

DIAGEO PLC
Form 20-F
August 11, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 20-F
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: 30 June 2015

Commission file number 1-10691

DIAGEO plc

(Exact name of Registrant as specified in its charter)

England and Wales

(Jurisdiction of incorporation or organisation)

Lakeside Drive, Park Royal, London NW10 7HQ, England

(Address of principal executive offices)

Paul Tunnacliffe, Company Secretary

Tel: +44 20 8978 6000

E-mail: the.cosec@diageo.com

Lakeside Drive, Park Royal, London NW10 7HQ, England

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

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

Title of each class	Name of each exchange on which registered
American Depositary Shares	New York Stock Exchange
Ordinary shares of 28 ¹⁰¹ / ₁₀₈ pence each	New York Stock Exchange ⁽ⁱ⁾
5.300% Guaranteed Notes due 2015	New York Stock Exchange
0.625% Guaranteed Notes due 2016	New York Stock Exchange
5.500% Guaranteed Notes due 2016	New York Stock Exchange
1.500% Guaranteed Notes due 2017	New York Stock Exchange
5.750% Guaranteed Notes due 2017	New York Stock Exchange
1.125% Guaranteed Notes due 2018	New York Stock Exchange
4.850% Guaranteed Notes due 2018	New York Stock Exchange
4.828% Guaranteed Notes due 2020	New York Stock Exchange
2.875% Guaranteed Notes due 2022	New York Stock Exchange
8.000% Guaranteed Notes due 2022	New York Stock Exchange
2.625% Guaranteed Notes due 2023	New York Stock Exchange
7.450% Guaranteed Notes due 2035	New York Stock Exchange
5.875% Guaranteed Notes due 2036	New York Stock Exchange
4.250% Guaranteed Notes due 2042	New York Stock Exchange
3.875% Guaranteed Notes due 2043	New York Stock Exchange

(i) Not for trading, but only in connection with the registration of American Depositary Shares representing such ordinary shares, pursuant to the requirements of the Securities and Exchange Commission.

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

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: **None**

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the Annual Report: 2,754,308,400 ordinary shares of 28¹⁰¹/₁₀₈ pence each.

Indicate by check mark if each registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes x No ..

If this report is an annual or transition report, indicate by check mark if each registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes No

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 corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether each registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP International Financial Reporting Standards Other
as issued by the International Accounting Standards Board

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow. Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

This document comprises the annual report on Form 20-F and the annual report to shareholders for the year ended 30 June 2015 of Diageo plc (the 2015 Form 20-F).

Contents

5	Introduction
7	Recent trends
8	Historical information
12	Strategic report
12	<i>Business description</i>
12	Our business
17	Our global reach
18	Our brands
19	Outstanding breadth and depth across price points
20	Our Performance Ambition
21	Our business model
22	Chairman's statement
25	Chief Executive's statement
28	How we measure performance: key performance indicators
32	Market dynamics
35	How we will deliver our Performance Ambition
36	Risk factors
42	Cautionary statement concerning forward-looking statements
44	<i>Business review</i>
44	Operating results 2015 compared with 2014
75	Operating results 2014 compared with 2013
99	Liquidity and capital resources
101	Contractual obligations and commitments
102	Off-balance sheet arrangements
102	Risk management
102	Critical accounting policies
102	New accounting standards
103	Sustainability & Responsibility review
120	Definitions and reconciliations of non-GAAP measures to GAAP measures
134	Governance
134	Board of Directors and Company Secretary
137	Executive Committee
139	Corporate governance report
147	Report of the Audit Committee
151	Directors' remuneration report
178	Directors' report

Contents (continued)

180 Financial statements

- 180 Reports of independent registered public accounting firms
- 182 Consolidated income statement
- 183 Consolidated statement of comprehensive income
- 184 Consolidated balance sheet
- 185 Consolidated statement of changes in equity
- 186 Consolidated statement of cash flows
- Notes to the consolidated financial statements
- 187 Accounting information and policies
- 190 Results for the year
- 206 Operating assets and liabilities
- 225 Risk management and capital structure
- 240 Other financial information

247 Report of independent registered public accounting firm - internal controls

248 Unaudited computation of ratio of earnings to fixed charges

249 Additional information for shareholders

- 249 Legal proceedings
- 249 Related party transactions
- 249 Share capital
- 250 American depositary shares
- 251 Articles of association
- 255 Exchange controls
- 255 Documents on display
- 256 Taxation
- 259 Warning to shareholders - share fraud
- 260 Signature
- 261 Exhibits
- 263 Cross reference to Form 20-F

265 Glossary of terms and US equivalents

Introduction

Diageo is the world's leading premium drinks business. Its geographic breadth and range of industry leading brands across categories and price points is unparalleled.

Diageo plc is incorporated as a public limited company in England and Wales. Diageo was incorporated as Arthur Guinness Son and Company Limited on 21 October 1886. The group was formed by the merger of Grand Metropolitan Public Limited Company (GrandMet) and Guinness PLC (the Guinness Group) in December 1997. Diageo plc's principal executive office is located at Lakeside Drive, Park Royal, London NW10 7HQ and its telephone number is +44 (0) 20 8978 6000. Diageo plc's agent for service of process in the United States is General Counsel, Diageo North America, Inc., 801 Main Avenue (6078-06), Norwalk, CT 06851.

This is the Annual Report on Form 20-F of Diageo plc for the year ended 30 June 2015. The information set out in this Form 20-F does not constitute Diageo plc's statutory accounts under the UK Companies Acts for the years ended 30 June 2015, 2014 or 2013. KPMG LLP has reported on the accounts for the year ended 30 June 2015 and 2014 and KPMG Audit Plc has reported on the accounts for the year ended 30 June 2013; their audit reports were (i) unqualified, (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report and (iii) did not contain a statement under section 498 (2) or (3) of the Companies Act 2006 in respect of the accounts for the years ended 30 June 2015, 2014 or 2013. The accounts for 2014 and 2013 have been delivered to the registrar of companies and those for 2015 will be delivered in due course.

This document contains forward-looking statements that involve risk and uncertainty. There are a number of factors that could cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements, including factors beyond Diageo's control. For more details, please refer to the cautionary statement concerning forward-looking statements on pages 42-43.

The content of the company's website (www.diageo.com) should not be considered to form a part of or be incorporated into this report. This report includes names of Diageo's products, which constitute trademarks or trade names which Diageo owns or which others own and license to Diageo for use. In this report, the term "company" refers to Diageo plc and terms "group" and "Diageo" refer to the company and its consolidated subsidiaries, except as the context otherwise requires. A glossary of terms used in this report is included at the end of the report.

Diageo's consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed and adopted for use in the European Union (EU) and IFRS as issued by the International Accounting Standards Board (IASB). References to IFRS hereafter should be construed as references to both IFRS as adopted by the EU and IFRS as issued by the IASB. Unless otherwise indicated, all financial information contained in this document has been prepared in accordance with IFRS.

Information presented

Unless otherwise stated in this document, percentage movements are organic movements. These movements and operating margins are before exceptional items. Commentary, unless otherwise stated, refers to organic movements. Share, unless otherwise stated, refers to value share. See the "Definitions and reconciliations of non-GAAP measures to GAAP measures" for an explanation of organic movement calculations on page 120.

The brand ranking information presented in this report, when comparing information with competitors, reflects data published by source such as IWSR, Impact Databank, Nielsen, Beverage Information Group and Plato Logic. Market data information and competitive set classifications are taken from independent industry sources in the markets in which Diageo operates.

Disclosures not incorporated by reference

The following pages and sections of the Annual Report of Diageo plc for the year ended 30 June 2015, are not incorporated by reference into this report on Form 20-F and are furnished to United States Securities and Exchange Commission (SEC) for information only:

Disclosures under the headings "Doing business the right way", "We produce", "We market", "We innovate", and "We sell" in the section

Strategic Report "Our business" on page 12.

Disclosures included under the titles "Number of responsible drinking programs (%)", "Water withdrawals" and "Carbon emissions" in the section "Strategic Report "Our Global Reach" Diageo reports as five region" on page 17.

Disclosures under the heading "Sustainability and responsibility" in the Chairman's Statement on page 23.

Introduction (continued)

Disclosures under the heading *Sustainability and responsibility* in the Chief Executive's statement on page 26.

Disclosures on pages 29 and 31 in the section *Strategic Report How we measure performance: key performance indicators* of non-financial key performance indicators.

Disclosures included under the title *Leadership in alcohol in society* in the section *Strategic Report How we will deliver our Performance Ambition our three Sustainability and Responsibility imperatives* on page 35.

Disclosures included under the titles *Increasing expectations of businesses and brands*, *Creating a positive role for alcohol in society*, *Factors affecting the operational environment*, *Climate change and water scarcity*, and *Local communities and supply chains* in the section *Strategic report Market dynamics* on pages 33 and 34.

Disclosures included under the titles *Sustainability and responsibility* on pages 55, 59, 63, 66, and 69 in relation to each reporting segment in the *Business Review*.

Disclosures in the section *Strategic report Sustainability & Responsibility review* on pages 103 to 119.

Recent trends

The following comments were made by Ivan Menezes, Chief Executive of Diageo, in Diageo's preliminary announcement on 30 July 2015:

Our F15 performance reflects the challenges we have seen on top line growth. However, it does not diminish my confidence in what we can achieve in F16 and even more so beyond that. Diageo has an enviable position, by geography, by brand and by category range, in an attractive consumer market place with strong long term growth drivers. This year we made further changes to build strong, sustained performance including embedding our sell out discipline, improving cash conversion and strengthening our route to consumer. We have consistently applied a long term perspective in making these changes, despite the short term challenges we have faced from an external environment where currency volatility continues to impact the emerging market consumer.

We acquired control of United Spirits in the year giving Diageo unparalleled access to one of the world's most attractive spirits markets. We have enhanced our position in tequila by acquiring the remaining 50% of Don Julio, a brand that is already growing net sales double digit and for which I see significant potential now we have full control. Our participation strategy is clear by market and category. We are focused on our core and have a more proactive approach to our portfolio. We sold Gleneagles in the year, and since the year end, have sold the shares USL owned in United Breweries and we restructured our South African operations to focus on spirits and monetise investments worth £125 million.

We are delivering the change which will further strengthen this business and deliver our performance ambition. In F16 we believe stronger volume growth will deliver an improved top line performance. As we achieve our productivity gains from F17 we expect to deliver mid single digit organic top line growth on a sustained basis and operating margin expansion of 100 basis points over 3 years. Our brands, our global footprint and our people give me confidence that Diageo can deliver strong and sustained performance.

Historical information

The following tables present selected consolidated financial data for Diageo for the five years ended 30 June 2015 and as at the respective year ends. The data presented below for the four years ended 30 June 2015 and the respective year ends has been derived from Diageo's consolidated financial statements, audited by Diageo's independent auditor. The financial information for the year ended 30 June 2011 has been derived from Diageo's financial statements, audited by Diageo's independent auditor, and restated in the year 30 June 2014 to reflect the adjustments resulting from the adoption of IFRS 11 and the amendment to IAS 19.

Income statement data

	Year ended 30 June				
	2015	2014	2013	2012	2011
	£ million	£ million	£ million	£ million	£ million
Sales	15,966	13,980	15,276	14,392	13,043
Excise duties	(5,153)	(3,722)	(3,973)	(3,753)	(3,224)
Net sales	10,813	10,258	11,303	10,639	9,819
Cost of sales	(4,610)	(4,029)	(4,416)	(4,208)	(3,958)
Gross profit	6,203	6,229	6,887	6,431	5,861
Marketing	(1,629)	(1,620)	(1,769)	(1,671)	(1,520)
Other operating expenses	(1,777)	(1,902)	(1,738)	(1,652)	(1,789)
Operating profit	2,797	2,707	3,380	3,108	2,552
Non-operating items	373	140	(83)	147	(14)
Net interest and other finance charges	(412)	(388)	(457)	(441)	(449)
Share of after tax results of associates and joint ventures	175	252	217	229	192
Profit before taxation	2,933	2,711	3,057	3,043	2,281
Taxation	(466)	(447)	(507)	(1,011)	(321)
Profit from continuing operations	2,467	2,264	2,550	2,032	1,960
Discontinued operations		(83)		(11)	
Profit for the year	2,467	2,181	2,550	2,021	1,960
Per share data	pence	pence	pence	pence	pence
Dividend per share	56.4	51.7	47.4	43.5	40.4
Earnings per share					
Basic					
Continuing operations	95.0	93.0	98.0	76.6	74.3
Discontinued operations		(3.3)		(0.4)	

Basic earnings per share	95.0	89.7	98.0	76.2	74.3
Diluted					
Continuing operations	94.6	92.6	97.4	76.2	74.1
Discontinued operations		(3.3)		(0.4)	
Diluted earnings per share	94.6	89.3	97.4	75.8	74.1
	million	million	million	million	million
Weighted average number of shares	2,505	2,506	2,502	2,495	2,493

Historical information (continued)**Balance sheet data**

	2015	2014	2013	2012	As at 30 June 2011
	£ million	£ million	£ million	£ million	£ million
Non-current assets	18,134	15,495	16,481	15,098	12,633
Current assets	7,670	7,469	8,510	7,171	7,087
Total assets	25,804	22,964	24,991	22,269	19,720
Current liabilities	(5,290)	(4,851)	(5,519)	(4,762)	(4,903)
Non-current liabilities	(11,258)	(10,523)	(11,384)	(10,715)	(8,858)
Total liabilities	(16,548)	(15,374)	(16,903)	(15,477)	(13,761)
Net assets	9,256	7,590	8,088	6,792	5,959
Share capital	797	797	797	797	797
Share premium	1,346	1,345	1,344	1,344	1,343
Other reserves	1,994	2,243	3,154	3,213	3,300
Retained earnings/(deficit)	3,634	2,438	1,741	234	(195)
Equity attributable of equity shareholders of the parent company	7,771	6,823	7,036	5,588	5,245
Non-controlling interests	1,485	767	1,052	1,204	714
Total equity	9,256	7,590	8,088	6,792	5,959
Net borrowings	(9,527)	(8,850)	(8,403)	(7,573)	(6,480)

Notes to the historical information

1. Accounting policies The consolidated financial statements for the five years ended 30 June 2015 have been prepared in accordance with IFRS. The IFRS accounting policies applied by the group to prepare the financial information in this document are disclosed in the notes to the consolidated financial statements.

2. Exceptional items Exceptional items are those that in management's judgement need to be disclosed by virtue of their size or nature. Such items are included within the income statement caption to which they relate, and are separately disclosed in the notes to the consolidated financial statements. An analysis of exceptional items is as follows:

	Year ended 30 June				
	2015	2014	2013	2012	2011
	£ million	£ million	£ million	£ million	£ million
Items included in operating profit					
Restructuring programmes	(82)	(163)	(69)	(96)	(111)
Duty settlements	(146)				(127)
Associate impairment	(41)				
Brand and tangible asset impairment		(264)	(50)	(59)	(39)
Pension changes past service credits			20	115	
SEC settlement					(12)
	(269)	(427)	(99)	(40)	(289)
Non-operating items	373	140	(83)	147	(14)
Items included in taxation					
Tax on exceptional operating items	51	99	27	19	51
Tax on sale of businesses			28		3
Loss of future tax amortisation				(524)	
Settlements with tax authorities					66
	51	99	55	(505)	120
Exceptional items in continuing operations	155	(188)	(127)	(398)	(183)
Discontinued operations net of taxation (note 3)		(83)		(11)	
Exceptional items	155	(271)	(127)	(409)	(183)

Historical information (continued)

3. Discontinued operations in the year ended 30 June 2014 comprised a charge after taxation of £83 million (£91 million less tax of £8 million) in respect of the settlement of thalidomide litigation in Australia and New Zealand and anticipated future payments to thalidomide organisations.

4. Dividends The Board expects that Diageo will pay an interim dividend in April and a final dividend in October of each year. Approximately 40% of the total dividend in respect of any financial year is expected to be paid as an interim dividend and approximately 60% as a final dividend. The payment of any future dividends, subject to shareholder approval, will depend upon Diageo's earnings, financial condition and such other factors as the Board deems relevant. Proposed dividends are not considered to be a liability until they are approved by the Board for the interim dividend and by the shareholders at the annual general meeting for the final dividend.

The table below sets out the amounts of interim, final and total cash dividends paid by the company on each ordinary share. The dividends are translated into US dollars per ADS (each ADS representing four ordinary shares) at the actual rate on each of the respective dividend payment dates.

		Year ended 30 June				
		2015	2014	2013	2012	2011
		pence	pence	pence	pence	pence
Per ordinary share	Interim	21.50	19.70	18.10	16.60	15.50
	Final	34.90	32.00	29.30	26.90	24.90
	Total	56.40	51.70	47.40	43.50	40.40
		\$	\$	\$	\$	\$
Per ADS	Interim	1.28	1.31	1.10	1.05	1.01
	Final	2.18	2.06	1.89	1.72	1.59
	Total	3.46	3.37	2.99	2.77	2.60

Note: Subject to shareholders' approval the final dividend for the year ended 30 June 2015 will be paid on 8 October 2015, and payment to US ADR holders will be made on 14 October 2015. In the table above, an exchange rate of £1 = \$1.56 has been assumed for this dividend, but the exact amount of the payment to US ADR holders will be determined by the rate of exchange on 8 October 2015.

5. Net borrowings Net borrowings are defined as gross borrowings (short term borrowings and long term borrowings plus finance lease liabilities plus interest rate hedging instruments, cross currency interest rate swaps and funding foreign currency forwards and swaps used to manage borrowings) less cash and cash equivalents.

6. Share capital There were 2,754 million ordinary shares of 28 ¹⁰¹/₁₀₈ pence each in issue with a nominal value of £797 million throughout the five year period ended 30 June 2015.

7. Exchange rates A substantial portion of the group's assets, liabilities, revenues and expenses are denominated in currencies other than sterling. For a discussion of the impact of exchange rate fluctuations on the group's financial position and results of operations, see note 15 to the consolidated financial statements.

The following table shows year end and average US dollar/pound sterling noon buying exchange rates, for the periods indicated, expressed in US dollars per £1.

	2015	2014	2013	Year ended 30 June	
	\$	\$	\$	2012	2011
	\$	\$	\$	\$	\$
Year end	1.57	1.71	1.52	1.57	1.61
Average rate ⁽ⁱ⁾	1.57	1.64	1.57	1.59	1.59

(i) The average of the noon buying rates on the last business day of each month during the year ended 30 June.

Historical information (continued)

The following table shows period end, high, low and average US dollar/pound sterling noon buying exchange rates by month, for the six month period to 31 July 2015, expressed in US dollars per £1. The information in respect of the month of July is for the period up to and including 31 July 2015.

	July	June	May	April	March	2015 February
	\$	\$	\$	\$	\$	\$
Month end	1.56	1.57	1.53	1.53	1.49	1.54
Month high	1.56	1.59	1.58	1.55	1.54	1.55
Month low	1.54	1.52	1.51	1.46	1.47	1.50
Average rate ⁽ⁱ⁾	1.56	1.56	1.55	1.50	1.50	1.53

(i) The average of the noon buying rates on each business day of the month.
The noon buying exchange rate as at 31 July 2015 was £1 = \$1.56.

These rates have been provided for information only. They are not necessarily the rates that have been used in this document for currency translations or in the preparation of the consolidated financial statements. See note 1 to the consolidated financial statements for the actual rates used in the preparation of the consolidated financial statements.

Strategic report

Business description

OUR BUSINESS

Diageo is a global leader in beverage alcohol with iconic brands in spirits, beer and wine. We provide consumers with choice and quality across categories and price points.

Diageo has built a strong platform for growth through investing in our brands and route to consumer. Over the last five years we have made acquisitions in brands and local distribution while doubling the size of our luxury business. We have also made changes to our operating model and culture aligning Diageo behind the need for greater agility and responsiveness, creating a business that is closer to the consumer.

Our 21 market model⁽ⁱ⁾ has established strong local business units, well positioned to win in increasingly competitive and fast paced operating environments.

We know that we must earn the trust and respect of everyone that comes into contact with our company. We must be transparent and authentic, demonstrating good citizenship every day, everywhere.

STRENGTH IN GLOBAL REACH AND ICONIC BRANDS

We have outstanding breadth and depth in our portfolio, with brands across price points and categories to meet consumer demand now and in the future.

DOING BUSINESS THE RIGHT WAY

For us, standards are everything, from how we produce and market our brands, to how we innovate and sell, and in governance and ethics as codified in our Code of Business Conduct.

WE PRODUCE	WE MARKET	WE INNOVATE	WE SELL
We produce our brands from more than 200 sites in over 30 countries. We are committed to efficient, sustainable production to the highest quality standards. Our export-led International Supply Centre (ISC) employs over 4,000 people across more than 55 sites in Scotland, England, Ireland, Italy and the Netherlands.	We invest in world-class marketing to build our brands, focusing on connecting with existing and new consumers. For decades our brands have been at the forefront of marketing innovation and the same remains true today. We take seriously our obligations to market responsibly and help consumers make informed decisions.	Innovation is critical to our continued growth. We are committed to finding breakthrough innovations to serve customers and consumers. We identify emerging trends, and boldly innovate at scale. Innovation is a permanent engine of growth for our business and we are restless in our search for new products.	Everyone at Diageo sells or understands how they can help sell. This is just one expression of the sales-led organisation we are building. In each of our 21 markets, we are passionate about ensuring our products are available where consumers want them. We work to deliver amazing consumer experiences and to extend our sales reach.

CREATING SHARED VALUE

Our distilleries, breweries and wineries are at the heart of the communities where we work. We have a responsibility to create shared value for our shareholders, our people, and for the societies that enable our business to grow. Within the community, we are proud of our work to address development challenges, including skills, social enterprise and access to clean water, and to encourage responsible drinking.

Our values underpin our business and guide us. We are passionate about our customers and consumers and want to be the best. We give our people the freedom to do the best work of their careers and value everyone's contribution. We are proud of what we do, and how we do it.

Our purpose, celebrating life, every day, everywhere, is to make the most of life to be the best at work, at home, with friends, in the community, and for the community. For our brands to be part of celebrations big and small.

- (i) Throughout this Form 20-F for the year ended 30 June 2015, reference to Diageo's 21 geographically based markets will be stated as 21 markets .

Business description (continued)**Production**

Diageo owns manufacturing production facilities across the globe, including maltings, distilleries, breweries, packaging plants, maturation warehouses, cooperages, vineyards, wineries and distribution warehouses. Diageo's brands are also produced at plants owned and operated by third parties and joint ventures at a number of locations internationally.

Diageo has been investing in restructuring programmes that increase the efficiency of its supply operations. The most significant programmes are referred to in note 4 to the consolidated financial statements.

The locations, principal activities, products, packaging production capacity and packaging production volume of Diageo's principal production centres in the year ended 30 June 2015 are as follows:

Location	Principal products	Production capacity in millions of equivalent units ⁽ⁱ⁾	Production volume in 2015 in millions of equivalent units
United Kingdom (Spirits)	Scotch whisky, Irish whiskey, gin, vodka, rum, ready to drink	91	51
UK, Ireland (Guinness)	Beer	8	7
Ireland (Baileys)	Irish cream liqueur	12	7
Italy (Santa Vittoria)	Vodka, wine, rum, ready to drink	11	5
Turkey	Raki, vodka, gin, liqueur, wine	8	6
United States, Canada, US Virgin Islands	Vodka, gin, tequila, rum, wine, Canadian whisky, American whiskey, progressive adult beverages, ready to drink	44	33
United States	Wine	2	1
Brazil	Cachaça, vodka	9	7
Jamaica	Beer	1	1
Mexico	Tequila	1	1
Australia	Rum, vodka, ready to drink	4	2
Singapore	Finishing centre	4	1
India	Rum, vodka, whisky, scotch, brandy, gin, wine	161	117
Nigeria	Beer	7	5
South Africa ⁽ⁱⁱ⁾	Beer and spirits	4	3
East Africa (Uganda, Kenya, Tanzania)	Beer and spirits	13	8
Africa Regional Markets (Ethiopia, Cameroon, Ghana, Seychelles)	Beer	5	4

- (i) Capacity represents ongoing production capacity. The production capacities quoted in the table are based on actual production levels for the year ended 30 June 2015 adjusted for the elimination of unplanned losses and inefficiencies.
- (ii) In South Africa Diageo has agreed to dispose of its 25% equity interest in Sedibeng Limited.

Spirits

Spirits are produced in distilleries located worldwide. The group owns 29 Scotch whisky distilleries in Scotland, two whisky distilleries in Canada and a whiskey distillery in the United States. Diageo produces Smirnoff internationally. Ketel One and Cîroc vodkas are purchased as finished product from The Nolet Group and Eurowinegate, respectively. Gin distilleries are located in both the United Kingdom and the United States. Baileys is produced in the Republic of Ireland and Northern Ireland. Rum is blended and bottled in the United States, Canada, Italy and the United Kingdom, and is distilled and blended in the US Virgin Islands and in Australia, Venezuela and Guatemala. Raki is produced in Turkey, Chinese spirits are produced in Chengdu, in the Sichuan province of China and cachaça is produced in Ceará State in Brazil. Diageo's maturing Scotch whisky is located in warehouses in Scotland (the largest at Blackgrange holding approximately 50% of the group's maturing Scotch whisky), its maturing Canadian whisky in La Salle and Gimli in Canada and its maturing American whiskey in Kentucky and Tennessee in the United States. In May 2014 the company announced its intention to invest approximately \$115 million (£73 million) over three years to build a distillery and six barrel storage warehouses in Shelby County, Kentucky. The new distillery is expected to be in operation by the end of 2016. In February 2015 Diageo sold its Bushmills distillery in Northern Ireland to the Cuervo Group.

Business description (continued)

From 2 July 2014 the group accounted for United Spirits Limited (USL) as a subsidiary with a 54.78% equity interest. USL is the leading alcoholic beverage company in India selling over 90 million equivalent cases of Indian Made Foreign Liquor (IMFL). It has a significant market presence across India and presently has 30 owned, 15 leased and 43 third party manufacturing facilities in India and Nepal. USL also operates spirit distillation plants for neutral alcohol, malt spirit, grape spirit and rum spirit with accompanying maturation facilities. USL has many leading Indian brands such as McDowell's (Indian whisky, rum and brandy), Black Dog (scotch), Signature (Indian whisky), Antiquity (Indian whisky) and Bagpiper (Indian whisky).

On 27 February 2015, Diageo acquired the 50% of Don Julio B.V. that it did not already own. Don Julio owns a distillery (located near Guadalajara, Mexico), maturing tequila inventory, bulk storage and bottling assets, as well as 6 million agave plants. Diageo's intent is to invest in the short term in house bottling capacity and agricultural operations and in the medium and long term in expanding distillation capacity.

In June 2012, the company announced a multi-year investment plan in Scotch whisky production and inventory. To date the spend is approximately £0.8billion and the programme is expected to be completed by 30 June 2017.

During the year to 30 June 2015, the company completed major expansions in Scotland at Glen Ord and Teaninich distilleries doubling the capacity at both sites as well as completing the second phase of seven warehouse builds at the new warehousing facility at Cluny near Kirkcaldy. On Speyside, the new bioenergy plant at Glendullan which treats by-products and generates biogas to be used as renewable energy by the distillery was completed.

Current maturing whisky inventory levels have allowed the commencement of the announced expansions at Clynelish and Mortlach distilleries to be delayed, however work has commenced on upgrading both distilleries.

Beer

Diageo's principal brewing facility is at the St James's Gate brewery in Dublin where the capacity was recently expanded to brew all beers sold in Western Europe and for global exports in particular to the United States. The Dundalk, Kilkenny and Waterford operations were closed in 2013. Diageo has breweries in a number of African countries; Nigeria, Kenya, Ghana, Cameroon, Ethiopia, Tanzania, Uganda, Seychelles, and brews Red Stripe in Jamaica. In the last six years Diageo has invested heavily in order to increase brewing capacity in Nigeria, Ghana, Cameroon, Kenya and in Ethiopia. The African businesses have also been investing in launching mainstream spirits in Africa, and have utilised a number of revolutionary portable spirits production units.

In addition, Diageo owns a 25.5% effective interest in Guinness Anchor Bernhard which operates a brewery in Malaysia, and a 25% equity interest in Sedibeng brewery in South Africa. On 28 July 2015 it was announced that the company agreed to dispose of its 25% interest in Sedibeng to Heineken.

Guinness is also brewed by over 50 third parties around the world under licence arrangements. Guinness flavour extract is shipped from Ireland to all overseas Guinness brewing operations which use the flavour extract to brew Guinness locally. Guinness Draught in cans and bottles is packaged at Runcorn and Belfast in the United Kingdom. The Runcorn facility performs the keggings of Guinness Draught which is transported to Great Britain in bulk.

Wine

Diageo's principal wineries are in the United States but the group also has operations in Argentina, Turkey and India. For European markets, wines are mainly bottled in Diageo's facilities in Italy. Wines are sold both in their local markets and overseas.

Ready to drink

Diageo produces a range of ready to drink products mainly in the United Kingdom, Italy, South Africa, Australia, the United States and Canada.

Property, plant and equipment

Diageo owns approximately 93% of the manufacturing, distilling, brewing, bottling and administration facilities it uses across the group's worldwide operations. It holds approximately 2% of properties on leases in excess of 50 years. The principal production facilities are described above. As at 30 June 2015, Diageo's land and buildings are included in the group's consolidated balance sheet

Business description (continued)

at a net book value of £1,044 million. Diageo's two largest individual facilities, in terms of book value, are the Leven bottling, blending and warehousing facility in Scotland and St James's Gate brewery in Dublin. Approximately 38% of the net book value of Diageo's land and buildings are properties located in Great Britain, 14% in Ireland, 13% in the United States and 8% in India.

Raw materials and supply agreements

The group has a number of long term contracts in place for the purchase of raw materials including glass, other packaging, spirit, cream, rum and grapes. Forward contracts are in place for the purchase of cereals to minimise the effects of short term price fluctuations.

Cream is the principal raw material used in the production of Irish cream liqueur and is sourced from Ireland. Grapes are used in the production of wine and raki and are sourced from suppliers in the United States, Argentina and Turkey. Other raw materials purchased in significant quantities for the production of spirits and beer are molasses, cereals, sugar and a number of flavours (such as juniper berries, agave, aniseed, chocolate and herbs). These are sourced from suppliers around the world.

The majority of products are supplied to customers in glass bottles. Glass is purchased from a variety of multinational and local suppliers; the largest suppliers are Ardagh Packaging in the United Kingdom and Owens Illinois in the United States.

Competition

Diageo's brands compete on the basis of consumer loyalty, quality and price.

In spirits, Diageo's major global competitors are Pernod Ricard, Beam Suntory, Bacardi and Brown-Forman, each of which has several brands that compete directly with Diageo's brands. In addition, Diageo faces competition from local and regional companies in the countries in which it operates.

In beer, Diageo competes globally as well as on a regional and local basis (with the profile varying between regions) with several competitors, including AB InBev, Heineken, SABMiller, Molson Coors and Carlsberg.

In wine, the market is fragmented with many producers and distributors.

Research and development

Innovation forms an important part of Diageo's growth strategy, playing a key role in positioning its brands for continued growth in both the developed and emerging markets. The strength and depth of Diageo's brand range provides a solid platform from which to drive innovation. Diageo continuously invests to deepen its understanding of shopper trends and changing consumer habits to inform product and packaging development. Supporting this, the group has ongoing programmes to develop new products across beverage alcohol categories which are managed internally by the innovation and research and development function, which also takes advantage of a substantial open innovation network.

In the year ended 30 June 2015, the group's research and development expenditure amounted to £26 million (2014 £24 million; 2013 £21 million), representing principally the cost of developing new products, from idea generation

through to full product development. Research and development expenditure is generally written off in the year in which it is incurred.

Trademarks

Diageo produces, sells and distributes branded goods and is therefore substantially dependent on the maintenance and protection of its trademarks. All brand names mentioned in this document are trademarks. The group also holds numerous licences and trade secrets, as well as having substantial trade knowledge related to its products. The group believes that its significant trademarks are registered and/or otherwise protected (insofar as legal protection is available) in all material respects in its most important markets. Diageo also owns valuable patents and trade secrets for technology and takes all reasonable steps to protect these rights.

Regulations and taxes

Diageo's worldwide operations are subject to extensive regulatory requirements regarding production, product liability, distribution, importation, marketing, promotion, sales, pricing, labelling, packaging, advertising, labour, pensions, compliance and control systems and environmental issues. In the United States, the beverage alcohol industry is subject to strict federal and state government regulations covering virtually every aspect of its operations, including production, distribution, marketing, promotion, sales, pricing, labelling, packaging and advertising.

Business description (continued)

Spirits, beer and wine are subject to national import and excise duties in many markets around the world. Most countries impose excise duties on beverage alcohol products, although the form of such taxation varies significantly from a simple application to units of alcohol by volume, to advanced systems based on imported or wholesale value of the product. Several countries impose additional import duty on distilled spirits, often discriminating between categories (such as Scotch whisky or bourbon) in the rate of such tariffs. Within the European Union, such products are subject to different rates of excise duty in each country, but within an overall European Union framework, there are minimum rates of excise duties that can be applied.

Import and excise duties can have a significant impact on the final pricing of Diageo's products to consumers. These duties have an impact on the competitive position as compared to other brands. The group devotes resources to encouraging the equitable taxation treatment of all beverage alcohol categories and to reducing government-imposed barriers to fair trading.

Advertising, marketing and sales of alcohol are subject to various restrictions in markets around the world. These range from a complete prohibition of alcohol in certain countries and cultures, through the prohibition of the import of spirits, wine and beer, to restrictions on the advertising style, media and messages used. In a number of countries, television is a prohibited medium for spirits brands and in other countries, television advertising, while permitted, is carefully regulated. Many countries also regulate the use of internet-based advertising and social media in connection with alcohol sales.

Spirits, beer and wine are also regulated in distribution. In many countries, alcohol may only be sold through licensed outlets, both on and off trade, varying from government or state operated monopoly outlets (for example, Canada, Norway and certain US states) to the common system of licensed on trade outlets (for example, licensed bars and restaurants) which prevails in much of the Western world (for example, most US states and the European Union). In about one-third of the states in the United States, price changes must be filed or published 30 days to three months, depending on the state, before they become effective.

Labelling of beverage alcohol products is also regulated in many markets, varying from health warning labels to importer identification, alcohol strength and other consumer information. As well as producer, importer or bottler identification, specific warning statements related to the risks of drinking beverage alcohol products are required to be included on all beverage alcohol products sold in the United States and in other countries where Diageo operates. Expressions of political concern signify the uncertain future of beverage alcohol products advertising on network television in the United States. Any prohibitions on advertising or marketing could have an adverse impact on sales of the group.

Regulatory decisions and changes in the legal and regulatory environment could increase Diageo's costs and liabilities or impact on its business activities.

Acquisitions and disposals

Diageo has made a number of acquisitions of brands, distribution rights and equity interests and disposals in premium drinks businesses. For a description of principal acquisitions and disposals since 1 July 2012, see note 9 to the consolidated financial statements.

Business description (continued)**OUR GLOBAL REACH**

One of Diageo's key strengths is its geographic reach. We operate as 21 geographically based markets around the world and have a presence in over 180 countries. We employ more than 33,000 talented people across our global business. 43% of Diageo's business is in the emerging markets in Latin America, Asia, Africa, Eastern Europe and Turkey. This presence is balanced through our strong businesses in the world's most profitable beverage alcohol market, the United States, and an integrated Western European business.

% SHARE OF NET SALES BY OUR 21 MARKETS**REACH OF OUR 21 MARKETS****MARKETS ACCOUNTABLE FOR ITS OWN PERFORMANCE AND**

MARKETS ACCOUNTABLE FOR ITS OWN PERFORMANCE AND	North America	Europe	Africa	Latin America and Caribbean	Asia Pacific
MARKETS DRIVING GROWTH	US Spirits and Wines	Western Europe ⁽ⁱ⁾			
15%					India
10%	Diageo Guinness USA (DGUSA)	Turkey	Nigeria, East Africa	West LAC	Global Travel, Asia and Middle East
6%	Canada		Africa Regional Markets	Paraguay, Uruguay and Brazil	Australia
3%					North Asia
					Greater China
2%		Russia and Eastern Europe ⁽ⁱ⁾	South Africa	Mexico, Venezuela, Colombia	South East Asia

Based on reported net sales for the year ended 30 June 2015.

(i) On 1 July 2015, Russia became a standalone market and Eastern Europe was merged with Western Europe to create a Diageo Europe market.

DIAGEO REPORTS AS FIVE REGIONS

	North America	Europe	Africa and Caribbean	Latin America	Asia Pacific
% SHARE BY REGION					
Volume (%)	19.2	17.9	10.6	8.8	43.5
Net sales⁽ⁱ⁾ (%)	32.2	24.4	13.2	9.6	20.6
Operating profit⁽ⁱⁱ⁾ (%)	45.4	25.2	10.0	8.2	11.2
Number of responsible drinking programmes⁽ⁱⁱⁱ⁾ (%)	21.1	24.5	14.1	19.8	20.5
Water withdrawals⁽ⁱⁱⁱ⁾ (%)	11.1	45.3	37.2	4.5	1.9

Carbon emissions⁽ⁱⁱⁱ⁾ (%)	8.5	51.8	35.0	3.2	1.5
Number of employees^(iv) (%)	9.8	33.0	16.5	8.8	31.9

- (i) Excluding corporate net sales of £80 million. (ii) Excluding exceptional operating charges of £269 million and corporate costs of £123 million. (iii) Excludes United Spirits Limited. See further details on pages 103-119.
(iv) Employees have been allocated to the region in which they reside.

Business description (continued)**OUR BRANDS**

Our 21 market model affords each market the flexibility to select the right portfolio of brands to capture the unique consumer opportunities that exist in that market and place resources directly against our biggest growth opportunities.

Our 21 market structure means we now look at our brands through the lens of global giants and local stars, alongside our leading reserve brands. Our in-market local star brands can be individual to any one market, and provide a platform to accelerate the growth of our international premium spirits. A selection of these brands are included in the table below.

Global giants⁽ⁱ⁾					
Johnnie Walker	Smirnoff	Captain Morgan	Baileys	Tanqueray	Guinness
Local stars⁽ⁱⁱ⁾			Reserve⁽ⁱⁱⁱ⁾		
Crown Royal	Yeni Raki	JeB	Johnnie Walker Extra Rare	John Walker & Sons Odyssey	Johnnie Walker King George V
Buchanans	Windsor	Grand Old Parr	Johnnie Walker Blue Label	Johnnie Walker Gold Label Reserve	The Singleton of Glen Ord
Bundaberg	Bells	McDowell's No. 1	Cîroc	Ketel One vodka	Tanqueray No. TEN
Ypióca	Cacique	Shui Jing Fang	Ron Zacapa Centenario XO	Tequila Reserva de Don Juilo	Bulleit Bourbon

(i) Global giants represent 39% of Diageo net sales. (ii) Local stars represent 16% of Diageo net sales. (iii) Reserve brands represent 13% of Diageo net sales.

Business description (continued)**OUTSTANDING BREADTH AND DEPTH ACROSS PRICE POINTS**

In our portfolio we have brands at almost every price tier of every category. The range of our price points means we are able to capture consumption shifts across the price spectrum. The breadth and depth of our business provide resilience, and enable us to sustain our performance over time.

	Ultra premium⁽ⁱ⁾	Super premium	Premium	Standard	Value
Scotch whisky	Johnnie Walker Blue Label	The Singleton of Glen Ord	Johnnie Walker Black Label	JeB	VAT 69
Other whisk(e)y	Crown Royal Extra Rare	Bulleit Bourbon	Crown Royal	Seagram's 7 Crown	
Vodka	Cîroc	Ketel One vodka	Smirnoff Iced Cake Flavoured Vodka	Smirnoff	Istanblue
Rum	Ron Zacapa Centenario XO	Pampero Aniversario Ron Extra Añejo	Captain Morgan Private Stock	Captain Morgan	
Liqueur	Grand Marnier Cuvée du Cent Cinquantaire	Grand Marnier Cuvée Louis Alexandre	Sheridan's Original Layered Liqueur	Baileys	Emmets
Tequila	DeLeón tequila	Tequila Reserva de Don Juilo			
Gin	Tanqueray No. TEN		Tanqueray	Gordon's	Gilbey's
Local spirits	Shui Jing Fang		Yeni Raki	Ypióca	McDowell's
Beer		Kilkenny	Guinness	Meta Beer	No. 1 Dubic Extra Lager

(i) Ultra premium includes prestige.

Business description (continued)

OUR PERFORMANCE AMBITION

Diageo's Performance Ambition is to create one of the best performing, most trusted and respected consumer products companies in the world.

DIAGEO'S STRATEGY AIMS TO DELIVER OUR PERFORMANCE AMBITION THROUGH:

- | | | | | |
|--|------------------------------------|---------------------------------|---------|---------|
| 1. Prioritised investment in: | | 2. Targeted investment in: | | |
| a. Premium core spirits ⁽ⁱ⁾ (Read more on page 35.) | b. Reserve (Read more on page 35.) | a. Other spirits ⁽ⁱ⁾ | b. Beer | c. Wine |
- (i) Spirits include ready to drink (RTDs).

We measure progress against our Performance Ambition using the following financial and non-financial indicators:

#1 Efficient growth	#2 Consistent value creation	#3 Credibility and trust	#4 Motivated people
Organic net sales		Responsible drinking	Health and safety
Operating margin	Return on average invested capital		Employee
Earnings per share		programmes	engagement
Free cash flow	Total shareholder return	Water efficiency	
		Carbon emissions	

See our key performance indicators (KPIs) on pages 28-31.

Business description (continued)

OUR BUSINESS MODEL

Diageo has grown through investment in our brands and route to consumer, and by acquisitions to broaden our geographical footprint and our category depth and range. Our business model is designed to drive returns for shareholders, while creating value for our customers, employees and the communities in which we operate.

1. STRONG PLATFORM

Broad portfolio: Diageo has world-leading brands across categories and price points.

Geographic reach: we have geographic reach through the breadth and depth of our global and local brands.

Financial strength: our competitive advantage is reflected by our strong financial returns and consistent financial performance.

**2. AGILE OPERATING MODEL
21 markets**

Participation strategy: our participation strategy is to invest behind the biggest growth opportunities, by category and channel, for our brands in our 21 markets.

Supply management: our 21 markets are designated as import markets, import and third party production markets, or import and local production markets.

3. FOCUSED INVESTMENT

Performance drivers: Diageo has identified six performance drivers which are key to achieving our aims. Each market focuses on the priorities that will drive performance in that market: **premium core brands; reserve; innovation; route to consumer; cost; and talent.**

Sustainability & Responsibility imperatives:

Alcohol in society we aim to create a positive role for alcohol in society through partnerships and programmes that reduce harmful drinking.

Thriving communities we must equip people in our business, our supply chain and our communities, particularly women, with the skills and resources they need to build a better future for themselves.

Environmental impact we will make our products and business operations more environmentally sustainable, targeting water use, carbon emissions and waste, reducing the volume of packaging we use and sourcing paper and board from sustainable forests.

Our performance drivers and Sustainability & Responsibility

imperatives are underpinned by our commitment to the highest standards of governance and ethics.

Efficient supply and procurement: across the world we have efficiency in supply and procurement, with our manufacturing operations working to high quality and environmental standards.

Consumer insights: our deep consumer insights help us to anticipate and respond to rapidly changing dynamics across all markets, and continue to nurture and grow some of the world's best-loved brands.

Leading capabilities: Diageo's focus is on brilliant execution including breakthrough marketing, scalable innovation, and winning relationships with our customers and consumers through distribution and sales.

Global functions: Diageo's 21 markets are supported by a global structure and shared services designed to share best practice, impart knowledge and help build capability at a local level, as well as apply governance of controls, compliance and ethics.

Values: at the heart of everything we do are our company values: passionate about customers and consumers; be the best; freedom to succeed; proud of what we do; valuing each other.

4. Value creation: shareholder value; investment in the business; customer, employee and social value

Business description (continued)

CHAIRMAN'S STATEMENT:

WE ARE CREATING ONE OF THE BEST PERFORMING, MOST TRUSTED AND RESPECTED CONSUMER PRODUCTS COMPANIES.

Over the last two years we have taken the necessary steps to strengthen Diageo, to position our company to drive sustainable growth and value for you, our shareholders, and to ensure we are a trusted and respected partner to all our stakeholders around the world.

Interim dividend per share

21.5p (h9%)

31 December 2013: 19.7p

Final recommended dividend per share

34.9p (h9%)

30 June 2014: 32.0p

Total dividend per share⁽ⁱ⁾

56.4p (h9%)

Full year 2014: 51.7p

(i) Includes recommended final dividend.

Diageo is a leader in beverage alcohol, one of the most attractive growth sectors in consumer products. With our portfolio of global and local brands, and the presence we have built in developed and emerging markets, we are well positioned to capture this growth.

Performance and dividend

In a volatile global environment, our commitment to being one of the best performing, most trusted and respected consumer products companies is as strong as ever. Ivan and the Executive Committee have taken actions to strengthen the business to deliver operational and cultural change, greater agility and responsiveness. Performance this year reflects these actions and continued tough conditions in some markets. In addition, currency volatility affected trading, especially in some of our scotch markets where currency devaluation impacted the price of imported goods for local consumers.

We are more focused than ever on managing cost and delivering cash, and I am pleased that we achieved strong cash conversion, over 100%, during the year. This, together with the actions we are taking to realise our full potential, has enabled the Board to recommend a final dividend of 34.9 pence per share. This would bring the total dividend for the

year to 56.4 pence per share, an increase of 9% over the prior year. The final dividend will be paid to shareholders on 8 October 2015. Earnings per share to dividend cover at 1.6 times is now outside our cover ratio, and we will look to rebuild cover over time, maintaining dividend increases at a mid-single digit rate until we are back in range.

Strategic progress

Diageo's strategy is delivered through a market focus. In individual markets, we compete with our iconic global brands and local stars while building strong routes to consumer. Our in-market teams are accountable for delivering holistic performance and are empowered to act with speed and agility, supported by the scale and expertise of our global business.

Business description (continued)

As a business we have been focused on organic growth while capturing inorganic opportunities. For example, we have been capitalising on North American whisk(e)y trends with the launch of Crown Royal Regal Apple and the continuing success of Bulleit and our other craft bourbons. We have also been broadening our participation in new categories and across price points, with the Orijin brand in Nigeria and Haig Club, a single grain Scotch whisky.

Diageo acquired a majority stake in United Spirits Limited (USL) in India in July 2014, consolidating Diageo's position as a local leader in spirits in this exciting growth market. We are now moving into the next phase of integration, prioritising brand investment, driving efficiencies and continuing the implementation of Diageo's operational and governance standards across the business, while putting in place a route to consumer team to further develop USL's already impressive market coverage.

In February 2015, we completed the acquisition of the remaining 50% of tequila brand, Don Julio. In gaining full global ownership and management control of the brand and its supply assets, we enhance our position in the high growth segments of super and ultra premium tequila. With this deal we also repatriated the Smirnoff brand into our in-market company in Mexico which will allow us to extend our leading position in spirits in this attractive market.

We remain committed to reviewing our portfolio to ensure that we are the best owners of our assets. We realised full management control of Don Julio through the sale of Bushmills. While Bushmills is a good brand, this was the right strategic decision for Diageo as we invest behind the biggest growth opportunities. The sale of Gleneagles Hotels Limited is another example of Diageo's decision to focus on key priorities. Following the success of the Ryder Cup we felt it was an appropriate time to realise value through this sale. We are pleased that the new owner of Gleneagles has committed to be a significant inward investor in Scottish tourism and will work closely with the local community to make a positive contribution to the visitor industry and the Scottish economy.

Sustainability and responsibility

Diageo has a long history of working within the communities where our products are enjoyed, and we understand that the role and impact of alcohol within society must be our primary focus. Our work to promote responsible drinking and reduce alcohol-related harm remains central to our purpose of celebrating life every day, everywhere, and we share the goal of the World Health Organization (WHO) to reduce the harmful use of alcohol by 10% by 2025. In line with the industry's commitments, during the year progress was made on underage drinking, reducing drink driving and strengthening marketing codes.

We are proud of the broad contribution we are making to society, through our economic contribution and through our three community programmes: Learning for Life, Water of Life and Plan W. These programmes have: provided training and skills to more than 100,000 people in the Americas and Britain to help them secure new jobs; delivered access to clean water and sanitation to more than ten million people in Africa supporting better health; and empowered around 100,000 women across Asia. And within Diageo, we continue to champion diversity and inclusivity. One example of this is the level of female representation at Board and Executive Committee level, at 45% and 40% respectively.

Business environment

With our strong portfolio of Scotch whisky brands, we have a deep commitment to Scotland built on the heritage of some of the industry's greatest entrepreneurs. The current debate over the United Kingdom's role within the European Union is one in which Diageo is actively engaged. We want our Scotch whisky business, which makes a considerable

contribution to the British economy, to remain competitive in the global marketplace and believe that the best interests of the whole industry are served by the United Kingdom remaining within a strong, reformed European Union.

Board changes

Having been on the Board for nine years, Laurence Danon will step down at the upcoming Annual General Meeting. On your behalf I would like to thank Laurence for her contribution over a period of progress and growth for Diageo. In July 2015, we announced that Emma Walmsley will join the Board as a Non-Executive Director effective 1 January 2016. Emma is currently Chief Executive Officer of GSK Consumer Healthcare.

Our people

Diageo's success is in the hands of our 33,000 employees around the world. I would like to thank them all for their dedication and hard work during the year. We must create an environment that stretches and challenges our people and enables them to do their best work, living our values each and every day. I am committed to continuing to build such an environment, and look forward to working with my colleagues on the Board and throughout the business to make sure that we do.

Business description (continued)

Looking ahead

Your Board is confident that Diageo will deliver its Performance Ambition. Over the last two years we have taken the necessary steps to strengthen Diageo, to position our company to drive sustainable growth and value for you, our shareholders, and to ensure we are a trusted and respected partner to all our stakeholders around the world.

Dr Franz B Humer

Chairman

Business description (continued)

CHIEF EXECUTIVE'S STATEMENT:

WE HAVE DELIVERED CHANGES WHICH WILL BUILD STRONG, SUSTAINED PERFORMANCE.

The fundamentals for future growth remain strong: Diageo will benefit from the increasing penetration of spirits in emerging markets, innovation and the growing appetite for luxury spirits around the world.

In the next decade one billion new consumers will be able to afford our brands and an additional 800 million consumers will reach levels of income where luxury brands are affordable. Diageo has the leading position in the United States, an integrated Western Europe business, a strong beer platform in Africa from which to build spirits, the leading spirits business in India, and a strong presence in the growth markets of Latin America and Asia.

This year we improved cash conversion, strengthened our route to consumer, delivered industry leading innovation at scale, extended our leadership in reserve and accelerated delivery of our programmed cost savings. We have further sharpened our marketing to better navigate changing consumer trends. So, while some markets have been challenging, we remain confident in the long term global demographics and our ability to deliver growth through the business transformation we are effecting.

Driving operational and cultural change

In the past year we have implemented some important changes to strengthen our business. These changes are aimed at providing greater visibility and will allow us to react more quickly to changes in the marketplace, consumer sentiment and demand.

We have completed our shift to a market-led model, enabling greater speed in the way we execute and local accountability.

We have shifted our focus to the consumer, allowing us to make better decisions on how we use our marketing spend and run our supply chains.

We have embedded a productivity discipline, in order to create more opportunity to invest behind growth in our brands.

We continue to ensure we have the right people with the right capabilities to deliver our plans across our business.

Results

Organic net sales were flat. Volume declined 1% reflecting a destock in South East Asia, lower shipments in the United States and improving price/mix led by the growth of reserve brands.

Organic operating margin was up 24 basis points delivered by cost savings and efficiencies, which more than offset the impact of cost inflation and negative market mix. Our global efficiency programme identified £200 million of cost savings to be delivered by the end of fiscal 2017. We delivered £127 million this year, and as planned reinvested £30 million of the savings.

Free cash flow was up over £700 million this year, to almost £2 billion, as I made cash a clear priority for improvement. To deliver this, incentive programmes were changed and we set clear targets for each market. This focus has led to many examples across markets where we have improved processes and ways of working to reduce our working capital. The sales of the Bushmills brand and the Gleneagles Hotel also generated cash in the year.

Business description (continued)

Earnings per share before exceptionals fell 7% to 88.8 pence largely as a result of adverse exchange movements and lower income from associates and joint ventures, offset by underlying improvements.

Sustainability and responsibility

In December 2014 we launched our 2020 Sustainability & Responsibility targets. Stretching and industry leading, our 2020 targets address our most material issues: leadership in alcohol in society; building thriving communities; and reducing our environmental impact. The 2020 targets draw on our achievements to date and are aligned with the new, emerging United Nations Sustainable Development Goals.

With these targets, we are going beyond the establishment of programmes on responsible drinking, community development and environmental performance, to focus on measuring their impact, challenging ourselves to strengthen their value, impact and scale. In doing so, we will work in partnership with governments, civil society, individuals, NGOs and other companies to put in place programmes with quantifiable outcomes. We continue to support fully the Global Producers' Commitments, a co-ordinated industry response to support the World Health Organization's (WHO) Global Strategy to Reduce the Harmful Use of Alcohol.

In April this year we announced an ambitious strategy for water stewardship. With water a pressing business and global issue, our Water Blueprint recognises the responsibilities of operating in water-stressed areas and explains how we will support the sustainability of the water resources on which we and those around us rely. Our Water Blueprint and our progress towards all of our targets are essential parts of our long term plan, not just in enabling sustainable operations but also in creating opportunities for growth.

Our people

It is a privilege to work with Diageo teams across the world. I feel honoured to lead a company where purpose and values are deeply ingrained. The commitment of our people to get behind the decisions taken during the year is encouraging. This was demonstrated in the results of our annual employee Values Survey, with employee engagement improving through a tough performance period. This evidence of the passion and commitment all of us hold for Diageo is the perfect fuel to drive future growth, and I look forward to working with our teams across the business, implementing the exciting plans we have for the year ahead.

Larry Schwartz, President Diageo North America, will retire at the end of this calendar year. Larry has many achievements in a 40-year career in the industry, not least his commitment to deliver growth for Diageo and build our strong North American platform. Deirdre Mahlan, currently Chief Financial Officer and the incoming leader of this business, will have this platform to build on as she drives the next stage of Diageo North America's growth.

Productivity

At the end of July 2015, we announced our intention to deliver productivity gains of a further £500 million over three years from fiscal 2017 to invest in growth and improve margin. As we achieve our productivity gains we expect to

deliver mid-single digit organic top line growth on a sustained basis and operating margin expansion of 100 basis points over the same three year period.

Business description (continued)

Outlook

The fundamentals for future growth remain strong: Diageo will benefit from the increasing penetration of spirits in emerging markets, innovation and the growing appetite for luxury spirits around the world.

We have taken some tough decisions over the last couple of years to set Diageo up to deliver strong, sustained performance. Today we are closer to the consumer, more agile, and focused on productivity, with the people, skills and capabilities to deliver on the opportunity. We are at an exciting point on our journey. In 2016, we believe stronger volume growth will deliver an improved top line performance.

Ivan Menezes

Chief Executive

Business description (continued)

HOW WE MEASURE PERFORMANCE: KEY PERFORMANCE INDICATORS

We use the following 11 key performance indicators (KPIs) to measure our financial and non-financial performance.

Their relevance to our strategy and our performance against these measures are explained below:

Relevance to strategy

- #1 Efficient growth
- #2 Consistent value creation
- #3 Credibility and trust
- #4 Motivated people

**FINANCIAL
ORGANIC NET SALES GROWTH
(%)[®] #1**

**FINANCIAL
ORGANIC OPERATING
MARGIN IMPROVEMENT (BPS)
[®] #1**

**FINANCIAL
EARNINGS PER SHARE
BEFORE EXCEPTIONAL ITEMS
(PENCE)⁽ⁱ⁾ [®] #1**

Definition

Sales growth after deducting excise duties, excluding the impact of exchange rate movements, acquisitions and disposals.

Why we measure

This measure reflects our performance as the result of the choices made in terms of category and market participation, and Diageo's ability to build brand equity, increase prices and grow market share.

Performance

Definition

The percentage point movement in operating profit before exceptional items, divided by net sales after excluding the impact of exchange rate movements and acquisitions and disposals.

Why we measure

The movement in operating margin measures the efficiency of the business. Consistent operating margin improvement is a business imperative, driven by investment choices, our focus on driving out costs across the business and improving mix.

Performance

Definition

Profit before exceptional items attributable to equity shareholders of the parent company, divided by the weighted average number of shares in issue.

Why we measure

Earnings per share reflects the profitability of the business and how effectively we finance our balance sheet. It is a key measure for our shareholders.

Performance

Organic net sales were flat, with volume decline of 1% reflecting a destock in South East Asia and West LAC, lower shipments in the United States and improving price/mix led by the growth of reserve brands. See page 47 for more detail.

Margin improved mainly due to cost savings, primarily through our global efficiency programme, partially offset by reinvestment in route to consumer, cost inflation and negative market mix. See page 47 for more detail.

Eps before exceptional was down by 6.7 pence per share driven by adverse exchange movements and lower income from associates and joint ventures, offset by underlying improvements. See page 48 for more detail.

Business description (continued)**NON-FINANCIAL
ALCOHOL IN SOCIETY⁽ⁱⁱⁱ⁾****(RESPONSIBLE DRINKING
PROGRAMMES) #3****Definition**

Programmes supported by Diageo that aim to reduce harmful drinking.

Why we measure

Alcohol-related harm is our most important social issue. These programmes address risks such as: harm to consumers and communities; limitations to our licence to operate; and the loss of trust and respect from our stakeholders.

Performance

In shifting our focus towards the Global Producers Commitments, we supported fewer programmes this year, and in line with our 2020 target, we are prioritising impact, which involves supporting fewer but more effective programmes.

See page 104 for more detail.

**NON-FINANCIAL
HEALTH AND SAFETY⁽ⁱⁱⁱ⁾****(LOST-TIME ACCIDENT
FREQUENCY PER 1,000
EMPLOYEES) #4****Definition**

Number of accidents per 1,000 employees and directly supervised contractors resulting in time lost from work of one calendar day or more.

Why we measure

Safety is a basic human right: everyone has the right to work in a safe environment, and our Zero Harm safety philosophy is that everyone should go home safe, every day, everywhere.

Performance

Our overall lost-time accident frequency rate has remained static despite improvements in our operations, our accident rate in offices and sales functions has increased. Addressing this will be a key focus for us in 2016.

See page 113 for more detail.

**NON-FINANCIAL
WATER EFFICIENCY^{(iii), (v)} (L/L)
#3****Definition**

Ratio of the amount of water required to produce one litre of packaged product.

Why we measure

Water is the main ingredient in all of our brands. To sustain production growth and respond to the growing global demand for water, we aim to improve efficiency, minimising our water use, particularly in water-stressed areas.

Performance

11.8% improvement on 2014, resulting from process optimisations and improvements related to equipment, raw material handling, culture and behaviour towards water stewardship.

See page 108 for more detail.

Business description (continued)**FINANCIAL
FREE CASH FLOW****(£ MILLION)[®] #1****Definition**

Free cash flow comprises the net cash flow from operating activities aggregated with the net cash received/paid for loans receivable and other investments, and the net cash cost paid for property, plant and equipment, and computer software.

Why we measure

Free cash flow is a key indicator of the financial management of the business and reflects the cash generated by the business to fund payments to our shareholders and acquisitions.

Performance

Improved working capital, primarily due to lower debtors driven by phasing of sales in the last quarter, was the biggest driver of the improvement in free cash flow.

See page 49 for more detail.

**FINANCIAL
RETURN ON AVERAGE
INVESTED CAPITAL (ROIC)****(%)⁽ⁱⁱ⁾ #2****Definition**

Profit before finance charges and exceptional items attributable to equity shareholders divided by average invested capital. Invested capital comprises net assets aggregated with exceptional restructuring costs and goodwill at the date of transition to IFRS, excluding post employment liabilities, net borrowings and non-controlling interests.

Why we measure

ROIC is used by management to assess the return obtained from the group's asset base. Improving ROIC builds financial strength to enable Diageo to attain its financial objectives.

Performance

The additional investment in United Spirits Limited and its full consolidation reduced ROIC by 1.1 pps. Adverse exchange and lower income from associates resulted in a further reduction offset by organic operating profit growth.

See page 49 for more detail.

**FINANCIAL
TOTAL SHAREHOLDER
RETURN (%)[®] #2****Definition**

Percentage growth in the value of a Diageo share (assuming all dividends and capital distributions are re-invested).

Why we measure

As a public limited company, Diageo has a fiduciary responsibility to maximise long term value for shareholders. We also monitor our relative TSR performance against our peers.

Performance

Diageo delivered total shareholder return of 2% as dividends paid increased by 9% and earnings declined mainly as a result of adverse exchange movements.

Business description (continued)

**NON-FINANCIAL
CARBON EMISSIONS^{(iii), (vi)}
(1,000 TONNES CO₂E) #3**

Definition

Absolute volume of carbon emissions, in 1,000 tonnes.

Why we measure

Carbon is a key element of our overall environmental impact and the impact of the industry. We recognise the importance of reducing our carbon emissions, not just to create efficiencies and savings now, but also to mitigate climate change and position us well for a low carbon economy in the future.

Performance

Improved performance resulting from cumulative impacts of multiple energy efficiency initiatives and switches to renewable fuels, predominately biogas recovery and reuse.

See page 109 for more detail.

**NON-FINANCIAL
EMPLOYEE ENGAGEMENT
INDEX (%) #4**

Definition

Measured through our Values Survey; includes metrics for employee satisfaction, loyalty, advocacy and pride.

Why we measure

Employee engagement is a key enabler of our strategy and performance. The survey allows us to measure, quantitatively and qualitatively, how far employees believe we are living our values. The results inform our ways of working, engagement strategies and leadership development.

Performance

94% of our people participated in our Annual Values Survey. Our people confirmed that one of our core strengths continues to be our employees' pride and strong sense of ownership of our business and our brands.

See page 114 for more detail.

Remuneration

Some KPIs are used as a measure in the incentives plans for the remuneration of executives. These are identified with the symbol@.

See our Directors' remuneration report from page 151 for more detail.

- (i) For reward purposes this measure is further adjusted for the impact of exchange rates and other factors not controlled by management, to ensure focus on our underlying performance drivers.
- (ii) The group has revised the return on average invested capital calculation by excluding the profit and net assets attributable to non-controlling interests. Comparative figures have been restated.
- (iii) Excludes United Spirits Limited. See pages 103 – 119 for further details.
- (iv) Revised comparative amount to be consistent with current year presentation, see more details on page 114.
- (v) In accordance with Diageo's environmental reporting methodologies, data for each of the two years in the period ended 30 June 2014 has been restated and total water used excludes irrigation water for agricultural purposes on land under the operational control of the company.
- (vi) Data for each of the two years in the period ended 30 June 2014 has been restated in accordance with the WRI/WBCSD GHG Protocol and Diageo's environmental reporting methodology.
- (vii) In 2014, we reviewed our overall approach to measuring engagement, and adopted a revised index (it is not possible to restate prior year figures under the new method, so 2013 show highly engaged scores based on the former method). The new index allows us to compare our results with other best-in-class organisations, and sets a more challenging benchmark for employee engagement. As part of this process, we changed our key performance indicator from 'super engagement' to 'engagement'.

Business description (continued)

MARKET DYNAMICS

The global beverage alcohol market is large and diverse, with an estimated six billion equivalent units of alcohol sold each year, generating £300 billion of net sales. It is also one of the most regulated in the world, and beverage alcohol companies operate in the context of a range of stakeholder expectations and demands. This environment presents opportunities for a business like Diageo, with our global scale, our diverse range of leading brands, and our high standards of governance and ethics.

A growing global market

Beverage alcohol is a profitable, growing and attractive market in which to participate. Margins are significantly higher than for the overall consumer goods market, while, over the medium term, the industry is expected to grow in both volume and value. While the global market is split almost equally between emerging and developed markets, emerging markets are expected to grow at a faster rate.

Within emerging markets and developed markets, every individual market presents different consumer dynamics and a different outlook determined by specific local conditions. Our 21-market operating model, coupled with tailored local strategies, enables us to meet the specific needs of consumers across different geographies.

Opportunities in developed markets

In developed markets, the population is ageing, and in aggregate is growing more slowly than in emerging markets in some countries it is shrinking. Overall, wealth is fairly static but is increasingly polarised as growth is skewed towards the most affluent. The opportunities in developed markets are therefore very different from emerging markets. Given the higher levels of disposable income and the importance of branding, in developed markets consumers are often prepared to pay more for high quality brands with heritage and provenance. Our key opportunities are to offer beer customers other products, particularly spirits, and, as tastes evolve, to encourage consumers to trade up within spirits brands.

Opportunities in emerging markets

Growth of beverage alcohol consumption in emerging markets is driven by strong, underlying consumer fundamentals. The number of people of legal purchasing age is growing worldwide, and is set to increase by over 450 million over the next decade. Wealth is increasing, with the middle class growing. This means more consumers are buying brands and they have more money to spend on them. There is a good opportunity for growth for spirits, as consumer tastes shift and disposable incomes rise.

Factors affecting consumer choices

While medium-term prospects for beverage alcohol are robust and positive for the reasons described above, in the short term there are particular challenges that face all consumer goods businesses.

Business description (continued)

Economic and political instability

Sudden changes to economic variables such as exchange rates and commodity prices, or changes in levels of political security, can reduce consumer confidence and spending power. Over the last year alone we have witnessed considerable economic, social and political upheaval in many places: huge currency devaluations in Venezuela; geo-political conflict in Russia and Ukraine; the Ebola outbreak; and terrorist threats in Nigeria and Kenya, to name some examples. The general operating environment will continue to be a turbulent and unpredictable one in which to compete.

Our approach is based on broad participation across geographies, categories and price tiers, which provides a natural hedge against individual market volatility, while tailored strategies for each market allow us to respond quickly to local dynamics. Operationally, we continue to focus on improving our risk management processes, while our 21-market operating model enables our markets to respond quickly to local events and trends. Our renewed focus on managing the business according to what is actually bought by consumers rather than what we sell to our customers will also help to improve the consistency of our performance across markets.

Increasing expectations of businesses and brands

Consumers today – particularly millennials – have increasing expectations of the businesses behind the brands they love. It is not enough to provide a great product and brand experience: companies must make a contribution that goes beyond economic benefits, to encompass environmental and social benefits as well.

This is reflected in the developing regulatory framework for listed companies, which are expected to be transparent about their key social and environmental issues, and, through reporting, to demonstrate progress. Going beyond what is mandatory has become the norm for global businesses, which are adopting various voluntary frameworks. These include the International Integrated Reporting Framework, published last year, the Global Reporting Initiative Guidelines, launched in 2000 and updated last year, and the United Nations Global Compact principles, established in 2006, all of which we follow in our reporting.

This high and growing level of regulation and scrutiny can be an advantage to companies with good corporate governance and the right approach to sustainability and responsibility.

Creating a positive role for alcohol in society

Diageo has always believed that creating a positive role for alcohol in society is about working in partnership with all the relevant stakeholders, through concerted industry initiatives. We are one of 13 global producers of beer, wine and spirits which, in 2013, launched a set of commitments designed to support Member States' implementation of the World Health Organization's (WHO) global strategy to reduce the harmful use of alcohol. They include a focus on reducing underage drinking, strengthening and expanding marketing codes of practice, providing consumer information and responsible product innovation, reducing drink driving, and enlisting the support of retailers to reduce harmful drinking.

Diageo also believes that the most effective alcohol policies are evidence-based, account for drinking patterns, target at-risk groups, treat all forms of alcohol equally, and involve all stakeholders. Such policies include mandating a minimum legal purchasing age of not less than 18; a maximum blood alcohol concentration (BAC) level for drivers of no more than 0.08mg; and lower BACs for novice and commercial drivers. Also effective are high-visibility

enforcement campaigns of drink-driving laws and alcohol interlock devices for convicted drink drivers.

Diageo advocates these policies while opposing measures that are not based on evidence, and are likely to have unintended consequences. For example the use of high taxes to control consumption can in some cases push consumers to unregulated alcohol markets. These are potentially dangerous for consumers what little is known about this unrecorded alcohol, which the WHO estimates accounts for 25% of alcohol consumed, suggests that some may be contaminated, some toxic, and a risk to public health.

Factors affecting the operational environment

The developments in reporting social and environmental issues noted above are a reflection of their importance to business performance. The interdependence of companies and their local environments, communities and economies is a growing phenomenon, which Diageo has long recognised through our sustainability and responsibility programmes. In December 2014 we launched our 2020 Sustainability & Responsibility targets, which focus on three imperatives: leadership in alcohol in society; building thriving communities; and reducing our environmental impact.

Business description (continued)

Climate change and water scarcity

Companies particularly those that rely on agricultural raw materials are increasingly being affected by a variety of environmental issues associated with climate change, such as extreme weather events, water scarcity and biodiversity loss.

For the alcohol industry, water scarcity demands particular attention given that water is the main ingredient in all alcoholic beverages. The World Bank expects water scarcity to affect 2.8 billion people directly by 2025, and the increasing importance of water as a global issue is recognised in our Water Blueprint, launched in April 2015, which defines our strategic approach to water stewardship across the value chain. The map below shows our sites located in water-stressed areas where our approach to water stewardship is particularly important.

Local communities and supply chains

Alcohol beverage companies contribute to the economic development of their communities in a variety of ways, whether through direct or indirect employment, taxes or community investment efforts. However, companies can further contribute by leveraging the economic impact of their entire value chain in the way they work with suppliers and customers and doing so is an increasing expectation of the private sector by government and international development institutions. One powerful trend in the food and beverage industry is a focus on local sourcing in markets with an agricultural economy or the potential for one, and, in Africa, we have a target of sourcing 80% of agricultural materials locally (sourced within Africa and used by our African markets). This helps build trust with government and other stakeholders, can help secure supply, and it delivers wider benefits to the local community.

Business description (continued)

HOW WE WILL DELIVER OUR PERFORMANCE AMBITION

Diageo's performance drivers and Sustainability & Responsibility imperatives are key to achieving our Performance Ambition. Each of our 21 markets focuses on the priorities that are most relevant to driving growth and creating shared value in that market.

OUR SIX PERFORMANCE DRIVERS

1. Strengthen and accelerate growth of our premium core brands

Our premium core brands are sold in more than 180 countries around the world. They are enjoyed by consumers in the developed markets and have wide appeal in emerging markets. They include iconic brands like Johnnie Walker, Smirnoff, Captain Morgan and Baileys.

2. Win in reserve in every market

Our reserve or luxury portfolio accounts for 13% of our total net sales. Over the last six years we have transformed our luxury brand building capabilities and are now the industry leader in the super and ultra premium segments.

3. Innovate at scale to meet new consumer needs

Our ability to innovate is a competitive advantage. A proven driver of growth, it is critical to the performance in each of our markets. Since 2009, innovation has accounted for at least half of Diageo's sales growth, growing double-digit each year.

4. Build and then constantly extend our advantage in route to consumer

Our global programme looks at how we can profitably extend where our brands appear and improve the quality of how they appear at every appropriate drinking or buying occasion, achieving higher rates of sale in an efficient way.

5. Drive out costs to invest in growth

Increasing productivity and efficiency within Diageo will improve profitability and allow us to invest back into the business to drive growth.

6. Ensure we have the talent to deliver our Performance Ambition

We employ bright, collaborative people at all levels in our business, and must continue to do so if we are to achieve our Performance Ambition. Ensuring that we have the best talent now and in the future is one of our biggest challenges and one of our greatest opportunities.

OUR THREE SUSTAINABILITY & RESPONSIBILITY IMPERATIVES

1. Leadership in alcohol in society

Creating a positive role for alcohol in society is our primary focus, and over the last decade we have supported hundreds of programmes to tackle harmful drinking and encourage responsibility. We will continue these efforts with our various stakeholder partners as well as focus on delivering the five Global Producers Commitments.

2. Building thriving communities

Our distilleries, breweries and wineries are at the heart of our communities, and we have a responsibility to create shared value throughout our supply chain. Our targets commit us to further partnerships with local farmers and agricultural communities to develop more sustainable supply chains and secure our raw material supply.

3. Reducing our environmental impact

Recognising that our impact on the environment is not limited to our own sites, our targets reflect the need to better manage water stewardship and carbon emissions across our whole supply chain. We will work increasingly with suppliers, striving to decouple the growth of our business from our impact on the environment.

Business description (continued)

Risk factors

Diageo believes the following to be the principal risks and uncertainties facing the group. If any of these risks occur, Diageo's business, financial condition and performance could suffer and the trading price and liquidity of securities could decline.

In the ongoing uncertain economic environment, certain risks may gain more prominence either individually or when taken together. For example, demand for beverage alcohol products, in particular luxury or super premium products, may decrease with a reduction in consumer spending levels. Costs of operations may increase if inflation were to become prevalent, or upon an increase in the costs of raw materials. These conditions may also lead to intensified competition for market share, with potentially adverse effects on volume and prices. The financial and economic situation may have a negative impact on third parties with whom Diageo does, or may do, business. Any of these factors may affect the group's performance, financial condition and liquidity. Diageo has taken and may take further steps to manage its business through this challenging economic environment and to position its business to benefit from economic recovery as and when that may occur in the markets in which Diageo operates, but there can be no assurance that the steps taken will have the intended results.

Diageo's ability to fund its long term strategies may be adversely affected if there is an extended period of constraint in the capital markets, particularly the debt markets, at the same time that cash flows from Diageo's business are under pressure. Such developments may adversely affect shareholder returns or share price. Additionally, continued volatility in exchange rates used to translate foreign currencies into pounds sterling may have a significant impact on Diageo's reported results. Changes in the trustees' valuations of the assets and liabilities of Diageo's pension plans may also increase pension funding requirements.

Risks related to the global economy

Diageo's business may be adversely impacted by unfavourable economic conditions or political or other developments and risks in the countries in which it operates

Diageo may be adversely affected by political, economic or social developments in any of the countries where it has distribution networks, production facilities or marketing companies. Diageo's business is dependent on general economic conditions in the United States, countries that form the European Union and other important markets.

If the economy in any of these markets does not recover as forecast, or if there is a significant deterioration in the economic conditions in any of Diageo's important markets, including any resulting social unrest, reduction in consumer confidence and spending levels, customer destocking, the failure of customer, supplier or financial counterparties or a reduction in the availability of, or an increase in the cost of financing to, Diageo, it could have a material adverse effect on Diageo's business and performance. Any such economic developments may lead to reduced economic growth and, in turn, reduced demand for Diageo's products, in Europe and other markets in which Diageo operates. This could have a material adverse effect on Diageo's business.

Diageo is headquartered in the United Kingdom and has significant production and investment in Scotland. Following the result of the Scottish independence referendum in 2014 and the UK general election in 2015, legislation to grant more devolved powers to the Scottish parliament has been introduced. Diageo will monitor the passage of this Bill. Amendments granting additional devolved powers may be proposed, and these could result in a further period of political uncertainty that may adversely affect Diageo's business. Regarding Britain's place in Europe, by the end of

2017, the current government in the United Kingdom has undertaken to conduct a referendum on the UK's continued membership of the European Union. The UK's withdrawal from the EU would involve a sustained period of uncertainty and complexity which could have an adverse effect on our operations and profitability. In addition, Diageo's operations are also subject to a variety of other risks and uncertainties related to trading in numerous foreign countries, including political or economic upheaval and the imposition of any import, investment or currency restrictions, including tariffs and import quotas or any restrictions on the repatriation of earnings and capital. Political and/or social unrest, potential health issues, natural disasters and terrorist threats and/or acts may also occur in various places around the world, which will have an impact on trade, tourism and travel. Many of these risks are heightened, or occur more frequently, in emerging markets. These disruptions can affect Diageo's ability to import or export products and to repatriate funds, as well as affecting the levels of consumer demand (for example, in duty free outlets at airports or in on trade premises in affected regions) and therefore Diageo's levels of sales or profitability. A substantial portion of Diageo's operations, representing approximately 43% of Diageo's net sales for the year ended 30 June 2015, are carried out in emerging markets. Emerging markets are also generally exposed to relatively higher risk of liquidity constraints, inflation, devaluation, price volatility, currency convertibility and sovereign default. Due to Diageo's specific exposures, any or all of the aforementioned factors may affect Diageo disproportionately or in a different manner as compared to its competitors.

Business description (continued)

Part of Diageo's growth strategy includes expanding its business in certain countries where consumer spending in general, and spending on Diageo's products in particular, has not historically been as great but where there are strong prospects for growth. There is no guarantee that this strategy will be successful and some of these markets represent a higher risk in terms of their changing regulatory environments and higher degree of uncertainty over levels of consumer spending.

Risks related to the industry

Demand for Diageo's products may be adversely affected by many factors, including changes in consumer preferences and tastes and adverse impacts of a declining economy

Diageo's collection of brands includes some of the world's leading beverage alcohol brands as well as brands of local prominence. Maintaining Diageo's competitive position depends on its continued ability to offer products that have a strong appeal to consumers. Consumer preferences may shift due to a variety of factors including changes in demographic and social trends, public health regulations, changes in travel, vacation or leisure activity patterns, weather effects and a downturn in economic conditions, which may reduce consumers' willingness to purchase premium branded products. Continued economic pressures could also lead to consumers selecting products at lower price points, whether Diageo's or those of its competitors, which may have an adverse effect on Diageo's profitability. The competitive position of Diageo's brands could also be affected adversely by any failure to achieve consistent, reliable quality in the product or in service levels to customers.

In addition, the social acceptability of Diageo's products may decline due to public concerns about alcohol consumption. These concerns could also result in regulatory action, litigation or customer complaints against companies in the industry and may have an adverse effect on Diageo's profitability.

Growth in Diageo's business has benefited from both the launch of new products and the creation of brand extensions and product innovation remains a significant element of Diageo's growth plans. The launch and ongoing success of new