and are immaterial for separate disclosure, they have been grouped together as a single reportable segment.

The three remaining reportable segments are based on geographic location – Europe which consists principally of European countries; Latin America which is comprised of Central and South America and includes Mexico; and Asia Pacific which is comprised of South Africa, Australia and other Asian and Pacific markets.

The measurement of reportable segment results is based on segment operating profit which is generally consistent with the presentation of operating profit in the Consolidated Statement of Income. Intercompany transactions between operating segments were insignificant in all periods presented.

| (millions) | 2011 | 2010 | 2009 |
|--------------------------------------|-----------|-----------|-----------|
| Net sales | | | |
| U.S. Morning Foods & Kashi | \$ 3,635 | \$ 3,480 | \$ 3,587 |
| U.S. Snacks | 2,908 | 2,745 | 2,758 |
| U.S. Specialty | 955 | 916 | 913 |
| North America Other | 1,375 | 1,261 | 1,252 |
| Europe | 2,334 | 2,230 | 2,361 |
| Latin America | 1,049 | 923 | 963 |
| Asia Pacific | 942 | 842 | 741 |
| Consolidated | \$ 13,198 | \$ 12,397 | \$ 12,575 |
| Operating profit | | | |
| U.S. Morning Foods & Kashi | \$ 648 | \$ 630 | \$ 728 |
| U.S. Snacks | 431 | 475 | 436 |
| U.S. Specialty | 216 | 240 | 190 |
| North America Other | 258 | 220 | 228 |
| Europe | 338 | 364 | 348 |
| Latin America | 176 | 153 | 179 |
| Asia Pacific | 106 | 74 | 86 |
| Total Reportable Segments | 2,173 | 2,156 | 2,195 |
| Corporate (a) | (197) | (166) | (194) |
| Consolidated | \$ 1,976 | \$ 1,990 | \$ 2,001 |
| Depreciation and amortization | | | |

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| | | | |
|----------------------------|--------|--------|--------|
| U.S. Morning Foods & Kashi | \$ 131 | \$ 125 | \$ 132 |
| U.S. Snacks | 91 | 96 | 94 |
| U.S. Specialty | 5 | 5 | 4 |
| North America Other | 30 | 31 | 26 |
| Europe | 57 | 53 | 60 |
| Latin America | 20 | 17 | 28 |
| Asia Pacific | 27 | 53 | 22 |
| Total Reportable Segments | 361 | 380 | 366 |
| Corporate | 8 | 12 | 18 |
| Consolidated | \$ 369 | \$ 392 | \$ 384 |

(a) Research and Development expense totaling \$11 million for 2010 and \$13 million for 2009 was reallocated to Corporate from the North America businesses. Certain items such as interest expense and income taxes, while not included in the measure of reportable segment operating results, are regularly reviewed by Management for our internationally-based reportable segments as shown below.

| (millions) | 2011 | 2010 | 2009 |
|---------------------------|--------|--------|--------|
| Interest expense | | | |
| Europe | \$ 4 | \$ 1 | \$ 1 |
| Latin America | 6 | | |
| Asia Pacific | 2 | 1 | |
| Corporate | 221 | 246 | 294 |
| Consolidated | \$ 233 | \$ 248 | \$ 295 |
| Income taxes | | | |
| Europe | \$ 40 | \$ 23 | \$ 22 |
| Latin America | 49 | 29 | 32 |
| Asia Pacific | 21 | 19 | 16 |
| Corporate & North America | 393 | 431 | 406 |
| Consolidated | \$ 503 | \$ 502 | \$ 476 |

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Management reviews balance sheet information, including total assets, based on geography. For all North American-based operating segments, balance sheet information is reviewed by Management in total and not on an individual operating segment basis.

| (millions) | 2011 | 2010 | 2009 |
|---------------------------------------|-----------|-----------|-----------|
| Total assets | | | |
| North America | \$ 9,128 | \$ 8,623 | \$ 8,465 |
| Europe | 1,584 | 1,700 | 1,630 |
| Latin America | 798 | 784 | 585 |
| Asia Pacific | 529 | 596 | 535 |
| Corporate | 2,275 | 3,006 | 3,354 |
| Elimination entries | (2,413) | (2,862) | (3,369) |
| Consolidated | \$ 11,901 | \$ 11,847 | \$ 11,200 |
| Additions to long-lived assets | | | |
| North America | \$ 421 | \$ 327 | \$ 236 |
| Europe | 61 | 57 | 50 |
| Latin America | 53 | 43 | 58 |
| Asia Pacific | 54 | 45 | 30 |
| Corporate | 5 | 2 | 3 |
| Consolidated | \$ 594 | \$ 474 | \$ 377 |

The Company's largest customer, Wal-Mart Stores, Inc. and its affiliates, accounted for approximately 20% of consolidated net sales during 2011, 21% in 2010, and 21% in 2009, comprised principally of sales within the United States.

Supplemental geographic information is provided below for net sales to external customers and long-lived assets:

| (millions) | 2011 | 2010 | 2009 |
|--------------------------|-----------|-----------|-----------|
| Net sales | | | |
| United States | \$ 8,239 | \$ 7,786 | \$ 7,946 |
| All other countries | 4,959 | 4,611 | 4,629 |
| Consolidated | \$ 13,198 | \$ 12,397 | \$ 12,575 |
| Long-lived assets | | | |
| United States | \$ 2,151 | \$ 1,993 | \$ 1,916 |
| All other countries | 1,130 | 1,135 | 1,094 |
| Consolidated | \$ 3,281 | \$ 3,128 | \$ 3,010 |

Supplemental product information is provided below for net sales to external customers:

| (millions) | 2011 | 2010 | 2009 |
|-------------------------------|-----------|-----------|-----------|
| Retail channel cereal | \$ 6,725 | \$ 6,256 | \$ 6,406 |
| Retail channel snacks | 4,940 | 4,734 | 4,751 |
| Frozen and specialty channels | 1,533 | 1,407 | 1,418 |
| Consolidated | \$ 13,198 | \$ 12,397 | \$ 12,575 |

NOTE 17

SUPPLEMENTAL FINANCIAL STATEMENT DATA

Consolidated Statement of Income

| (millions) | 2011 | 2010 | 2009 |
|----------------------------------|----------|----------|----------|
| Research and development expense | \$ 192 | \$ 187 | \$ 181 |
| Advertising expense | \$ 1,138 | \$ 1,130 | \$ 1,091 |

Consolidated Balance Sheet

2011 2010

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| | | |
|---|-----------------|-----------------|
| (millions) | | |
| Trade receivables | \$ 991 | \$ 893 |
| Allowance for doubtful accounts | (8) | (10) |
| Refundable income taxes | 73 | 189 |
| Other receivables | 132 | 118 |
| Accounts receivable, net | \$ 1,188 | \$ 1,190 |
| Raw materials and supplies | \$ 247 | \$ 224 |
| Finished goods and materials in process | 885 | 832 |
| Inventories | \$ 1,132 | \$ 1,056 |
| Deferred income taxes | \$ 149 | \$ 110 |
| Other prepaid assets | 98 | 115 |
| Other current assets | \$ 247 | \$ 225 |
| Land | \$ 104 | \$ 107 |
| Buildings | 1,896 | 1,842 |
| Machinery and equipment | 5,444 | 5,319 |
| Capitalized software | 184 | 143 |
| Construction in progress | 500 | 407 |
| Accumulated depreciation | (4,847) | (4,690) |
| Property, net | \$ 3,281 | \$ 3,128 |
| Other intangibles | \$ 1,503 | \$ 1,503 |
| Accumulated amortization | (49) | (47) |
| Other intangibles, net | \$ 1,454 | \$ 1,456 |
| Pension | \$ 150 | \$ 333 |
| Other | 366 | 387 |
| Other assets | \$ 516 | \$ 720 |
| Accrued income taxes | \$ 66 | \$ 60 |
| Accrued salaries and wages | 242 | 153 |
| Accrued advertising and promotion | 410 | 405 |
| Other | 411 | 421 |
| Other current liabilities | \$ 1,129 | \$ 1,039 |
| Nonpension postretirement benefits | \$ 188 | \$ 214 |
| Other | 404 | 425 |
| Other liabilities | \$ 592 | \$ 639 |

Allowance for doubtful accounts

| | | | |
|--------------------------------------|-------|-------|-------|
| (millions) | 2011 | 2010 | 2009 |
| Balance at beginning of year | \$ 10 | \$ 9 | \$ 10 |
| Additions charged to expense | | 2 | 3 |
| Doubtful accounts charged to reserve | (2) | (1) | (4) |
| Balance at end of year | \$ 8 | \$ 10 | \$ 9 |

NOTE 18

SUBSEQUENT EVENT

On February 15, 2012, the Company announced that it had entered into an agreement to acquire Procter & Gamble's Pringle® business for approximately \$2.7 billion, which is expected to be funded by international cash and the issuance of approximately \$2.0 billion of short and long term debt. The transaction is subject to customary conditions, including receipt of required regulatory approvals. The transaction is expected to close in the Summer of 2012.

Management's Responsibility for Financial Statements

Management is responsible for the preparation of the Company's consolidated financial statements and related notes. We believe that the consolidated financial statements present the Company's financial position and results of operations in conformity with accounting principles that are generally accepted in the United States, using our best estimates and judgments as required.

The independent registered public accounting firm audits the Company's consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board and provides an objective, independent review of the fairness of reported operating results and financial position.

The board of directors of the Company has an Audit Committee composed of four non-management Directors. The Committee meets regularly with management, internal auditors, and the independent registered public accounting firm to review accounting, internal control, auditing and financial reporting matters.

Formal policies and procedures, including an active Ethics and Business Conduct program, support the internal controls and are designed to ensure employees adhere to the highest standards of personal and professional integrity. We have a rigorous internal audit program that independently evaluates the adequacy and effectiveness of these internal controls.

Management's Report on Internal Control over Financial Reporting

Management is responsible for designing, maintaining and evaluating adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

We conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

Based on our evaluation under the framework in Internal Control Integrated Framework, management concluded that our internal control over financial reporting was effective as of December 31, 2011. The effectiveness of our internal control over financial reporting as of December 31, 2011 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which follows.

John A. Bryant
President and Chief Executive Officer

Ronald L. Dissinger
Senior Vice President and Chief Financial Officer

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of Kellogg Company

In our opinion, the consolidated financial statements listed in the index appearing under Item 15(a)(1) present fairly, in all material respects, the financial position of Kellogg Company and its subsidiaries at December 31, 2011 and January 1, 2011, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2011 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Battle Creek, Michigan
February 28, 2012

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

(a) We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer as appropriate, to allow timely decisions regarding required disclosure under Rules 13a-15(e) and 15d-15(e). Disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable, rather than absolute, assurance of achieving the desired control objectives.

As of December 31, 2011, management carried out an evaluation under the supervision and with the participation of our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

(b) Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, we have included a report of management's assessment of the design and effectiveness of our internal control over financial reporting as part of this Annual Report on Form 10-K. The independent registered public accounting firm of PricewaterhouseCoopers LLP also attested to, and reported on, the effectiveness of our internal control over financial reporting. Management's report and the independent registered public accounting firm's attestation report are included in our 2011 financial statements in Item 8 of this Report under the captions entitled "Management's Report on Internal Control over Financial Reporting" and "Report of Independent Registered Public Accounting Firm" and are incorporated herein by reference.

(c) During the last fiscal quarter, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

Not applicable.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Directors Refer to the information in our Proxy Statement to be filed with the Securities and Exchange Commission for the Annual Meeting of Shareowners to be held on April 20, 2012 (the "Proxy Statement"), under the caption "Proposal 1 Election of Directors," which information is incorporated herein by reference.

Identification and Members of Audit Committee; Audit Committee Financial Expert Refer to the information in the Proxy Statement under the caption "Board and Committee Membership," which information is incorporated herein by reference.

Executive Officers of the Registrant Refer to "Executive Officers" under Item 1 of this Report.

For information concerning Section 16(a) of the Securities Exchange Act of 1934 Refer to the information under the caption "Security Ownership - Section 16(a) Beneficial Ownership Reporting Compliance" of the Proxy Statement, which information is incorporated herein by reference.

Code of Ethics for Chief Executive Officer, Chief Financial Officer and Controller We have adopted a Global Code of Ethics which applies to our chief executive officer, chief financial officer, corporate controller and all our other employees, and which can be found at

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www.kelloggcompany.com. Any amendments or waivers to the Global Code of Ethics applicable to our chief executive officer, chief financial officer or corporate controller may also be found at www.kelloggcompany.com.

ITEM 11. EXECUTIVE COMPENSATION

Refer to the information under the captions 2011 Director Compensation and Benefits, Compensation Discussion and Analysis, Executive Compensation, Retirement and Non-Qualified Defined Contribution and Deferred Compensation Plans, Employment Agreements, and Potential Post-Employment Payments of the Proxy Statement, which is incorporated herein by reference. See also the information under the caption

Compensation Committee Report of the Proxy Statement, which information is incorporated herein by reference; however, such information is only furnished hereunder and not deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Refer to the information under the captions Security Ownership Five Percent Holders and Security Ownership Officer and Director Stock Ownership of the Proxy Statement, which information is incorporated herein by reference.

Securities Authorized for Issuance Under Equity Compensation Plans

(millions, except per share data)

| Plan category | Number of securities to be issued upon exercise of outstanding options, warrants and rights as of December 31, 2011 (a) | Weighted-average exercise price of outstanding options, warrants and rights as of December 31, 2011 (b) | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a) as of December 31, 2011 (c) |
|--|--|--|--|
| Equity compensation plans approved by security holders | 23.7 | \$ 48 | 17.6 |
| Equity compensation plans not approved by security holders | | NA | 0.1 |
| Total | 23.7 | \$ 48 | 17.7 |

Three plans are considered Equity compensation plans not approved by security holders. The Kellogg Share Incentive Plan, which was adopted in 2002 and is available to most U.K. employees of specified Kellogg Company subsidiaries; a similar plan, which is available to employees in the Republic of Ireland; and the Deferred Compensation Plan for Non-Employee Directors, which was adopted in 1986 and amended in 1993 and 2002.

Under the Kellogg Share Incentive Plan, eligible U.K. employees may contribute up to 1,500 Pounds Sterling annually to the plan through payroll deductions. The trustees of the plan use those contributions to buy shares of our common stock at fair market value on the open market, with Kellogg matching those contributions on a 1:1 basis. Shares must be withdrawn from the plan when employees cease employment. Under current law, eligible employees generally receive certain income and other tax benefits if those shares are held in the plan for a specified number of years. A similar plan is also available to employees in the Republic of Ireland. As these plans are open market plans with no set overall maximum, no amounts for these plans are included in the above table. However, approximately 68,000 shares were purchased by eligible employees under the Kellogg Share Incentive Plan, the plan for the Republic of Ireland and other similar predecessor plans during 2011, with approximately an additional 68,000 shares being provided as matched shares.

Under the Deferred Compensation Plan for Non-Employee Directors, non-employee Directors may elect to defer all or part of their compensation (other than expense reimbursement) into units which are credited to their accounts. The units have a value equal to the fair market value of a share of our common stock on the appropriate date, with dividend equivalents being earned on the whole units in non-employee Directors' accounts. Units may be paid in either cash or shares of our common stock, either in a lump sum or in up to ten annual installments, with the payments to begin as soon as practicable after the non-employee Director's service as a Director terminates. No more than 150,000 shares are authorized for use under this plan, of which approximately 11,000 had been issued as of December 31, 2011. Because Directors may elect, and are likely to elect, a distribution of cash rather than shares, the contingently issuable shares are not included in column (a) of the table above.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Refer to the information under the captions Corporate Governance Director Independence and Related Person Transactions of the Proxy Statement, which information is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Refer to the information under the captions Proposal 3 Ratification of PricewaterhouseCoopers LLP Fees Paid to Independent Registered Public Accounting Firm and Proposal 3 Ratification of PricewaterhouseCoopers LLP Preapproval Policies and Procedures of the Proxy Statement, which information is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

The Consolidated Financial Statements and related Notes, together with Management's Report on Internal Control over Financial Reporting, and the Report thereon of PricewaterhouseCoopers LLP dated February 28, 2012, are included herein in Part II, Item 8.

(a) 1. Consolidated Financial Statements

Consolidated Statement of Income for the years ended December 31, 2011, January 1, 2011 and January 2, 2010.

Consolidated Balance Sheet at December 31, 2011 and January 1, 2011.

Consolidated Statement of Equity for the years ended December 31, 2011, January 1, 2011 and January 2, 2010.

Consolidated Statement of Cash Flows for the years ended December 31, 2011, January 1, 2011 and January 2, 2010.

Notes to Consolidated Financial Statements.

Management's Report on Internal Control over Financial Reporting.

Report of Independent Registered Public Accounting Firm.

(a) 2. Consolidated Financial Statement Schedule

All financial statement schedules are omitted because they are not applicable or the required information is shown in the financial statements or the notes thereto.

(a) 3. Exhibits required to be filed by Item 601 of Regulation S-K

The information called for by this Item is incorporated herein by reference from the Exhibit Index included in this Report.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, this 28th day of February, 2012.

KELLOGG COMPANY

By: /s/ John A. Bryant
John A. Bryant
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

| Name | Capacity | Date |
|--|---|-------------------|
| /s/ JOHN A. BRYANT John A. Bryant | President and Chief Executive Officer and Director (Principal Executive Officer) | February 28, 2012 |
| /s/ RONALD L. DISSINGER Ronald L. Dissinger | Senior Vice President and Chief Financial Officer (Principal Financial Officer) | February 28, 2012 |
| /s/ ALAN R. ANDREWS Alan R. Andrews | Vice President and Corporate Controller (Principal Accounting Officer) | February 28, 2012 |
| * James M. Jenness | Chairman of the Board and Director | February 28, 2012 |
| * Benjamin S. Carson Sr. | Director | February 28, 2012 |
| * John T. Dillon | Director | February 28, 2012 |
| * Gordon Gund | Director | February 28, 2012 |
| * Dorothy A. Johnson | Director | February 28, 2012 |
| * Donald R. Knauss | Director | February 28, 2012 |

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| | | | |
|--------------------------|---------------------|------------------|-------------------|
| | * | Director | February 28, 2012 |
| Ann McLaughlin Korologos | | | |
| | * | Director | February 28, 2012 |
| Rogelio M. Rebolledo | | | |
| | * | Director | February 28, 2012 |
| Sterling K. Speirn | | | |
| | * | Director | February 28, 2012 |
| John L. Zabriskie | | | |
| * By: | /s/ GARY H. PILNICK | Attorney-in-Fact | February 28, 2012 |
| | Gary H. Pilnick | | |

EXHIBIT INDEX

| Exhibit No. | Description | Electronic(E), Paper(P) or Incorp. By Ref.(IBRF) |
|-------------|--|--|
| 2.01 | Transaction Agreement between us and The Procter & Gamble Company, incorporated by reference to Exhibit 2.1 of our Current Report on Form 8-K dated February 17, 2012, Commission file number 1-4171. | IBRF |
| 3.01 | Amended Restated Certificate of Incorporation of Kellogg Company, incorporated by reference to Exhibit 4.1 to our Registration Statement on Form S-8, file number 333-56536. | IBRF |
| 3.02 | Bylaws of Kellogg Company, as amended, incorporated by reference to Exhibit 3.1 to our Current Report on Form 8-K dated April 24, 2009, Commission file number 1-4171. | IBRF |
| 4.01 | Indenture dated August 1, 1993, between us and Harris Trust and Savings Bank, incorporated by reference to Exhibit 4.1 to our Registration Statement on Form S-3, Commission file number 33-49875 | IBRF |
| 4.02 | Indenture and Supplemental Indenture dated March 15 and March 29, 2001, respectively, between Kellogg Company and BNY Midwest Trust Company, including the form of 7.45% Debentures due 2031, incorporated by reference to Exhibit 4.01 and 4.02 to our Quarterly Report on Form 10-Q for the quarter ending March 31, 2001, Commission file number 1-4171. | IBRF |
| 4.03 | Form of Indenture between Kellogg Company and The Bank of New York Mellon Trust Company, N.A., incorporated by reference to Exhibit 4.1 to our Registration Statement on Form S-3, Commission file number 333-159303. | IBRF |
| 4.04 | Officers Certificate of Kellogg Company (with form of Kellogg Company 4.450% Senior Note Due May 30, 2016), incorporated by reference to Exhibit 4.2 to our Current Report on Form 8-K dated May 18, 2009, Commission file number 1-4171. | IBRF |
| 4.05 | Officers Certificate of Kellogg Company (with form of Kellogg Company 4.150% Senior Note Due 2019), incorporated by reference to Exhibit 4.2 to our Current Report on Form 8-K dated November 16, 2009, Commission file number 1-4171. | IBRF |
| 4.06 | Officers Certificate of Kellogg Company (with form of Kellogg Company 4.000% Senior Note Due 2020), incorporated by reference to Exhibit 4.1 to our Current Report on Form 8-K dated December 8, 2010, Commission file number 1-4171. | IBRF |
| 4.07 | Four-Year Credit Agreement dated as of March 4, 2011 with 32 lenders, JPMorgan Chase Bank, N.A., as Administrative Agent, Barclays Capital, as Syndication Agent, BNP Paribas, Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A., Rabobank Nederland, New York Branch and Wells Fargo Bank, N.A., as Documentation Agents, J.P. Morgan Securities LLC, Barclays Capital, BNP Paribas Securities Corp., Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A., Rabobank Nederland, New York Branch and Wells Fargo Securities, LLC, as Joint Lead Arrangers and Joint Bookrunners, incorporated by reference to Exhibit 4.1 to our Current Report on Form 8-K dated March 10, 2011, Commission file number 1-04171. | IBRF |
| 4.08 | Officers Certificate of Kellogg Company (with form of Kellogg Company 3.25% Senior Note Due 2018), incorporated by reference to Exhibit 4.1 to our Current Report on Form 8-K dated May 15, 2011, Commission file number 1-4171. | IBRF |
| 4.09 | Officers Certificate of Kellogg Company (with form of Kellogg Company 1.875% Senior Note Due 2016), incorporated by reference to Exhibit 4.1 to our Current Report on Form 8-K dated November 17, 2011, Commission file number 1-4171. | IBRF |
| 10.01 | Kellogg Company Excess Benefit Retirement Plan, incorporated by reference to Exhibit 10.01 to our Annual Report on Form 10-K for the fiscal year ended December 31, 1983, Commission file number 1-4171.* | IBRF |
| 10.02 | Kellogg Company Supplemental Retirement Plan, incorporated by reference to Exhibit 10.05 to our Annual Report on Form 10-K for the fiscal year ended December 31, 1990, Commission file number 1-4171.* | IBRF |
| 10.03 | Kellogg Company Supplemental Savings and Investment Plan, as amended and restated as of January 1, 2003, incorporated by reference to Exhibit 10.03 to our Annual Report on Form 10-K for the fiscal year ended December 28, 2002, Commission file number 1-4171.* | IBRF |

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| Exhibit No. | Description | Electronic(E), Paper(P) or Incorp. By Ref.(IBRF) |
|-------------|--|--|
| 10.04 | Kellogg Company International Retirement Plan, incorporated by reference to Exhibit 10.05 to our Annual Report on Form 10-K for the fiscal year ended December 31, 1997, Commission file number 1-4171.* | IBRF |
| 10.05 | Kellogg Company Executive Survivor Income Plan, incorporated by reference to Exhibit 10.06 to our Annual Report on Form 10-K for the fiscal year ended December 31, 1985, Commission file number 1-4171.* | IBRF |
| 10.06 | Kellogg Company Key Executive Benefits Plan, incorporated by reference to Exhibit 10.09 to our Annual Report on Form 10-K for the fiscal year ended December 31, 1991, Commission file number 1-4171.* | IBRF |
| 10.07 | Kellogg Company Key Employee Long Term Incentive Plan, incorporated by reference to Exhibit 10.6 to our Annual Report on Form 10-K for the fiscal year ended December 29, 2007, Commission file number 1-4171.* | IBRF |
| 10.08 | Amended and Restated Deferred Compensation Plan for Non-Employee Directors, incorporated by reference to Exhibit 10.1 to our Quarterly Report on Form 10-Q for the fiscal quarter ended March 29, 2003, Commission file number 1-4171.* | IBRF |
| 10.09 | Kellogg Company Senior Executive Officer Performance Bonus Plan, incorporated by reference to Exhibit 10.10 to our Annual Report on Form 10-K for the fiscal year ended December 31, 1995, Commission file number 1-4171.* | IBRF |
| 10.10 | Kellogg Company 2000 Non-Employee Director Stock Plan, incorporated by reference to Exhibit 10.10 to our Annual Report on Form 10-K for the fiscal year ended December 29, 2007, Commission file number 1-4171.* | IBRF |
| 10.11 | Kellogg Company 2001 Long-Term Incentive Plan, as amended and restated as of February 20, 2003, incorporated by reference to Exhibit 10.11 to our Annual Report on Form 10-K for the fiscal year ended December 28, 2002.* | IBRF |
| 10.12 | Kellogg Company Bonus Replacement Stock Option Plan, incorporated by reference to Exhibit 10.12 to our Annual Report on Form 10-K for the fiscal year ended December 31, 1997, Commission file number 1-4171.* | IBRF |
| 10.13 | Kellogg Company Executive Compensation Deferral Plan incorporated by reference to Exhibit 10.13 to our Annual Report on Form 10-K for the fiscal year ended December 31, 1997, Commission file number 1-4171.* | IBRF |
| 10.14 | Employment Letter between us and James M. Jenness, incorporated by reference to Exhibit 10.18 to our Annual Report in Form 10-K for the fiscal year ended January 1, 2005, Commission file number 1-4171.* | IBRF |
| 10.15 | Agreement between us and other executives, incorporated by reference to Exhibit 10.05 of our Quarterly Report on Form 10-Q for the quarter ended June 30, 2000, Commission file number 1-4171.* | IBRF |
| 10.16 | Stock Option Agreement between us and James Jenness, incorporated by reference to Exhibit 4.4 to our Registration Statement on Form S-8, file number 333-56536.* | IBRF |
| 10.17 | Kellogg Company 2002 Employee Stock Purchase Plan, as amended and restated as of January 1, 2008, incorporated by reference to Exhibit 10.22 to our Annual Report on Form 10-K for the fiscal year ended December 29, 2007, Commission file number 1-4171.* | IBRF |
| 10.18 | Kellogg Company 1993 Employee Stock Ownership Plan, incorporated by reference to Exhibit 10.23 to our Annual Report on Form 10-K for the fiscal year ended December 29, 2007, Commission file number 1-4171.* | IBRF |
| 10.19 | Kellogg Company 2003 Long-Term Incentive Plan, as amended and restated as of December 8, 2006, incorporated by reference to Exhibit 10. to our Annual Report on Form 10-K for the fiscal year ended December 30, 2006, Commission file number 1-4171.* | IBRF |
| 10.20 | Kellogg Company Severance Plan, incorporated by reference to Exhibit 10. of our Annual Report on Form 10-K for the fiscal year ended December 28, 2002, Commission file number 1-4171.* | IBRF |
| 10.21 | Form of Non-Qualified Option Agreement for Senior Executives under 2003 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.4 to our Quarterly Report on Form 10-Q for the fiscal period ended September 25, 2004, Commission file number 1-4171.* | IBRF |

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| Exhibit No. | Description | Electronic(E), Paper(P) or Incorp. By Ref.(IBRF) |
|-------------|--|--|
| 10.22 | Form of Restricted Stock Grant Award under 2003 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.5 to our Quarterly Report on Form 10-Q for the fiscal period ended September 25, 2004, Commission file number 1-4171.* | IBRF |
| 10.23 | Form of Non-Qualified Option Agreement for Non-Employee Director under 2000 Non-Employee Director Stock Plan, incorporated by reference to Exhibit 10.6 to our Quarterly Report on Form 10-Q for the fiscal period ended September 25, 2004, Commission file number 1-4171.* | IBRF |
| 10.24 | First Amendment to the Key Executive Benefits Plan, incorporated by reference to Exhibit 10.39 of our Annual Report in Form 10-K for our fiscal year ended January 1, 2005, Commission file number 1-4171.* | IBRF |
| 10.25 | Restricted Stock Grant/Non-Compete Agreement between us and John Bryant, incorporated by reference to Exhibit 10.1 of our Quarterly Report on Form 10-Q for the period ended April 2, 2005, Commission file number 1-4171 (the 2005 Q1 Form 10-Q).* | IBRF |
| 10.26 | Restricted Stock Grant/Non-Compete Agreement between us and Jeff Montie, incorporated by reference to Exhibit 10.2 of the 2005 Q1 Form 10-Q.* | IBRF |
| 10.27 | Executive Survivor Income Plan, incorporated by reference to Exhibit 10.42 of our Annual Report in Form 10-K for our fiscal year ended December 31, 2005, Commission file number 1-4171.* | IBRF |
| 10.28 | Agreement between us and James M. Jenness, incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated October 20, 2006, Commission file number 1-4171.* | IBRF |
| 10.29 | Letter Agreement between us and John A. Bryant, dated July 23, 2007, incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated July 23, 2007, Commission file number 1-4171.* | IBRF |
| 10.30 | Agreement between us and James M. Jenness, dated February 22, 2008, incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K dated February 22, 2008, Commission file number 1-4171.* | IBRF |
| 10.31 | Form of Amendment to Form of Agreement between us and certain executives, incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K dated December 18, 2008, Commission file number 1-4171.* | IBRF |
| 10.32 | Amendment to Letter Agreement between us and John A. Bryant, dated December 18, 2008, incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated December 18, 2008, Commission file number 1-4171.* | IBRF |
| 10.33 | Form of Restricted Stock Grant Award under 2003 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated December 18, 2008, Commission file number 1-4171.* | IBRF |
| 10.34 | 2009-2011 Executive Performance Plan, incorporated by reference to Exhibit 10.1 of our Current Report on Form 8-K dated February 20, 2009, Commission file number 1-4171.* | IBRF |
| 10.35 | Form of Option Terms and Conditions for SVP Executive Officers under 2003 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated February 20, 2009, Commission file number 1-4171.* | IBRF |
| 10.36 | Kellogg Company 2009 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.1 to our Registration Statement on Form S-8 dated April 27, 2009, Commission file number 333-158824.* | IBRF |
| 10.37 | Kellogg Company 2009 Non-Employee Director Stock Plan, incorporated by reference to Exhibit 10.1 to our Registration Statement on Form S-8 dated April 27, 2009, Commission file number 333-158825.* | IBRF |
| 10.38 | 2010-2012 Executive Performance Plan, incorporated by reference to Exhibit 10.1 of our Current Report on Form 8-K dated February 23, 2010, Commission file number 1-4171.* | IBRF |
| 10.39 | 2011-2013 Executive Performance Plan, incorporated by reference to Exhibit 10.1 of our Current Report on Form 8-K dated February 25, 2011, Commission file number 1-4171.* | IBRF |
| 10.40 | Form of Option Terms and Conditions under 2009 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated February 25, 2011, Commission file number 1-4171. | IBRF |

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| Exhibit No. | Description | Electronic(E), Paper(P) or Incorp. By Ref.(IBRF) |
|-------------|---|--|
| 10.41 | Letter Agreement between us and Gary Pilnick, dated May 20, 2008, incorporated by reference to Exhibit 10.54 to our Annual Report on Form 10-K for the fiscal year ended January 1, 2011, commission file number 1-4171.* | IBRF |
| 10.42 | Kellogg Company Senior Executive Annual Incentive Plan, incorporated by reference to Appendix A of our Board of Directors proxy statement for the annual meeting of shareholders held on April 29, 2011.* | IBRF |
| 10.43 | 2012-2014 Executive Performance Plan, incorporated by reference to Exhibit 10.1 of our Current Report on Form 8-K dated February 23, 2012, Commission file number 1-4171.* | IBRF |
| 10.44 | Form of Option Terms and Conditions under 2009 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated February 23, 2012, Commission file number 1-4171.* | IBRF |
| 10.45 | Form of Restricted Stock Terms and Conditions under 2009 Long-Term Incentive Plan. | E |
| 21.01 | Domestic and Foreign Subsidiaries of Kellogg. | E |
| 23.01 | Consent of Independent Registered Public Accounting Firm. | E |
| 24.01 | Powers of Attorney authorizing Gary H. Pilnick to execute our Annual Report on Form 10-K for the fiscal year ended December 31, 2011, on behalf of the Board of Directors, and each of them. | E |
| 31.1 | Rule 13a-14(a)/15d-14(a) Certification by John A. Bryant. | E |
| 31.2 | Rule 13a-14(a)/15d-14(a) Certification by Ronald L. Dissinger. | E |
| 32.1 | Section 1350 Certification by John A. Bryant. | E |
| 32.2 | Section 1350 Certification by Ronald L. Dissinger. | E |
| 101.INS | XBRL Instance Document | E |
| 101.SCH | XBRL Taxonomy Extension Schema Document | E |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document | E |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document | E |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document | E |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document | E |

* A management contract or compensatory plan required to be filed with this Report.

We agree to furnish to the Securities and Exchange Commission, upon its request, a copy of any instrument defining the rights of holders of long-term debt of Kellogg and our subsidiaries and any of our unconsolidated subsidiaries for which Financial Statements are required to be filed.

We will furnish any of our shareowners a copy of any of the above Exhibits not included herein upon the written request of such shareowner and the payment to Kellogg of the reasonable expenses incurred in furnishing such copy or copies.