GRANDMET FOODS (UK) LIMITED

FINANCIAL STATEMENTS

PERIOD ENDED 30 JUNE 1998

Registered in England No. 472217

DIRECTORS' REPORT

The directors have pleasure in submitting their annual report, together with the audited financial statements for the nine months ended 30 June 1998.

On 17 December 1997 Grand Metropolitan PLC ("GrandMet") merged with Guinness PLC to form Diageo plc which as a result became the ultimate parent undertaking of the company.

Activities

The company's principal activity is as the parent holding company of the majority of the companies comprising Diageo plc's food sector in the United Kingdom.

In the financial year to 30 September 1997, the assets and trade of the Brossard business were disposed of to a non-group company.

Year 2000

The Diageo Group has recognised that Year 2000 is a major issue and has established a Year 2000 team, which has made good progress in establishing an effective post-integration framework for its Year 2000 programme, having completed their impact assessment and project plans. Based on the work detailed above, the company believes that once the testing and conversion of computer systems is complete, internal systems and equipment will not give rise to significant operational problems as a result of the Year 2000 issue.

The Diageo Group is also working with key business suppliers, joint distribution arrangement partners and customers to prepare for the Year 2000 and is establishing contingency plans for Year 2000 failures by such business partners. Contingency plans are also being prepared for unexpected Year 2000 failures that may affect business critical systems and equipment.

The general expectation by those who have studied best practice in managing the Year 2000 problem is that even the best run projects will face some Year 2000 compliance failures. There can be no assurance that Year 2000 projects will be successful or that the date change from 1999 to 2000 will not adversely affect the company's operations and financial results. The Diageo Group may also be adversely affected by the inability of third parties to manage the Year 2000 problem.

DIRECTORS' REPORT (continued)

The euro

In accordance with the Treaty on European Union, signed at Maastricht on 7 February 1992, the third stage of Economic and Monetary Union (EMU) commenced on 1 January 1999. At that time, a single currency, the 'euro', was introduced. The Diageo Group's euro-readiness is being managed as a discrete business project, the Group has systems and procedures in place which will enable it to conduct euro transactions appropriate to local market requirements.

The Diageo Group is also working actively with key business suppliers, joint distribution arrangement partners and customers in respect of EMU. In addition, monetary union may have a significant impact on macroeconomic factors, including interest and foreign exchange.

Looking forward, key commercial risks, such as pricing transparency, have been analysed, with a view to minimising the impact through active management in these areas over the EMU transition period and beyond. However, there can be no assurance that the euro will not have a negative impact. The impact of future entry to EMU of other European countries (particularly the UK) has been similarly analysed.

Financial

The financial year end of the company has been changed to 30 June from 30 September, and the results for the period shown on page 10 are for the nine months from 1 October 1997 to 30 June 1998.

The profit on ordinary activities after taxation was £1,204,000 (1997 - loss of £5,909,000). After deducting the dividend of £1,932,000 (1997 - £1,449,000) on the 5.75% fixed rate non-redeemable preference shares, a loss of £ 728,000 was transferred from reserves (1997 - loss of £7,358,000).

A summary of the company's investments is given in note 11 on page 15 of the financial statements.

DIRECTORS' REPORT (continued)

Directors

The directors who served during the period were as follows:

J M Summerlin
M R Jamieson

M R Jamieson resigned as director on the 24 July 1998. R J Gardner was appointed director on the same date.

Directors' interests

No directors had any interest, beneficial or non-beneficial, in the share capital of the company or had a material interest during the period in any significant contract with the company or any subsidiary.

On 2 February 1998 the company's ultimate parent company, Diageo plc, made a capital repayment to shareholders equivalent to 70 pence per Diageo plc ordinary share, which took the form of the issue of redeemable B shares of 514 $^{12}/_{17}$ pence and the consolidation of existing shares from 25 pence ordinary shares to 28 $^{101}/_{108}$ pence ordinary shares. For every 1,000 existing ordinary shares shareholders received 864 consolidated ordinary shares and 136 B shares.

The directors who held office at the end of the financial period had the following interests in the shares of Diageo plc, the ultimate holding company:

Shares and awards over ordinary shares

	Ordinary shares of 25p or 28 $^{101}/_{108}$p 1.10.97 or as at date of appointment	Ordinary Shares of 28 $^{101}/_{108}$p 30.6.98	B Shares 30.6.98	MTEP Awards* 30.6.98	RSP Awards* 30.6.98
MR Jamieson	-	-	-	-	4,630
JM Summerlin	634	2,500	-	-	4,820

Options

	1.10.97 or as at date of appointment	Granted during period	Exercised during period	30.6.98
MR Jamieson	45,000	-	-	45,000
JM Summerlin	95,493	-	10,500	84,993

DIRECTORS' REPORT (continued)

The directors held the above options under Grand Metropolitan PLC and Diageo plc share option schemes at prices between 313p and 459p per share exercisable by 2006.

The mid-market share price of Diageo plc shares fluctuated between 535p and 762.5p per share during the period. The mid-market share price on 30 June 1998 was 711p.

J M Summerlin had an interest in 10,878,743 shares subject to call options held by the Grand Metropolitan PLC No.1 Employee Share Trust to satisfy grants made under the various Grand Metropolitan PLC share option schemes existing prior to the merger.

* Notes

(i) The Guinness Medium Term Executive Plan (MTEP) was established in 1997. The plan was operated by the trustees of the Diageo plc Employee Incentive Trust 1997. Awards were made only to B grade executives and below world-wide. Performance conditions were tailored to the particular division within which the relevant executive works and could be adjusted when they moved within the Group. The plan was wound up in June 1998 with cash payments made to participants in September 1998 in lieu of shares. Proportionate payments were made based on the time elapsed since the plan was first established.

(ii) The Grand Metropolitan Restricted Share Plan (RSP). In 1997, GrandMet shares or ADSs were conditionally awarded to executives, with eventual release dependent on the performance of GrandMet's TSR compared with the TSR of the other FTSE 100 companies, over a minimum of three years. The allocation for UK directors was 100% of base salary, using the average share price for the calendar year prior to the date of the award. Following the merger, these awards have been converted to Diageo shares, and their release to participants will depend on the ranking of Diageo's TSR at the end of three years after the date of grant. If the company is ranked in the top 20% of selected companies, the maximum number of shares will be released; if it is ranked below the 50th percentile, no shares will be released. Releases between these points are on a sliding scale.

DIRECTORS' REPORT (continued)

Auditor

A resolution is to be proposed at the annual general meeting for the re-appointment of KPMG Audit Plc as auditor of the company.

By order of the board

R J Gardner
Secretary
Harman House
1 George Street,
Uxbridge
Middlesex, UB8 1QQ

12 April 1999

DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE PREPARATION OF FINANCIAL STATEMENTS

The following statement, which should be read in conjunction with the report of the auditor set out on page 7, is made with a view to distinguishing for shareholders the respective responsibilities of the directors and of the auditor in relation to the financial statements.

The directors are required by the Companies Act 1985 to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the company at the end of the financial period and of the profit or loss for the financial period.

The directors in preparing the financial statements on pages 8 to 17 consider that, the company has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, that all accounting standards which they consider to be applicable have been followed and that it is appropriate to use a going concern basis.

The directors have responsibility for ensuring that the company keeps accounting records which disclose with reasonable accuracy the financial position of the company and which enable them to ensure that the financial statements comply with the Companies Act 1985.

The directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

J M Summerlin
Director

12 April 1999

REPORT OF THE AUDITOR, KPMG AUDIT PLC
TO THE MEMBERS OF GRANDMET FOODS (UK) LIMITED

We have audited the financial statements on pages 8 to 17.

Respective responsibilities of directors and auditor

As described on page 6 the company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free of material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 30th June 1998 and of its loss for the nine month period then ended and have been properly prepared in a accordance with the Companies Act 1985.

KPMG Audit Plc

KPMG Audit Plc
Chartered Accountants
Registered Auditor
London

12 April 1999

ACCOUNTING POLICIES

Basis of preparation

The financial statements of the company are prepared under the historical cost convention and comply with applicable UK accounting standards. The bases used are consistent with those used in the previous period. The company has not presented group financial statements by virtue of section 228 of the Companies Act 1985.

The company is a wholly owned subsidiary of Diageo plc and is included in the consolidated financial statements of Diageo plc, which are publicly available. Consequently, the company has taken advantage of the exception from preparing a cash flow statement under the terms of Financial Reporting Standard No 1 (Revised 1996). The company is also exempt under the terms of Financial Reporting Standard No 8 from disclosing related party transactions (but not balances) with entities that are part of the Diageo plc group or investees of the Diageo plc group.

Turnover

Turnover excluded VAT but included subsidies receivable.

Fixed assets and depreciation

Fixed assets were stated at cost. Profit or loss on sale of assets is the difference between the disposal proceeds and the net book value.

No depreciation was provided on freehold land. Freehold buildings and long leaseholds were depreciated over 40 years. Other leaseholds were depreciated over the unexpired period of the lease. Plant and machinery was depreciated to residual values over its estimated useful lives within 2 to 20 years.

The company disposed of all of its fixed assets during the year ended 30 September 1997.

Leases

Operating lease payments were taken to the profit and loss account on a straight line basis over the life of the lease.

NOTES (continued)

Investments

Investments are valued individually at the lower of cost and net realisable value. All investments are unlisted and the net realisable value is estimated by the directors.

Deferred Taxation

The charge for taxation is based on the profit for the period and takes into account taxation deferred because of short term timing differences between the treatment of certain items for taxation and accounting purposes. Provision is made for deferred tax only to the extent that it is probable that an actual liability will crystallise.

Pensions and other post employment benefits

The majority of company employees were members of group pension schemes operated by Grand Metropolitan PLC. The schemes are of the defined benefit type funded by payments to trustee administered funds. The costs of providing pensions and other post employment benefits are charged against profits on a systematic basis, with pension surpluses and deficits allocated on a straight line basis over the expected remaining service lives of current employees.

Differences between the amounts charged in the profit and loss account and payments made to the plans were treated as assets or liabilities in the balance sheet. Particulars of the valuations of the group plans were contained in the financial statements of Grand Metropolitan PLC.

PROFIT AND LOSS ACCOUNT

For the 9 months ended 30 June 1998

	Notes	9 months ended 30 June 1998 £'000	12 months ended 30 Sept 1997 £'000
Turnover	1	-	14,905
Changes in stocks of finished goods and work in progress		-	283
Raw materials and consumables		-	(7,318)
Other operating costs	2	-	(3,095)
Staff costs	3	-	(4,554)
Operating profit		-	221
Loss on disposal of discontinued operations	5	(306)	(4,305)
Loss on ordinary activities before interest		(306)	(4,084)
Interest receivable and similar income	6	2,189	2,122
Interest payable and similar charges	7	-	(4,895)
Profit/(loss) on ordinary activities before taxation		1,883	(6,857)
Tax (charge)/credit on profit/(loss) on ordinary activities	8	(679)	948
Profit/(loss) on ordinary activities after taxation		1,204	(5,909)
Preference dividend	9	(1,932)	(1,449)
Loss for the financial period transferred from reserves	15	(728)	(7,358)

All of the above relates to discontinued operations.

There are no recognised gains and losses other than the loss for the financial period and consequently a statement of total recognised gains and losses has not been presented as part of the financial statements.

There is no difference between the loss for the period and the historical loss for the period and consequently no note of historical cost losses has been presented as part of the financial statements.

BALANCE SHEET

As at 30 June 1998

		30 June 1998		30 September 1997	
	Notes	**£'000**	**£'000**	**£'000**	**£'000**
Fixed assets					
Intangible assets	10	-		50	
Investments	11	328,976		328,976	
			328,976		329,026
Current assets					
Debtors	12	50,295		48,608	
Creditors – amounts falling due within one year	13	(333,636)		(331,271)	
Net current liabilities			(283,341)		(282,663)
Total net assets			45,635		46,363
Capital and reserves					
Called up share capital - equity		1,000		1,000	
- non equity	14	42,000	43,000	42,000	43,000
Share premium account		105		105	
Other reserves		1,900		1,900	
Profit and loss account		630		1,358	
	15		2,635		3,363
Total shareholders' funds			45,635		46,363

The financial statements on pages 8 to 17 were approved by the Board of Directors on 12 April 1999 and signed on its behalf by:

J M Summerlin
Director

NOTES (Forming part of the financial statements)

1 Analysis of turnover and loss before taxation

The turnover and loss before taxation were attributable to the processing, manufacture and distribution of food products, all of which are carried out in the United Kingdom.

2 Other operating costs

Profit / (loss) on ordinary activities before taxation is stated after charging:	9 months ended 30 June 1998 £'000	12 months ended 30 Sept 1997 £'000
Depreciation and other amounts written off tangible fixed assets	-	447
Hire of plant and machinery	-	83
Hire of other assets - operating leases	-	24
Research and development	-	46

Auditor's remuneration was paid on behalf of the company by a fellow group undertaking.

3 Staff numbers and costs

	9 months ended 30 June 1998	12 months ended 30 Sept 1997
Average number of employees	-	805

All of the above employees were engaged in the manufacture, marketing and distribution of food products.

The average staff numbers shown reflects the level of staff during the period in which the company traded.

The aggregate payroll costs of these persons were as follows:	9 months ended 30 June 1998 £'000	12 months ended 30 Sept 1997 £'000
Wages and salaries	-	4,240
Social security costs	-	314
	-	4,554

NOTES (continued)

4 Directors emoluments

No director has been paid any remuneration during the period, or previous period, for his services as a director of the company.

The directors were remunerated for their services either as directors or senior executives of Pillsbury UK Limited and, where appropriate, emoluments are disclosed in the financial statements of that company.

5 Discontinued operations

	9 months ended 30 June 1998 £'000	12 months ended 30 Sept 1997 £'000
Loss on disposal of discontinued operations	306	4,305

The loss on disposal of discontinued operations in 1997 arises from the disposal of the assets and trade of Brossard. This business was purchased from Express Foods Group (International) Limited on 30 December 1996 and was subsequently sold to a non group company on 28 June 1997.

6 Interest receivable and similar income

	9 months ended 30 June 1998 £'000	12 months ended 30 Sept 1997 £'000
Interest receivable from group undertakings	2,189	2,122

7 Interest payable and similar charges

	9 months ended 30 June 1998 £'000	12 months ended 30 Sept 1997 £'000
Interest payable to group undertakings	-	4,895

NOTES (continued

8. **Tax on profit / (loss) on ordinary activities**

	9 months ended 30 June 1998 £'000	12 months ended 30 Sept 1997 £'000
UK corporation tax (charge) / credit at 31% (1997 - 32%) on the profit / (loss) for the period on ordinary activities	(679)	948

9. **Dividends**

	9 months ended 30 June 1998 £'000	12 months ended 30 Sept 1997 £'000
Preference share dividend	1,932	1,449

10. **Intangible assets**

	30 June 1998 £'000	30 Sept 1997 £'000
Patent	-	50

NOTES (continued)

11. Fixed asset investments

	Subsidiary undertakings £'000
Shares	
At cost at beginning and end of period	378,300
Provision at beginning and end of period	(49,324)
Net book value at beginning and end of period	328,976

The company's principal subsidiary undertakings are as follows:

Subsidiary Undertakings	Country of Registration	Principal activity	Class and no. of shares held	
Express Foods Group (International) Limited	England	Manufacture and processing of food products	800,000	Ordinary stock units of 25p each – 100% directly owned
			52,918,181	'A' ordinary stock units of 25p each – 100% directly owned
			200,000	6% cumulative preference stock of £1 each – 100% directly owned
			507,110	6% 'A' cumulative preference stock £1 each - 100% directly owned
			100,000	7% cumulative preference stock of £1 each - 100% directly owned
			902,601	7% 'A' cumulative preference stock of £1 each - 100% directly owned
C.Shippam Limited	England	Manufacture and distributing of food products	4,164,865	Ordinary shares of £1 each - 100% directly owned
Precis (1057) Limited	England	Investment Company	190,500,000	Ordinary shares of £1 each - 100% directly owned

In the opinion of the directors of the company, the aggregate value of the shares of the subsidiary undertakings is not less than the aggregate of the amounts at which the investments are stated in the balance sheet. A full list of subsidiaries, all of which are consolidated, will be included in the company's next annual return.

NOTES (continued)

12. Debtors

	30 June 1998 £'000	30 Sept 1997 £'000
Amounts owed by group undertakings	49,543	47,660
Group relief receivable	752	948
	50,295	48,608

13. Creditors - amounts falling due within one year

	30 June 1998 £'000	30 Sept 1997 £'000
Amounts owed to group undertakings:-		
Immediate parent undertaking	31,501	31,501
Fellow subsidiary undertakings	302,135	299,770
	333,636	331,271

14. Share capital

	Authorised		Allotted, called up and fully paid			
	30 June 1998 No.	30 Sept 1998 No.	30 June 1998 No.	30 June 1998 £'000	30 Sept 1998 No.	30 Sept 1997 £'000
Ordinary shares 25p each	6,000,000	6,000,000	4,000,000	1,000	4,000,000	1,000
5.75% fixed rate non-redeemable preference shares £50 each	840,000	840,000	840,000	42,000	840,000	42,000
Total equity share capital				1,000		1,000
Total non equity share capital				42,000		42,000
				43,000		43,000

NOTES (continued)

15. Reconciliation of movements in total shareholders' funds

	At beginning of period £'000	Retained loss for period £'000	At end of period £'000
Share capital	43,000	-	43,000
Share premium account	105	-	105
Other reserves	1,900	-	1,900
Profit & loss account	1,358	(728)	630
Total	46,363	(728)	45,635

16. Contingent liabilities and guarantees

The company has guaranteed the loans of its subsidiary undertakings at 30 June 1998, the maximum liability of which would be £nil (1997 - £1,155,000).

17. Immediate and ultimate parent undertaking

The immediate parent undertaking is Grand Metropolitan PLC a company registered in England.

The ultimate parent undertaking of the company as at 30 June 1998 was Diageo plc, a company registered in England. Diageo plc's accounting period end is 30 June. The first consolidated accounts of Diageo plc for the eighteen month period ended 30 June 1998, can be obtained from the Registered Office at 8 Henrietta Place, London W1M 9AG.