SPECTRUM CONTROL INC
Form 8-K
January 10, 2005

EFFECTIVE AUGUST 23RD, 2004

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

FORM 8-K

CURRENT REPORT
Pursuant to Section 13 OR 15(d) of The Securities Exchange Act of 1934

Date of Report (Date of earliest event reported) January 10, 2005

Spectrum Control, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania	**0-8796**	**25-1196447**
(State or other jurisdiction of incorporation)	*(Commission File Number)*	*(I.R.S. Employer Identification No.)*

8031 Avonia Road; Fairview, Pennsylvania	**16415**
(Address of principal executive offices)	*(Zip Code)*

Registrant s telephone number, including area code (814) 474-2207

(Former name or former address, if changed since last report.)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

o Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

o Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

o Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 2.02 Results of Operations and Financial Condition

The following information, including the exhibits attached hereto, shall not be deemed filed for purposes of the Securities Exchange Act of 1934, as amended (the Exchange Act), or incorporated by reference in any filing under the Securities Act of 1933, as amended, or under the Exchange Act, except as may be expressly set forth by specific reference in such a filing.

On January 10, 2005, Spectrum Control, Inc. issued an earnings release announcing its financial results for the fourth quarter and fiscal year ended November 30, 2004. A copy of the earnings release is attached as Exhibit 99.1.

Item 9.01 Financial Statements and Exhibits

(c) Exhibits 99.1 Press Release of Spectrum Control, Inc. dated January 1, 2005

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereto duly authorized.

SPECTRUM CONTROL, INC.

(Registrant)

Date: January 10, 2005

By: /s/ JOHN P. FREEMAN

(Signature)
Senior Vice President
and Chief Financial Officer

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2009
Reported

Exchange(1)

	Acquisitions and disposals(2)	Organic movement	2010 Reported	Organic movement
	£ million	£ million	£ million	£ million
	£ million	%		
Sales				

North America	
	1,969
	94
	(23
)	
	54
	2,094
	3
Europe	
	2,456

(50

)

(18

)

(76

)

2,312

(3

)

International

1,726

(174

)

(1

)

222

1,773

14

Asia Pacific

737

	80
	98
	915
	12
Corporate	
	40
	(1
)	
	(1
)	
	38
Total sales	
	6,928

(51

)

(42

)

297

7,132

4

2009
Reported

Exchange(1)

Acquisitions and disposals(2)

Organic movement

2010 Reported

Organic movement

£ million

£ million

£ million

£ million

£ million

%

Net sales

North America	
	1,695
	82
	(23
)	
	53
	1,807
	3
Europe	
	1,547

(38
)
(13
)
(52
)
1,444
(3
)
International
1,402
(149
)
(1
)
163
1,415
13
Asia Pacific
523

53

(40

)

616

7

Corporate

40

(1

)

(1

)

38

Total net sales

5,207

(53

)

(37

)

203

5,320

4

Excise duties

1,721

1,812

Total sales

6,928

7,132

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	2009 Reported £ million	Exchange(1) £ million	Acquisitions and disposals(2) £ million	Organic movement £ million	2010 Reported £ million	Organic movement %
Marketing spend						
North America	228	11		**29**	**268**	**12**
Europe	229	(6)	(1)	**3**	**225**	**1**
International	150			**27**	**177**	**18**
Asia Pacific	118	11	1	**13**	**143**	**10**
Total marketing spend	725	16		**72**	**813**	**10**

	2009 Reported £ million	Exchange(1) £ million	Acquisitions and disposals(2) £ million	Organic movement £ million	2010 Reported £ million	Organic movement %
Operating profit						
North America	667	23	(1)	**34**	**723**	**5**
Europe	528	(9)	1	**(49)**	**471**	**(9)**
International	460	(51)	(1)	**60**	**468**	**15**
Asia Pacific	103	9	(3)	**20**	**129**	**18**
Corporate	(127)	98		**(35)**	**(64)**	
Total operating profit before exceptional items	1,631	70	(4)	**30**	**1,727**	**2**
Exceptional items(3)	(95)				**(9)**	
Total operating profit	1,536				**1,718**	

Notes: Information relating to the organic movement calculations

(1) The exchange adjustments for sales, net sales, marketing spend and operating profit are primarily the retranslation of prior period reported results at current period exchange rates and are principally in respect of the strengthening of the US dollar offset by the weakening of the Venezuelan bolivar.

(2) The impacts of acquisitions and disposals are excluded from the organic movement percentages. In the six months ended 31 December 2010 there were no acquisitions impacting organic growth. Disposals in the six months ended 31 December 2010 were the disposals completed under the reorganisation of the group s US wines operations and the disposal of the Gilbeys wholesale wine business in Ireland. Adjustment is also made to exclude directly attributable transaction costs incurred in the six months ended 31 December 2010 of £6 million, netted against acquisition costs of £3 million incurred in the six months period ended 31 December 2009 primarily in respect of the acquisition of Serengeti Breweries and the potential acquisition of an additional equity stake in Quanxing.

(3) Operating exceptional items in the six months ended 31 December 2010 comprised charges of £4 million (2009 - £69 million) in respect of the restructuring of Global Supply operations and £5 million (2009 - £5 million) in respect of the restructuring of Irish brewing operations. In addition a charge of £21 million was incurred in respect of the global restructuring programme in the six months ended 31 December 2009.

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Strategic brands performance by category*

Brand performance is now reported using the 14 strategic brands below. This replaces the previous classification of 8 global priority brands, which was introduced in 2002 following the Seagram acquisition. The new classification is a natural evolution and better reflects the way in which brands are managed.

	Volume movement** %	Organic net sales movement %	Reported net sales movement %
Whisk(e)y			
Johnnie Walker	11	10	11
Crown Royal	3	5	10
J&B	(8)	(10)	(11)
Windsor	6	11	20
Buchanan s	(3)	14	(33)
Bushmills	5	5	7
Vodka			
Smirnoff	2	(1)	2
Ketel One	2		5
Cîroc	128	131	139
Liqueurs			
Baileys	3	1	
Rum			
Captain Morgan	7	7	12
Tequila			
Jose Cuervo	7	7	10
Gin			
Tanqueray	(3)	(2)	1
Beer			
Guinness	(2)	(1)	

* Spirits brands excluding ready to drink

** Volume movement is both reported and organic

The classification of brands as global priority brands and other brands has been discontinued for reporting purposes. Increases in organic and reported volume, organic net sales and reported net sales for global priority brands are 3%, 3% and 4%, respectively, and for other brands 3%, 6% and 0%, respectively, against the comparable period last year.

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Analysis by region

North America

Key highlights

- North America returned to volume growth and delivered mix improvement led by the growth of spirits
- Innovation contributed significantly to net sales growth
- Gross margin expansion was driven by improved product mix and tight control of cost of goods
- Marketing spend increased 12% with further increases in investment behind the strategic spirits brands
- Promotional spend was reduced on US spirits brands in the off trade which cost Diageo 1 percentage point of share
- Wine declined as promotional support was reduced in a category where growth was driven by increased promotions
- A reduction in overheads also contributed to operating margin improvement

Key measures:	**Six months ended 31 December 2010 Equivalent units million**	**Six months ended 31 December 2009 Equivalent units million**	**Organic movement %**	**Reported movement %**
Volume	**28.0**	27.6	**2**	**1**
	£ million	**£ million**	**%**	**%**
Net sales	**1,807**	1,695	**3**	**7**
Marketing spend	**268**	228	**12**	**18**
Operating profit before exceptional items	**723**	667	**5**	**8**
Operating profit	**723**	661	**5**	**9**

Organic performance:

Net sales growth of 3% in North America was driven by the improved performance of the strategic spirits brands. In the United States there were some signs of a gradual economic recovery but high unemployment and low income growth held back a significant improvement in consumer confidence. Despite this, the industry reported value growth across spirits, beer and wine. In spirits and wine, mirroring the positive mix trend in the industry, Diageo net sales grew faster in the premium and above segments than in standard and below. Diageo s strategy to reduce discounting and promotional activity resulted in share loss but contributed to positive price/mix. Mix improvement, strict control of cost of goods and a reduction in overheads delivered operating profit growth of 5%. Canada showed a solid recovery with growth in both the on and off trade and Diageo increased its share of spirits.

	Volume movement* %	Organic net sales movement %	Reported net sales movement %
By market:			
United States	1	3	6
Canada	4	4	13
By category:			
Spirits	2	4	9
Beer	(1)	1	7
Wine	(10)	(7)	(16)
Ready to drink	(1)	(2)	3
Strategic brands:**			
Johnnie Walker	(6)	(4)	
Smirnoff	2	1	6
Baileys	1	1	6
Captain Morgan	1	1	6
Jose Cuervo	7	7	12
Tanqueray	(7)	(5)	(1)
Crown Royal	2	4	9
Ketel One	1	(1)	4
Cîroc	131	134	144
Guinness	1	1	6

* Volume movement is both reported and organic except for wine where reported movement was (19)% due to disposals in the period

** Spirits brands excluding ready to drink

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The classification of brands as global priority brands and other brands has been discontinued for reporting purposes. Increases in organic volume, reported volume, organic net sales and reported net sales for global priority brands are 1%, 1%, 0% and 5%, respectively, and for other brands 3%, 2%, 7% and 9%, respectively, against the comparable period last year.

United States - Volume growth, mix improvement and strong marketing spend

Volume performance was driven by spirits, as beer and wine declined and ready to drink remained flat. Within spirits, volume growth was led by Cîroc up 131% and Jose Cuervo up 7%. Net sales growth was primarily driven by Cîroc up 134%, Crown Royal up 5% and innovation. The strategic decision to reduce promotional activity contributed to price/mix improvements in spirits, beer and wine but share losses across many categories and segments.

Johnnie Walker volume declined 9% due predominantly to a planned reduction in wholesaler inventories of Johnnie Walker Red and Black Labels to bring shipments and depletions closer in line. Net sales decreased 6% as price increases were taken across most variants and mix improved due to the performance of super deluxe variants, Johnnie Walker Gold, Blue and King George V, as well as the introduction of The John Walker.

Smirnoff returned to volume growth on the performance of Smirnoff Red up 3% partially offset by the decline in Smirnoff Flavours and Smirnoff Blue. Net sales declined 1% as price/mix was negative across all variants. Promotional activity in the premium vodka segment remained high. However, promotions on Smirnoff were reduced, resulting in a share loss of 1 percentage point.

Baileys net sales declined 1%. A good performance by Baileys flavours, up 6%, was not sufficient to offset a 3% decline on the base variant. The brand continued to sell at a premium price despite challenging economic conditions and Baileys gained 0.2 percentage points of share.

Captain Morgan remained under pressure from new spiced rum entrants, with over 40 new brands launched in the past five years. As a result, Captain Morgan lost 0.3 percentage points of share. Volume was flat and net sales declined 1%, primarily due to a reduction in volume of Parrot Bay.

Volume and net sales of Jose Cuervo increased 7% in comparison to the first half of fiscal 2010 when the brand experienced some destocking. The brand continued to sell at a premium price in line with strategy despite continued competition and Jose Cuervo lost 3.3 percentage points of share. Jose Cuervo Silver continued to perform well and maintained its position as the number one silver tequila by volume in the United States. In the super and ultra premium segments, Jose Cuervo Tradicional performed well.

Tanqueray volume declined as inventories of London Dry Gin were reduced at the wholesaler level. Positive price/mix was due to price increases and the strong performance of Tanqueray Ten, up 14% in net sales.

Crown Royal grew volume 2% and net sales 5% fuelled by the success of Crown Royal Black and Crown Royal Cask 16. Crown Royal Black remained number one in IRI s new spirits product tracker, while the brand grew 0.2 percentage points of share.

Ketel One vodka volume was flat and net sales decreased 1%. Declines in Ketel One Citroen were partially offset by increases in Ketel One Oranje which was launched last year. Competition remained strong in the vodka category and Ketel One vodka lost 0.2 percentage points of share.

Cîroc was the driving force behind growth in the United States. Volume increased due to the continued success of the new Cîroc flavours Coconut and Red Berry, which have exceeded expectations. Price increases helped drive positive price/mix. Cîroc s exceptional performance has driven 0.3 percentage points of share gain in a highly competitive category.

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Guinness grew volume and net sales 1% driven by Guinness Draft in Cans and the success of Guinness Foreign Extra Stout, which launched nationally in October. Guinness lost 0.1 percentage points of share driven by declines in Guinness Draft in Bottle, lapping the 250th Anniversary Stout launch of a year ago.

Bushmills grew volume 10% and net sales 5% following a planned price reduction to reposition the brand in line with its competition. Gordon s, Popov, Seagram s 7 Crown and Seagram s VO all declined reflecting the slowdown in the value and standard segments.

Reserve brands grew volume 23% and net sales 27% with growth across nearly all brands. Volume growth and selective price increases across key brands such as Johnnie Walker Blue Label and Cîroc helped drive much of the positive price/mix for the half. Also of note were the performances of Buchanan s Special Reserve up 36% and Classic Malts up 26% in net sales.

Red Stripe held volume flat but grew net sales 7% on price increases and the continued success of Red Stripe Light. Harp volume and net sales both fell 5% and Smithwick s volume and net sales declined 9% due to heavy competition from craft beers.

Wine volume declined 10% and net sales declined 7% as promotional support was reduced compared to the prior period. Declines in the Sterling Vintners Collection were partially offset by BV Georges de La Tour and the Sterling reserve wines. Within the Chalone wine group A by Acacia outperformed the market due to distribution gains and off trade programmes while Chalone Vineyards and Edna Valley declined. Rosenblum net sales declined as consumers shifted away from vineyard designate and appellations to vintner s cuvees.

Ready to drink volume was held flat on the success of Smirnoff Mixed Drinks. Net sales declined 1% as the Smirnoff, Jose Cuervo and Captain Morgan cocktail lines declined due to their premium price.

Innovation centred on the vodka category with the launch of RÖKK vodka, Godiva Chocolate Vodka and Moon Mountain Vodka. RÖKK, a freeze filtered vodka from Sweden, was positioned in the premium segment while Godiva Chocolate Vodka and Moon Mountain Vodka offered alternatives in the super premium segment.

Marketing increased by 11% as Diageo maintained its commitment to invest behind strategic brands and proven marketing programmes. Diageo continued its focus on Smirnoff Red behind the I Choose campaign and launched the DJ reality TV show Master of the Mix. Crown Royal integrated Crown Royal Black into NASCAR, football and the Crown Royal Affair. Captain Morgan increased its sport sponsorships and the One Million Pose social responsibility campaign. Cîroc continued its collaboration with Sean Diddy Combs around the Ultimate Summer Cabana and Cîroc the New Year in conjunction with E! Entertainment. This investment has increased Diageo s share of voice to 9.5% overall with increases across spirits, beer and ready to drink.

Canada - Recovery of the on trade drove volume and net sales growth

The favourable turnaround in the on trade was reflected in Diageo s volume and net sales growth of 4%. Volume performance was driven by Smirnoff up 6%, Captain Morgan up 8%, Johnnie Walker up 44% and Baileys up 8%, while net sales were driven by Smirnoff up 8%, Captain

Morgan up 11% and Johnnie Walker up 44%. Price/mix was flat as price increases on Smirnoff, Captain Morgan and Tanqueray were offset by the decline in the ready to drink segment.

Europe

Key highlights

- The economic pressures in Greece, Iberia and to a lesser extent Ireland led to a 13% net sales decline across these markets
- In Great Britain net sales grew 1%, however negative price/mix in spirits and the strong growth of wine led to margin erosion
- Russia and Eastern Europe grew net sales over 20% as a result of the improving economic situation and strong growth of imported spirits
- In the rest of Europe a mixed performance resulted in net sales decline of 1%
- Import restrictions in Turkey resulted in no trading in the domestic channel in the half
- In line with these trends, marketing spend in Greece and Iberia decreased 21%, spend in Russia and Eastern Europe increased over 50% whilst spend in the rest of Europe increased slightly, focused on strategic brands
- Operating profit decline was principally driven by negative category mix in Great Britain and economic weakness in Greece and Iberia

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Key measures:	Six months ended 31 December 2010 Equivalent units million	Six months ended 31 December 2009 Equivalent units million	Organic movement %	Reported movement %
Volume	**21.5**	22.0	**(2)**	**(2)**

	£ million	**£ million**	**%**	**%**
Net sales	**1,444**	1,547	**(3)**	**(7)**
Marketing spend	**225**	229	**1**	**(2)**
Operating profit before exceptional items	**471**	528	**(9)**	**(11)**
Operating profit	**471**	522	**(9)**	**(10)**

Organic performance:

Economic weakness in a number of markets created an overall challenging environment for the Europe region. There were notable net sales declines in Greece, Iberia and to a lesser extent Ireland that led to declines in Johnnie Walker, J£B and Guinness. Russia, Eastern Europe and Germany performed well, led by the scotch and liqueur categories in Russia and Eastern Europe and by the scotch and rum categories in Germany. There was moderate net sales growth in Great Britain with strong price/mix improvement in wine. Negative price/mix was mainly due to the decline in scotch in Southern Europe and challenging trading conditions for Smirnoff in Great Britain. Whilst marketing spend was reduced in line with net sales in Greece and Iberia, overall spend in Europe increased 1%, reflecting a significant increase in Russia and Eastern Europe. Captain Morgan benefited from a double digit increase in marketing spend as the brand continued to perform strongly. Operating profit declined 9%, driven by economic weakness in Southern Europe and margin decline in Great Britain.

	Volume movement* %	Organic net sales movement %	Reported net sales movement %
By market:			
Great Britain	(1)	1	1
Ireland	(1)	(5)	(12)
Iberia	(13)	(14)	(19)
Greece	(35)	(38)	(42)
Russia	9	31	36
By category:			
Spirits	(2)	(5)	(7)
Beer	(5)	(4)	(9)
Wine	(2)	17	8
Ready to drink	(4)	(8)	(9)
Strategic brands:**			
Johnnie Walker	(5)	(5)	(7)
Smirnoff	(6)	(15)	(16)
Baileys	1	(2)	(4)
J£B	(6)	(10)	(14)
Captain Morgan	37	45	44
Guinness	(6)	(5)	(7)

* Volume movement is both reported and organic, except for wine where reported movement was (6)% primarily due to the disposal of Barton & Guestier and Ireland where reported movement was (3)% primarily due to the disposal of the Gilbeys wine business in Ireland

** Spirits brands excluding ready to drink

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The classification of brands as global priority brands and other brands has been discontinued for reporting purposes. Decreases in organic volume, reported volume, organic net sales and reported net sales for global priority brands are (3)%, (3)%, (5)% and (8)%, respectively, and for other brands (1)%, (2)%, (1)% and (5)%, respectively, against the comparable period last year.

Great Britain - Moderate net sales growth achieved as the economy continued its fragile recovery

In Great Britain, net sales grew as the market continued to be characterised by the shift from the on trade to the off trade. The spirits market was flat and Diageo spirits broadly maintained share, as a gain of 0.9 percentage points in the off trade offset a decline of 0.7 percentage points in the on trade. Net sales of Smirnoff were down 16% following customer stock building in fiscal 2010 ahead of the anticipated duty increase in the emergency budget in June and a loss of share in the on trade. Smirnoff also experienced negative price/mix as the on trade contracted and price conscious consumers in the off trade bought more on promotion. Net sales of Baileys grew 2% and gained 2.9 percentage points of share, the new Let s do this again campaign was launched in the half and marketing spend was flat. Guinness net sales declined 2%. Although Guinness Surger increased brand distribution into a further 9,500 outlets, this failed to offset the continued contraction of the on trade with, on average, 29 outlets closing each week. The brand achieved 3 percentage points of price/mix driven by a price increase taken in the prior year and customer mix. Wine net sales grew 18% as price increases on Blossom Hill combined with strong sales of the higher value en primeur wines drove strong price/mix. Marketing spend increased 3% and investment behind the total Smirnoff brand increased 4%, focused on the global Nightlife Exchange Project , and support behind Smirnoff innovations including Smirnoff and Cola and Smirnoff Flavours. Guinness marketing spend was down as the brand switched its sponsorship programme from the rugby premiership to the Six Nations and international rugby.

Ireland - Spirits outperformed beer as Guinness was impacted by further on trade declines

In Ireland volume fell slightly whilst net sales declined 5% driven by beer which represents over 80% of Diageo Ireland net sales. Net sales of total beer declined 6% and Guinness net sales declined 8% as the economic conditions continued to impact the market. Core consumers reduced their consumption frequency and the shift to the off trade accelerated resulting in a share loss on Guinness of 0.2 percentage points. However, spirits performed better as volume grew 2% and 3 percentage points of price/mix drove net sales growth to 5%. This was driven by share gains in a declining spirits market and a reduction in cross border trade. Captain Morgan grew net sales double digit and remained the fastest growing spirit brand in Ireland, gaining over 10 percentage points of share. Procurement efficiencies drove a 3% reduction in marketing spend whilst the reinvestment rate was broadly flat. Guinness marketing spend was up as the business focused on fewer, bigger events such as Arthur s Day and spend decreased behind Captain Morgan and Smirnoff.

Iberia - Further deterioration in the spirits market and consumer confidence is reflected in business performance

Volume in Iberia declined 13% and net sales decreased 14%. The business was impacted by further destocking which accounted for over a third of the volume decline, as customers experienced reduced financial liquidity and further declines in consumer confidence impacted demand. Volume of JεB fell 10% as the scotch category continued to decline. There was also price/mix dilution due to the increased volume sold through lower margin cash and carry and hypermarket customers. Johnnie Walker was impacted by some destocking with volume down 11% and net sales down 12%, however both Johnnie Walker Red Label and Johnnie Walker Black Label grew share in the declining scotch category in the six months to December 2010 and Diageo grew its share of total scotch in the off trade in the half. In the slow growth rum category, private label and value brands grew, as consumers sought greater value for money. As a result, Cacique volume and net sales were down 24% and 26% respectively. The gin category continued to decline whilst premium gin grew at the expense of local and standard gin brands. Tanqueray delivered double digit volume and net sales growth, whilst sacrificing 1 percentage point of price/mix following deeper and more frequent off trade promotions to increase competitiveness. This was supported by a print and digital campaign combined with the Mentor at Home programme. Support continued behind ready to serve cocktails with the launch of JεB Manhattan and the further roll out of draught Cacique Mojito. The packaged ready to serve segment has become more competitive with private label entrants, which has impacted price/mix. Marketing spend declined in line with net sales. Remaining spend focused on the new JεB kite surfing sponsorship, JεB Masters of Kite to drive relevance with consumers, a TV campaign to support the launch of JεB Manhattan and the national launch of Johnnie Walker s Walk with Giants campaign.

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Greece - The deteriorating economic conditions impacted the business in the first half

Lower disposable income due to the economic downturn and excise duty increases totalling 87% over the course of 2010 led to a 35% decline in volume in Greece and net sales fell 38%. Negative price/mix was a result of the higher margin on trade declining at a faster rate than the off trade and prices of some brands being reduced to maintain affordability. As part of a large scotch market, Johnnie Walker was significantly impacted as was Dimple, which declined sharply, as deluxe scotch was impacted more severely. With its strong brand equity, Haig proved more robust and the brand gained share although volume again declined. Outside of the scotch category, net sales of all other spirits declined. Marketing spend was maintained as a percentage of net sales and therefore reduced by 38%.

Russia and Eastern Europe - Recovery continued in Russia and signs of trading up returned

Russia and Eastern Europe combined delivered double digit volume and net sales growth. The strong growth of imported spirits and the benefit of price increases last year drove mix improvements. Johnnie Walker performed well across the region with increased net sales of 26%. In addition, White Horse and Bell s continued to perform well delivering double digit growth and Baileys achieved double digit net sales growth across the region. Vodka net sales declined 2% as growth of Smirnov in Russia and growth of Smirnoff in third party distributor markets in Eastern Europe failed to offset the decline of Smirnoff Vladimir in Poland. Marketing spend increased markedly, following lower levels of investment last year. Investment was focused behind the Johnnie Walker Walk with Giants campaign and Captain Morgan internet advertising.

Rest of Europe - Strong performance of scotch and rum across the rest of Europe

Import restrictions on Diageo Turkey resulted in no trading in the domestic channel in the half. Elsewhere in Europe Johnnie Walker Red Label performed very well in Germany, following a planned price reduction to maintain its competitive price positioning. A renewed focus behind JεB in France drove good growth, with the execution of JεB Colours . In Benelux Johnnie Walker and JεB grew double digit volume and net sales, however the benefit was diluted by negative channel mix. Net sales declined in the Nordics as the result of continued decline in the spirits market and the cessation of the Smirnoff Ice distribution contract in Denmark. Within other brand performance, Captain Morgan showed excellent growth across Northern Europe supported by a significant increase in marketing spend behind proven growth drivers.

International

Key highlights

- Increased marketing spend across the region and improved distribution in key markets drove volume growth of 9% and net sales growth of 13%

- In Latin America and the Caribbean, the strong performance of scotch brands delivered double digit volume growth and price/mix improvement

- In Africa the continued strong performance of beer in East Africa, Nigeria and Cameroon and the growth of scotch in South Africa drove net sales growth of 10%

- GTME benefitted from further increases in marketing investment along with innovation in both product and retail offerings which resulted in volume growth of 10% and net sales growth of 15%

- Marketing investment grew ahead of net sales, driving strong top line growth. Nevertheless, operating margins improved again

Key measures:	Six months ended 31 December 2010 Equivalent units million	Six months ended 31 December 2009 Equivalent units million	Organic movement %	Reported movement %
Volume	**22.7**	20.8	**9**	**9**
	£ million	**£ million**	**%**	**%**
Net sales	**1,415**	1,402	**13**	**1**
Marketing spend	**177**	150	**18**	**18**
Operating profit before exceptional items	**468**	460	**15**	**2**
Operating profit	**468**	457	**15**	**2**

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Organic performance:

International delivered another strong performance in the first half with all hubs generating double digit net sales growth. Performance in Latin America was driven by scotch, with increased marketing spend driving volume in Brazil and Mexico, and price increases in Mexico driving net sales. GTME performance was also driven by scotch, in particular by Johnnie Walker Black Label and the ongoing roll out of Johnnie Walker Double Black. Increased distribution and supply, and improving brand equities drove lager growth across Africa. Diageo beer brands gained volume share in Cameroon, Nigeria and Kenya, and in South Africa brandhouse gained share in spirits and beer, notably scotch.

	Volume movement* %	Organic net sales movement %	Reported net sales movement %
By market:			
Latin America and the Caribbean	10	17	(15)
Africa	9	10	13
GTME	10	15	21
By category:			
Spirits	13	17	(4)
Beer	5	10	11
Wine	16	24	10
Ready to drink	(8)		(6)
Strategic brands:**			
Johnnie Walker	21	25	19
Buchanan s	(7)	11	(39)
Smirnoff	15	22	26
Baileys	10	16	7
Guinness	1	2	4

* Volume movement was both reported and organic except for wine where reported movement was 6% primarily due to the disposal of Barton & Guestier.

** Spirits brands excluding ready to drink

The classification of brands as global priority brands and other brands has been discontinued for reporting purposes. Increases/(decreases) in organic and reported volume, organic net sales and reported net sales for global priority brands are 11%, 14% and 12%, respectively, and for other brands 8%, 12% and (10)%, respectively, against the comparable period last year.

Latin America and the Caribbean - Marketing investment increased 21%, driving growth in scotch

Continuing positive economic trends in Brazil translated into double digit growth for beverage alcohol. Volume increased 26%, net sales increased 30%, and Diageo s scotch portfolio grew share 6 percentage points in the deluxe segment and 2 percentage points in the standard segment. Johnnie Walker volume and net sales both grew double digits. This was in part due to price reductions made in the second half of fiscal 2010, but growth was also driven by geographic expansion and continued investment in brand building activities. Black & White and Old Parr also delivered strong net sales growth of 20% and 36% respectively. Smirnoff maintained its leadership position in the vodka category supported by the Be There campaign and the Smirnoff Nightlife Exchange Project . Smirnoff ready to drink grew net sales 4% on the back of strong volume performance from Smirnoff Ice and the re-launch of Smirnoff Caipiroska with a new product formula and packaging.

Despite the relatively slow economic recovery in Mexico and ongoing security concerns, price increases on key brands and accelerated marketing spend drove 23% net sales growth. Increased investment behind the Strides and Join the Pact campaigns on Johnnie Walker Black Label, and on trade activities such as Adventure in a Glass for Johnnie Walker Red Label resulted in the highest awareness scores recorded for the brand in Mexico. All Johnnie Walker variants posted double digit net sales growth. Buchanan s share declined in the face of heavy competitive price reductions and liquid promotions, but positive price/mix fuelled 18% net sales growth.

The trading performance in Venezuela was impacted by the currency exchange restrictions which have constrained supply. Reported net sales and operating profit were therefore down significantly, although after adjusting for the year on year exchange impact Diageo generated organic operating profit growth in Venezuela.

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Africa - Improved distribution led to strong net sales growth in lager, and key spirits segments returned to growth

Net sales in Nigeria grew 10%, propelled by the double digit growth of Harp. Reduced stock outs and advertising campaigns increased trade and consumer confidence in the brand as demonstrated by volume growth of 19% despite two price increases in the first half. Malta Guinness continued to benefit from the bottle re-launch and improved distribution, which drove net sales growth of 18%. Guinness volume was up slightly, but net sales were flat due to the focus on the 45cl pack size. Smirnoff Ice performed well as off trade momentum behind the can format increased distribution and drove 34% net sales growth.

The East Africa hub delivered 12% volume growth and 10% net sales growth as the economy continued to recover. Negative price/mix was driven by a significant increase in duties which caused consumers to shift into value spirits and beer. However, Guinness net sales were up 6% despite price increases on the back of excise duty increases. Improved distribution increased Senator volume which in turn drove 17% net sales growth. Tusker also delivered strong results growing net sales 15% as a result of volume growth in Uganda and price increases.

In South Africa, net sales grew in line with volume with both up 5% driven primarily by scotch. Johnnie Walker Red Label delivered a particularly strong performance, with increased distribution and marketing investment driving 14% net sales growth. Johnnie Walker Black Label volume and net sales grew 9% and 3% respectively, driven by upweighted promotional activity. Bell s net sales grew 13% as improved consumer confidence and a strong festive season advertising campaign positioned the brand as an affordable luxury. Smirnoff volume was up 4% but price/mix was negative due to increased promotional activity. In total, the brandhouse venture grew share of both spirits and beer.

Elsewhere in Africa, Guinness volume in Ghana declined due to January 2010 excise duty and price increases, but double digit net sales growth from Star and Gulder lagers and non-alcoholic Alvaro, and significant growth in spirits compensated for Guinness performance. In Cameroon, a focus on improving the route to market and sales execution drove strong Guinness volume growth and net sales grew 18%.

Global Travel and Middle East - Marketing investment increased as passenger numbers recovered, with Johnnie Walker leading continued net sales growth

GTME delivered volume growth of 10% and net sales growth of 15% as marketing investment was upweighted on the back of the recovery in passenger numbers. The increased level of marketing spend reflects the important role GTME plays as a brand and category building channel. Johnnie Walker drove performance with 22% net sales growth. The Step Inside the Circuit campaign, a programme to encourage consumers into stores, the continuation of the Walk with Giants marketing campaign, and the ongoing roll out of Johnnie Walker Double Black all contributed to the brand s success. The largest non-scotch brands, Baileys, Smirnoff, Tanqueray and Captain Morgan all grew volume and net sales, and innovation continued to play a significant role in driving growth.

Asia Pacific

Key highlights

- Top line improvement was led by the emerging markets of Asia, which grew net sales 15% driven by India, Thailand, Malaysia and Vietnam, together with 9% growth in Korea

- Diageo strengthened its leadership position in scotch across the region gaining share in all markets
- Johnnie Walker was the key driver of performance, supported by double digit net sales growth on Windsor and The Singleton
- There was a strong performance in Korea with share gains in the scotch category
- In Australia, Diageo gained share in spirits and ready to drink, but net sales declined due to a more aggressive off trade pricing environment
- Marketing spend grew ahead of net sales, focused on Johnnie Walker in emerging markets
- Operating margin increased as higher marketing spend was more than offset by lower overheads

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Key measures:	Six months ended 31 December 2010 Equivalent units million	Six months ended 31 December 2009 Equivalent units million	Organic movement %	Reported movement %
Volume	**6.8**	6.4	**8**	**6**

	£ million	£ million	%	%
Net sales	**616**	523	**7**	**18**
Marketing spend	**143**	118	**10**	**21**
Operating profit before exceptional items	**129**	103	**18**	**25**
Operating profit	**129**	98	**18**	**32**

Organic performance:

Emerging markets were the key driver of net sales growth in Asia Pacific, growing 15% in total. By category, growth was led by scotch and the three largest brands, Johnnie Walker, Windsor and The Singleton all grew net sales in double digits. Diageo strengthened its leadership in the scotch category in Asia Pacific by growing share in the major markets of Korea, Thailand, Australia, India, Taiwan and China. The Smirnoff trademark grew 17% in total as the very strong growth of ready to drink added to 6% growth on Smirnoff spirits. The rum and beer categories also contributed to growth. Premiumisation was evident in the half with the premium and above price segments growing twice as fast as standard and below. This positive mix impact was offset by price reductions taken in Australia and China and negative market mix from strong volume growth in India and South East Asia. Marketing spend increased ahead of net sales, focused on driving sales of Johnnie Walker and Smirnoff by trading up increasingly affluent emerging market consumers into international spirits. Overheads were reduced resulting in operating profit growth of 18%.

	Volume movement* %	Organic net sales movement %	Reported net sales movement %
By market:			
Australia	3	(1)	12
Korea	4	9	18
China	(2)	(3)	2
India	67	134	34
By category:			
Spirits	9	9	20
Beer	2	6	18
Wine	21	44	(5)
Ready to drink	6	2	16
Strategic brands:**			
Johnnie Walker	17	12	22
Smirnoff	11	6	18
Baileys	10	(12)	(3)
Windsor	6	11	20
Guinness	(3)	3	13

* Volume movement is both reported and organic except for wine where the reported movement was (28)% primarily due to the disposal of Barton & Guestier

** Spirits brands excluding ready to drink

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The classification of brands as global priority brands and other brands has been discontinued for reporting purposes. Increases in organic volume, reported volume, organic net sales and reported net sales for global priority brands are 13%, 13%, 9% and 20%, respectively, and for other brands 1%, 0%, 4% and 15%, respectively, against the comparable period last year.

Australia - Gained share of spirits and ready to drink in a challenging market

Although the macro economic prospects look positive for Australia, the beverage alcohol market continued to be challenging. Price/mix was negative as a result of selective price reductions in the most competitive categories and the continued shift of sales to the larger off trade retailers. Diageo grew share in total due primarily to an increased focus on customer marketing activities with the largest off trade accounts and the continuation of a successful innovation programme. A key success in the half was the introduction into the market of Smirnoff Signature Serves and Smirnoff Cocktails which have provided net sales growth for Diageo and have re-invigorated the segment for retailers and consumers alike.

Korea - Share gains and a price increase on Windsor delivered a strong performance

Diageo Korea outperformed a broadly flat scotch market. Windsor extended its position as the leading brand by 1 percentage point driven by the strong performance of Windsor 12. A price increase on the brand taken in September 2010 drove 5 percentage points of positive price/mix. Diageo Korea continued its strategy to grow the brand range beyond blended scotch whisky, primarily investing behind Guinness, which received its first television campaign, and launching super premium products: Classic Malts, Ketel One vodka and Zacapa rum.

South East Asia - Double digit net sales growth led by Johnnie Walker

South East Asia again performed strongly. In Thailand, the economic recovery and increased brand building activities behind Johnnie Walker led to 19% net sales growth. There was continued strong momentum in Vietnam, particularly at the premium and above price segments, led by Johnnie Walker and The Singleton. Beer net sales grew 9%, driven primarily by Guinness in Malaysia as a result of a successful Arthur s Day campaign and increased on trade activity.

China - Share gains in scotch offset by lower volumes in other categories

Johnnie Walker volume grew 9% and the brand made share gains in the key deluxe and super deluxe segments. However, there was negative price/mix as last year s price increases were reversed, reflecting the highly competitive on trade environment. The total net sales decline of 3% was driven by higher trade investment behind Johnnie Walker Black Label, lower volumes of Smirnoff in a weak vodka category and the discontinuation of JεB. There was an increase in marketing spend behind super deluxe scotch, targeted to capture the increasing preference of Chinese consumers for super premium products. This helped drive net sales growth of 22% and share gains in this segment.

India - Strong growth of key brands enhanced by route to market changes

The first half was the first full period in which the new route to market structure was in place. All imported brands are now distributed by Diageo India. In the prior period Diageo did not record any sales of imported brands as the stocks held by the former third party distributor were reduced. India therefore delivered strong top and bottom line growth and there was a return to strong marketing spend behind key brands. A new Johnnie Walker brand campaign was launched in the period focusing on building the brand s quality credentials through mentoring sessions. Increased investment on Smirnoff behind the Nightlife Exchange Project and on the launch of a new bottle for VAT69 delivered significant double digit net sales growth for these key brands. Diageo gained 2 percentage points of share of scotch in the Duty Free Channel as depletions grew strongly in key airports.

Corporate revenue and costs

Net sales were £38 million in the six months ended 31 December 2010, down £2 million from £40 million in the comparable prior period. Net operating charges were £64 million in the six months ended 31 December 2010. This was a reduction of £63 million over the prior period. Diageo undertakes the majority of its currency transaction hedging centrally and therefore £98 million of positive year on year transaction impact was taken to corporate in this half. There was an incremental charge of £39 million relating to the difference between budget and achieved rates arising in the period as the results of the four regions are reported using budget transaction exchange rates. There was a £4 million reduction in underlying corporate costs.

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Liquidity and capital resources

Cash flow

A summary of the consolidated cash flow and reconciliation to movement in net borrowings for the six months ended 31 December 2010 compared to the six months ended 31 December 2009 is as follows:

		Six months ended 31 December
	2010	**2009**
	£ million	**£ million**
Operating profit	**1,718**	1,536
Depreciation and amortization	**144**	159
Movement in working capital	**(509)**	(72)
Dividend income and other items	**(29)**	(54)
Cash generated from operations	**1,324**	1,569
Net interest paid	**(176)**	(217)
Dividends paid to equity non-controlling interests	**(75)**	(55)
Taxation paid	**(150)**	(198)
Net cash from operating activities	**923**	1,099
Net capital expenditure	**(129)**	(150)
Net purchase of investments	**(19)**	(45)
Free cash flow	**775**	904
Acquisitions and disposals	**(32)**	(11)
Net sale/(purchase) of own shares for share schemes	**(29)**	41
Net equity dividends paid	**(586)**	(551)
Exchange adjustments	**(35)**	(201)
Borrowings acquired through purchase of businesses	**(15)**	
Non-cash items	**(134)**	(67)
(Increase)/decrease in net borrowings	**(56)**	115
Net borrowings at beginning of the period	**(6,954)**	(7,419)
Net borrowings at end of the period	**(7,010)**	(7,304)

The primary source of the group s liquidity has been cash generated from operations. These funds have generally been used to pay interest, taxes and dividends, and to fund capital expenditure and acquisitions.

Net cash from operating activities Cash generated from operations decreased from £1,569 million in the six months ended 31 December 2009 to £1,324 million in the six months ended 31 December 2010. The reduction of £245 million primarily arose from a decrease of £437 million in cash flows from net movements in working capital driven by a higher seasonal increase compared with the same period last year, partly offset by £182 million increase in operating profit. Cash generated from operations is after exceptional restructuring costs of £67 million (2009 - £76 million). Other items include £37 million of cash contributions to post employment schemes in excess of the income statement charge (2009 - £54 million higher contributions) and fair value movement in respect of dedesignated cash flow hedges charged to operating profit of £6 million (2009 - £26 million outflow) partly offset by the fair value charge in respect of share-based incentive plans of £16 million (2009 - £16 million). Net interest paid in the six months ended 31 December 2010 was £41 million lower than the six months ended 31 December 2009 driven by £32 million favourable phasing of bond coupon payments and £17 million positive impact of lower average net borrowings during the period partially offset by £6 million lower upfront cash premium received on the renegotiation of the terms of certain interest rate swaptions. Tax payments in the six months ended 31 December 2010 were lower than in the same period last year primarily as a result of settlements agreed with tax authorities paid over the previous two years.

Net cash from investing activities The purchase of tangible fixed assets and computer software increased from £153 million in the six months ended 31 December 2009 to £173 million in six months ended 31 December 2010 driven by increased payments due to supply changes to drive efficiencies primarily in Europe. Property disposals increased from £3 million in the six months ended 31 December 2009 to £44 million in the six months ended 31 December 2010 due to the receipt of £22 million on the sale and leaseback of land and buildings and £15 million on the sale of vineyards located in Napa Valley, California.

In the six months ended 31 December 2010 cash outflows of £51 million arose in respect of business acquisitions. This included £39 million in respect of 51% equity stake in Serengeti Breweries Limited, a company in Tanzania.

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Free cash flow Free cash flow decreased by £129 million to £775 million in the six months ended 31 December 2010 compared to the same period last year. Free cash flow comprises net cash flow from operating activities and net cash from investing activities apart from cash payments and receipts arising from the purchase and disposal of subsidiaries, associates and businesses.

Cash flows from financing activities Cash flows from financing activities included the payments to purchase treasury shares for scheme hedging of £57 million (2009 - £2 million) less receipts from employees on the exercise of share options of £28 million (2009 - £43 million). Equity dividends paid increased from £551 million in the six months ended 31 December 2009 to £586 million in the six months ended 31 December 2010.

Capital structure The group s management is committed to enhancing shareholder value in the long term, both by investing in the businesses and brands so as to improve the return on investment and by managing the capital structure. Diageo manages its capital structure to achieve capital efficiency, maximise flexibility and give the appropriate level of access to debt markets at attractive cost levels. This is achieved by targeting a range of ratios which are currently broadly consistent with an A band credit rating. Diageo would consider modifying these ratios in order to effect strategic initiatives within its stated goals, which could have an impact on its rating.

Capital repayments The group regularly assesses its debt and equity capital levels against its stated policy for capital structure.

Authorisation was given by shareholders on 14 October 2010 to purchase a maximum of 250,554,000 shares at a minimum price of 28101/108 pence and a maximum price of the higher of (a) 105% of the average of the middle market quotations for an ordinary share for the five preceding business days and (b) the higher of the price of the last independent trade and the highest current independent bid on the London Stock Exchange at the time the purchase is carried out. The expiration date for the programme is 19 October 2011.

Borrowings The group policy with regard to the expected maturity profile of borrowings of group finance companies is to limit the proportion of such borrowings maturing within 12 months to 50% of gross borrowings less money market demand deposits, and the level of commercial paper to 30% of gross borrowings less money market demand deposits. In addition, it is group policy to maintain backstop facility terms from relationship banks to support commercial paper obligations.

The group s net borrowings and gross borrowings in the tables below are measured at amortised cost with the exception of borrowings designated in fair value hedge relationships, interest rate hedging instruments and foreign currency swaps and forwards. For borrowings designated in fair value hedge relationships, Diageo recognises a fair value adjustment for the risk being hedged in the balance sheet, whereas interest rate hedging instruments and foreign currency swaps and forwards are measured at fair value. Net borrowings, reported on this basis, comprise the following:

	31 December 2010 £ million
Overdrafts	**(79)**
Other borrowings due within one year	**(715)**
Borrowings due within one year	**(794)**
Borrowings due between one and three years	**(2,946)**

Borrowings due between three and five years	**(2,261)**
Borrowings due after five years	**(2,640)**
Interest rate fair value hedging instruments	**44**
Cross currency interest rate swaps	**178**
Foreign currency swaps and forwards	**(7)**
Finance lease obligations	**(56)**
Gross borrowings	**(8,482)**
Offset by:	
Cash and cash equivalents	**1,472**
Net borrowings	**(7,010)**

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The group s gross borrowings and cash and cash equivalents at 31 December 2010 were denominated in the following currencies:

	Total £ million	US dollar %	Sterling %	Euro %	Other %
Gross borrowings (including foreign exchange forwards and swaps and finance lease obligations)	**(8,482)**	**43**	**21**	**24**	**12**
Cash and cash equivalents	**1,472**	**58**	**5**	**11**	**26**

The effective interest rate for the six months ended 31 December 2010, based on average net borrowings (excluding interest rate related fair value adjustments) and interest charge was 4.9%. For this calculation, the interest charge excludes finance charges unrelated to net borrowings, the forward element on derivative financial instruments and fair value adjustments to interest rate swaps and borrowings.

Diageo did not issue any bonds in the six months ended 31 December 2010 and no bond or medium term note was repaid.

The £56 million increase in net borrowings from 30 June 2010 to 31 December 2010 principally includes the free cash inflow of £775 million offset by £586 million equity dividend paid and adverse non-cash movements of £134 million comprising predominantly fair value movements.

The group had available undrawn committed bank facilities as follows:

	As at 31 December 2010 £ million
Expiring within one year	**693**
Expiring between one and two years	**1,551**
	2,244

Commitment fees are paid on the undrawn portion of these facilities. Borrowings under these facilities will be at prevailing LIBOR rates (dependent on the period of drawdown) plus an agreed margin. These facilities can be used for general corporate purposes and, together with cash and cash equivalents, support the group s commercial paper programmes. The committed bank facilities are subject to a single financial covenant, being a minimum interest cover ratio of two times (defined as the ratio of operating profit aggregated with share of associates profits to net interest). They are also subject to pari passu ranking and negative pledge covenants.

Any non-compliance with covenants underlying Diageo s financing arrangements could, if not waived, constitute an event of default with respect to any such arrangements, and any non compliance with covenants may, in particular circumstances, lead to an acceleration of maturity on certain notes and the inability to access committed facilities. Diageo was in full compliance with all of its financial covenants throughout each of the periods presented.

Diageo management believes that it has sufficient funding for its working capital requirements.

Off-balance sheet arrangements

Neither Diageo plc nor any member of the Diageo group has any off-balance sheet financing arrangements that currently have or are reasonably likely to have a material future effect on the group s financial condition, changes in financial condition, results of operations, liquidity, capital expenditure or capital resources.

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NEW INTERNATIONAL FINANCIAL REPORTING STANDARDS

A number of IFRS standards and interpretations have been issued by the IASB or IFRIC. Those that are of relevance to the group are discussed in note 1 to the unaudited condensed consolidated financial statements.

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RECENT DEVELOPMENTS

Paul Walsh, Chief Executive of Diageo, commenting on the six months ended 31 December 2010 said:

Momentum is building in our business. Our top line performance was stronger and price/mix improved. We have increased marketing spend significantly, up 10%, but in a very focused way. 35% of the increase was behind strategic brands in US spirits to build the brand equity as we move away from promotional support and over 60% of the increase was on our brands in the faster growing emerging markets. Despite the economic weakness in much of Europe, our first half performance gives me increased confidence that we will improve on the organic operating profit growth we delivered in fiscal 2010 .

The above comments were made by Paul Walsh, Chief Executive of Diageo, in connection with the release of the Interim Announcement published on 10 February 2011.

The following developments have occurred since the unaudited condensed consolidated financial information was approved by the board of directors on 9 February 2010.

On 12 February 2011, the Turkish parliament voted to approve the proposed legislation to restructure its public receivables law, which will allow the settlement of outstanding tax claims (including with respect to customs duties). The law will become effective upon signature by Turkey s president. Taxpayers wishing to avail themselves of this new law have a period of two months to file appropriate applications with the relevant authorities. Once the law becomes effective, Diageo will evaluate its position under the new legislation.

Litigation is ongoing at the Korean Tax Tribunal in connection with the application of the methodology used in transfer pricing on spirits imports since 2004 as described in note 13 to the financial statements on Contingent liabilities and legal proceedings . On 15 February 2011, Diageo Korea received a pre-imposition notice from the Korean customs authorities regarding a second customs audit, covering the period from 29 February 2008 to 31 October 2010, for Korean won 207 billion or approximately £118 million (including £14 million of value added tax). Diageo Korea has the right to appeal this pre-imposition notice before a final customs audit assessment notice is issued, and Diageo Korea intends to make this appeal. Following the receipt of any final customs audit assessment notice, Diageo Korea would be required to pay the full assessment amount in order to preserve its right to appeal to the Korean Tax Tribunal. Diageo Korea is unable to quantify meaningfully the possible loss or range of loss to which these claims may give rise. Diageo Korea intends to defend its position vigorously.

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INDEX TO THE UNAUDITED CONDENSED FINANCIAL INFORMATION

FOR THE SIX MONTHS ENDED 31 DECEMBER 2010 AND 31 DECEMBER 2009

The unaudited condensed consolidated financial information was approved by the board of directors on 9 February 2011.

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UNAUDITED CONDENSED CONSOLIDATED INCOME STATEMENT

	Notes	Six months ended 31 December 2010 £ million	Six months ended 31 December 2009 £ million
Sales	2	**7,132**	6,928
Excise duties		**(1,812)**	(1,721)
Net sales	2	**5,320**	5,207
Cost of sales		**(2,072)**	(2,123)
Gross profit		**3,248**	3,084
Marketing expenses		**(813)**	(725)
Other operating expenses		**(717)**	(823)
Operating profit	2, 3	**1,718**	1,536
Sale of businesses	3	**(1)**	
Net interest payable	4	**(196)**	(197)
Net other finance charges	4	**(13)**	(40)
Share of associates profits after tax		**104**	94
Profit before taxation		**1,612**	1,393
Taxation	5	**(352)**	(310)
Profit from continuing operations		**1,260**	1,083
Discontinued operations	6		(10)
Profit for the period		**1,260**	1,073
Attributable to:			
Equity shareholders of the parent company		**1,194**	1,016
Non-controlling interests		**66**	57
		1,260	1,073
Pence per share			
Basic earnings		**47.9p**	40.9p
Diluted earnings		**47.8p**	40.8p
Average shares		**2,492m**	2,482m

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UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF

COMPREHENSIVE INCOME

	Six months ended 31 December 2010 £ million	**Six months ended 31 December 2009 £ million**
Exchange differences on translation of foreign operations excluding borrowings	**7**	302
Exchange differences on borrowings and derivative net investment hedges	**(34)**	(201)
Effective portion of changes in fair value of cash flow hedges		
net losses taken to other comprehensive income	**(20)**	(69)
transferred to income statement	**29**	36
Net actuarial gain on post employment plans	**342**	176
Tax on other comprehensive income	**(83)**	(56)
Other comprehensive income for the period	**241**	188
Profit for the period	**1,260**	1,073
Total comprehensive income net of tax for the period	**1,501**	1,261
Attributable to:		
Equity shareholders of the parent company	**1,470**	1,187
Non-controlling interests	**31**	74
	1,501	1,261

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UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEET

	Notes	31 December 2010 £ million	£ million	30 June 2010 £ million	£ million	31 December 2009 £ million	£ million
Non-current assets							
Intangible assets		**6,661**		6,726		6,355	
Property, plant and equipment		**2,456**		2,404		2,390	
Biological assets		**29**		30		38	
Investments in associates		**2,268**		2,060		2,226	
Other investments		**139**		117		130	
Other receivables		**20**		115		18	
Other financial assets		**341**		472		261	
Deferred tax assets		**359**		529		594	
Post employment benefit assets		**57**		49		45	
			12,330		12,502		12,057
Current assets							
Inventories	7	**3,401**		3,281		3,279	
Trade and other receivables		**2,670**		2,008		2,596	
Assets held for sale	10	**63**		112			
Other financial assets		**63**		98		105	
Cash and cash equivalents	8	**1,472**		1,453		1,589	
			7,669		6,952		7,569
Total assets			**19,999**		19,454		19,626
Current liabilities							
Borrowings and bank overdrafts	8	**(794)**		(587)		(891)	
Other financial liabilities		**(139)**		(186)		(154)	
Trade and other payables		**(2,804)**		(2,615)		(2,738)	
Liabilities held for sale	10	**(5)**		(10)			
Corporate tax payable		**(417)**		(391)		(604)	
Provisions		**(174)**		(155)		(196)	
			(4,333)		(3,944)		(4,583)
Non-current liabilities							
Borrowings	8	**(7,847)**		(8,177)		(8,202)	
Other financial liabilities		**(140)**		(155)		(97)	
Other payables		**(54)**		(76)		(26)	
Provisions		**(258)**		(318)		(355)	
Deferred tax liabilities		**(825)**		(744)		(672)	
Post employment benefit liabilities		**(892)**		(1,254)		(1,100)	
			(10,016)		(10,724)		(10,452)
Total liabilities			**(14,349)**		(14,668)		(15,035)
Net assets			**5,650**		4,786		4,591
Equity							
Called up share capital		**797**		797		797	
Share premium		**1,342**		1,342		1,342	
Other reserves		**3,258**		3,245		3,331	
Retained deficit		**(511)**		(1,377)		(1,603)	
Equity attributable to equity shareholders of the parent company			**4,886**		4,007		3,867
Non-controlling interests			**764**		779		724
Total equity			**5,650**		4,786		4,591

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UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Share capital £ million	Share premium £ million	Other reserves £ million	Own shares £ million	Retained earnings/(deficit) Other retained earnings £ million	Total £ million	Equity attributable to parent company shareholders £ million	Non-controlling interests £ million	Total equity £ million
At 30 June 2010	**797**	**1,342**	**3,245**	**(2,253)**	**876**	**(1,377)**	**4,007**	**779**	**4,786**
Total comprehensive income			13		1,457	1,457	1,470	31	1,501
Employee share schemes				(26)	(3)	(29)	(29)		(29)
Share-based incentive plans					17	17	17		17
Tax on share-based incentive plans					7	7	7		7
Acquisitions								29	29
Dividends paid					(586)	(586)	(586)	(75)	(661)
At 31 December 2010	**797**	**1,342**	**3,258**	**(2,279)**	**1,768**	**(511)**	**4,886**	**764**	**5,650**
At 30 June 2009	797	1,342	3,279	(2,342)	93	(2,249)	3,169	705	3,874
Total comprehensive income			52		1,135	1,135	1,187	74	1,261
Employee share schemes				44	(1)	43	43		43
Share-based incentive plans					16	16	16		16
Tax on share-based incentive plans					3	3	3		3
Dividends paid					(551)	(551)	(551)	(55)	(606)
At 31 December 2009	797	1,342	3,331	(2,298)	695	(1,603)	3,867	724	4,591

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UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

		Six months ended 31 December 2010		Six months ended 31 December 2009
	£ million	£ million	£ million	£ million
Cash flows from operating activities				
Cash generated from operations (see note 12)	**1,324**		1,569	
Interest received	**133**		156	
Interest paid	**(309)**		(373)	
Dividends paid to equity non-controlling interests	**(75)**		(55)	
Taxation paid	**(150)**		(198)	
Net cash from operating activities		**923**		1,099
Cash flows from investing activities				
Disposal of property, plant and equipment and computer software	**44**		3	
Purchase of property, plant and equipment and computer software	**(173)**		(153)	
Net increase in other investments	**(19)**		(45)	
Disposal of businesses	**19**		1	
Purchase of businesses	**(51)**		(12)	
Net cash outflow from investing activities		**(180)**		(206)
Cash flows from financing activities				
Net (purchase)/sale of own shares for share schemes	**(29)**		41	
Net (decrease)/increase in loans	**(68)**		299	
Equity dividends paid	**(586)**		(551)	
Net cash outflow from financing activities		**(683)**		(211)
Net increase in net cash and cash equivalents		**60**		682
Exchange differences		**(65)**		(1)
Net cash and cash equivalents at beginning of the period		**1,398**		846
Net cash and cash equivalents at end of the period		**1,393**		1,527
Net cash and cash equivalents consist of:				
Cash and cash equivalents		**1,472**		1,589
Bank overdrafts		**(79)**		(62)
		1,393		1,527

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NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL INFORMATION

1. Basis of preparation

The financial information included within this report has been prepared using accounting policies in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and as endorsed and adopted for use in the European Union, and in accordance with the Disclosure and Transparency Rules (DTR) of the Financial Services Authority. The condensed consolidated financial statements have been prepared in accordance with IAS 34 - Interim Financial Reporting. This interim condensed consolidated financial information is unaudited and has been prepared on the basis of accounting policies consistent with those applied in the consolidated financial statements for the year ended 30 June 2010 except as noted below. IFRS is subject to ongoing review and endorsement by the EU or possible amendment by interpretative guidance from the IASB.

(a) Adopted by the group The following accounting standards and interpretations, issued by the International Accounting Standards Board (IASB) or International Financial Reporting Interpretations Committee (IFRIC), are effective for the first time in the current financial year and have been adopted by the group with no significant impact on its consolidated results or financial position:

Amendment to IAS 1 - Classification of the liability component of a convertible instrument

Amendment to IAS 7 - Classification of expenditures on unrecognised assets

Amendment to IAS 17 - Classification of leases of land and buildings

Amendment to IAS 27 - Consolidated and separate financial statements

Amendment to IAS 32 - Financial instruments: presentation - Classification of rights issues

Amendment to IAS 36 - Cash generating units

Amendments to IAS 39 - Financial instruments: recognition and measurement

Amendment to IFRS 2 - Group cash-settled share-based payment transactions

Amendment to IFRS 3 - Business combinations

Amendment to IFRS 5 - Non-current assets held for sale and discontinued operations

Amendment to IFRS 8 - Segment information with respect to total assets

IFRIC 19 - Extinguishing financial liabilities with equity instruments

(b) Not adopted by the group The following standards, amendments and interpretations issued by the IASB or IFRIC have not yet been adopted by the group. The group currently believes that the adoption of these standards or interpretations would not have a material impact on the consolidated results or financial position of the group. These standards, amendments and interpretations are effective for annual periods beginning on or after 1 January 2011 unless otherwise stated.

Amendment to IAS 1 - Presentation of financial statements

Limited scope amendment to IAS 12 - Income taxes (effective for annual periods beginning on or after 1 January 2012)

IAS 24 (Revised) - Related party disclosures

Amendment to IAS 34 - Interim financial reporting

Amendment to IFRS 7 - Financial instruments: disclosures

IFRS 9 - Financial instruments (effective for annual periods beginning on or after 1 January 2013)

Amendment to IFRIC 13 - Customer loyalty programmes

Amendment to IFRIC 14 - IAS 19: The limit on defined benefit assets, minimum funding requirements and their interaction

With the exception of *IAS 24 (Revised)* and the *Amendment to IFRIC 14*, none of the above standards and interpretations not yet adopted by Diageo has been endorsed or adopted for use in the European Union.

The comparative figures for the financial year ended 30 June 2010 are not the company s statutory accounts for that financial year. Those accounts have been reported on by the company s auditor and delivered to the registrar of companies. The report of the auditor was (i) unqualified, (ii) did not include a reference to any matters to which the auditor 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.

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2. Segmental analysis

The executive committee considers the business principally from a geographical perspective and the business analysis is presented under the operating segments of North America, Europe, International and Asia Pacific. In addition to these geographical selling segments, a further segment reviewed by the executive committee is Global Supply which manufactures and distributes premium drinks within the group. Continuing operations also include the Corporate function. In view of the focus on the geographical segments in explaining the group s performance in the Business review, the results of the Global Supply segment have, in order to provide additional reconciling information, been allocated to the geographical segments. This gives an additional basis of presenting the group s performance and results on the basis of the location of third party customers. Corporate revenues and costs are in respect of central costs, including finance, human resources and legal, as well as certain information systems, facilities and employee costs that do not relate to the geographical segments or to Global Supply and hence are not allocated. They also include rents receivable in respect of properties not used by Diageo in the manufacture, sale or distribution of premium drinks and the results of Gleneagles Hotel. The group also owns a 34% interest in Moët Hennessy which is based in France and accounted for as an associate.

The segmental information for net sales and operating profit is reported at budgeted exchange rates in line with internal reporting. For management reporting purposes Diageo measures the current period at, and restates the prior period net sales and operating profit to, the current year s budgeted exchange rates. These exchange rates are set prior to the financial year as part of the financial planning process and provide a consistent exchange rate to measure the performance of the business throughout the year. The adjustments required to retranslate the segmental information to actual exchange rates and to reconcile it to Diageo s reported results are shown in the tables below. The comparative segmental information, prior to re-translation, has not been restated at the current year s budgeted exchange rates but is presented at the budgeted rates for the year ended 30 June 2010.

In addition, for management reporting purposes Diageo excludes the impact on net sales and operating profit of acquisitions and disposals completed in the current and prior period from the results of the geographical segments in order to provide comparable results. The impact of acquisitions and disposals has been allocated to the appropriate geographical segments in the tables below. These acquisitions and disposals are the same as those disclosed in the organic growth reconciliations but for management reporting purposes they are disclosed here at budgeted exchange rates.

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2. Segmental analysis (continued)

Six months ended 31 December 2010	North America £ million	Europe £ million	International £ million	Asia Pacific £ million	Global Supply £ million	Eliminate inter-segment sales £ million	Total operating segments £ million	Corporate and other £ million	Total £ million
Sales	**2,094**	**2,312**	**1,773**	**915**	**1,411**	**(1,411)**	**7,094**	**38**	**7,132**
Net sales									
At budgeted exchange rates*	**1,770**	**1,428**	**1,415**	**562**	**1,468**	**(1,413)**	**5,230**	**38**	**5,268**
Acquisitions and disposals	**13**	**4**		**1**			**18**		**18**
Global Supply allocation	**16**	**26**	**8**	**5**	**(55)**				
Retranslation to actual exchange rates	**8**	**(14)**	**(8)**	**48**	**(2)**	**2**	**34**		**34**
Net sales	**1,807**	**1,444**	**1,415**	**616**	**1,411**	**(1,411)**	**5,282**	**38**	**5,320**
Operating profit/(loss)									
At budgeted exchange rates*	**683**	**435**	**489**	**121**	**92**		**1,820**	**(93)**	**1,727**
Acquisitions and disposals	**1**		**(3)**	**(3)**			**(5)**		**(5)**
Global Supply allocation	**40**	**40**	**8**	**4**	**(92)**				
Retranslation to actual exchange rates	**(1)**	**(4)**	**(26)**	**7**			**(24)**	**29**	**5**
Operating profit/(loss) before exceptional items	**723**	**471**	**468**	**129**			**1,791**	**(64)**	**1,727**
Exceptional restructuring costs					**(9)**		**(9)**		**(9)**
Operating profit/(loss)	**723**	**471**	**468**	**129**	**(9)**		**1,782**	**(64)**	**1,718**
Sale of businesses									**(1)**
Net finance charges									**(209)**
Share of associates profits									
- Moët Hennessy									**106**
- Other associates									**(2)**
Profit before taxation									**1,612**

* These items represent the IFRS 8 performance measures for the geographic and Global Supply segments.

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2. Segmental analysis (continued)

Six months ended 31 December 2009	**North America £million**	**Europe £million**	**International £million**	**Asia Pacific £million**	**Global Supply £million**	**Eliminate inter-segment sales £million**	**Total operating segments £million**	**Corporate and other £million**	**Total £million**
Sales	1,969	2,456	1,726	737	1,391	(1,391)	6,888	40	6,928
Net sales									
At budgeted exchange rates*	1,596	1,405	1,327	490	1,375	(1,319)	4,874	38	4,912
Acquisitions and disposals	26	4					30		30
Global Supply allocation	9	31	9	7	(56)				
Retranslation to actual exchange rates	64	107	66	26	72	(72)	263	2	265
Net sales	1,695	1,547	1,402	523	1,391	(1,391)	5,167	40	5,207
Operating profit/(loss)									
At budgeted exchange rates*	614	470	458	95	65		1,702	(95)	1,607
Acquisitions and disposals	(1)	1							
Global Supply allocation	30	33	6	1	(70)				
Retranslation to actual exchange rates	24	24	(4)	7	5		56	(32)	24
Operating profit/(loss) before exceptional items	667	528	460	103			1,758	(127)	1,631
Exceptional items	(6)	(6)	(3)	(5)	(74)		(94)	(1)	(95)
Operating profit/(loss)	661	522	457	98	(74)		1,664	(128)	1,536
Net finance charges									(237)
Share of associates profits									
- Moët Hennessy									90
- Other associates									4
Profit before taxation									**1,393**

* These items represent the IFRS 8 performance measures for the geographic and Global Supply segments.

The group s net finance charges are managed centrally and are not attributable to individual operating segments.

Apart from sales by the Global Supply segment, inter-segmental sales are not material.

The festive holiday season provides the peak period for sales. Approximately 40% of annual net sales occur in the last four months of each calendar year.

Weighted average exchange rates used in the translation of income statements were US dollar - £1 = $1.57 (2009 - £1 = $1.64) and euro - £1 = 1.18 (2009 - £1 = 1.12). Exchange rates used to translate assets and liabilities at the balance sheet date were US dollar - £1 = $1.56 (30 June 2010 - £1 = $1.50; 31 December 2009 - £1=1.62) and euro - £1 = 1.17 (30 June 2010 - £1 = 1.22; 31 December 2009 - £1 = 1.13). The group uses foreign exchange transaction hedges to mitigate the effect of exchange rate movements.

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3. Exceptional items

Exceptional items are those which, in management s judgement, need to be disclosed by virtue of their size or incidence in order for the user to obtain a proper understanding of the financial information.

	Six months ended 31 December 2010 £ million	Six months ended 31 December 2009 £ million
Restructuring of Global Supply operations	**(4)**	(69)
Restructuring of Irish brewing operations	**(5)**	(5)
Global restructuring programme		(21)
	(9)	(95)
Sale of businesses	**(1)**	
Exceptional items before taxation	**(10)**	(95)
Tax on exceptional operating items	**2**	24
Exceptional items in continuing operations	**(8)**	(71)
Discontinued operations net of taxation		(10)
Total exceptional items	**(8)**	(81)
Items included in operating profit are charged to:		
Cost of sales	**(9)**	(22)
Other operating expenses		(73)
	(9)	(95)

4. Net interest and other finance charges

	Six months ended 31 December 2010 £ million	Six months ended 31 December 2009 £ million
Interest payable	**(270)**	(284)
Interest receivable	**86**	97
Market value movements on interest rate instruments	**(12)**	(10)
Net interest payable	**(196)**	(197)
Net finance charge in respect of post employment plans	**(2)**	(25)
Unwinding of discounts	**(8)**	(7)
Other finance (charges)/ income	**(2)**	3
	(12)	(29)
Net exchange movements on certain financial instruments	**(1)**	(11)
Net other finance charges	**(13)**	(40)

Comparative data in the table for Interest receivable and Market value movements on interest rate instruments has been reclassified in order to show the impact of certain transactions on a net basis in line with the presentation followed in the annual report for the year ended 30 June 2010.

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5. Taxation

For the six months ended 31 December 2010, the £352 million taxation charge (2009 - £310 million) comprises a UK tax charge of £25 million (2009 - tax credit of £47 million) and a foreign tax charge of £327 million (2009 - £357 million). Included within the tax charge is a credit of £2 million (2009 - £24 million) in respect of the exceptional items identified in note 3.

6. Discontinued operations

No operations are classified as discontinued in the six months ended 31 December 2010. Discontinued operations for the six months ended 31 December 2009 represent a charge after taxation of £10 million in respect of anticipated future payments to thalidomide claimants.

7. Inventories

	31 December 2010 £ million	30 June 2010 £ million	31 December 2009 £ million
Raw materials and consumables	**296**	297	311
Work in progress	**23**	21	25
Maturing inventories	**2,585**	2,506	2,413
Finished goods and goods for resale	**497**	457	530
	3,401	3,281	3,279

8. Net borrowings

	31 December 2010 £ million	30 June 2010 £ million	31 December 2009 £ million
Borrowings due within one year and bank overdrafts	**(794)**	(587)	(891)
Borrowings due after one year	**(7,847)**	(8,177)	(8,202)
Fair value of interest rate hedging instruments	**44**	191	64
Fair value of foreign currency swaps and forwards	**171**	227	154
Finance lease liabilities	**(56)**	(61)	(18)
	(8,482)	(8,407)	(8,893)
Cash and cash equivalents	**1,472**	1,453	1,589
	(7,010)	(6,954)	(7,304)

9. Reconciliation of movement in net borrowings

	Six months ended 31 December 2010 £ million	Six months ended 31 December 2009 £ million
Increase in net cash and cash equivalents before exchange	**60**	682
Decrease/(increase) in loans	**68**	(299)
Decrease in net borrowings from cash flows	**128**	383
Exchange differences	**(35)**	(201)
Loans acquired on purchase of businesses	**(15)**	
Other non-cash items	**(134)**	(67)
Net borrowings at beginning of the period	**(6,954)**	(7,419)
Net borrowings at end of the period	**(7,010)**	(7,304)

Other non-cash items primarily comprise the fair value changes of bonds and interest rate derivatives.

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10. Assets and disposal groups held for sale

	31 December 2010 £ million	30 June 2010 £ million
Current assets	**26**	47
Non-current assets	**37**	65
	63	112
Current liabilities	**(1)**	(6)
Non-current liabilities	**(4)**	(4)
	(5)	(10)

The assets and disposal groups held for sale comprise a number of non-strategic wine businesses in California and the group s investment in Tanzania Breweries Limited. No assets and disposal groups were classified as held for sale at 31 December 2009.

11. Dividends and other reserves

	Six months ended 31 December 2010 £ million	Six months ended 31 December 2009 £ million
Amounts recognised as distributions to equity shareholders in the period		
Final dividend paid for the year ended 30 June 2010 of 23.50 pence per share (2009 - 22.20 pence)	**586**	551

For the six months ended 31 December 2010, an interim dividend of 15.50 pence per share (2009 - 14.60 pence) was approved by the Board on 9 February 2011. As this was after the balance sheet date, this dividend has not been included as a liability in the balance sheet at 31 December 2010.

Other reserves of £3,258 million at 31 December 2010 included capital redemption reserve of £3,146 million, fair value and hedging reserve of £12 million and exchange reserve of £100 million.

12. Cash generated from operations

	£ million	Six months ended 31 December 2010 £ million	£ million	Six months ended 31 December 2009 £ million
Profit for the period	**1,260**		1,073	

Discontinued operations			10	
Taxation	**352**		310	
Share of associates profits after tax	**(104)**		(94)	
Net interest and net other finance charges	**209**		237	
Sale of businesses	**1**			
Operating profit		**1,718**		1,536
Increase in inventories	**(119)**		(128)	
Increase in trade and other receivables	**(529)**		(488)	
Increase in trade and other payables and provisions	**139**		544	
Net movement in working capital		**(509)**		(72)
Depreciation and amortisation		**144**		159
Dividend income		**5**		6
Other items		**(34)**		(60)
Cash generated from operations		**1,324**		1,569

In the consolidated statement of cash flows, cash generated from operations is stated after £67 million (2009 - £76 million) of cash outflows in respect of exceptional operating items.

In the calculation of cash generated from operations, Other items include £37 million of cash contributions to post employment schemes in excess of the income statement charge (2009 - £54 million).

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13. Contingent liabilities and legal proceedings

(a) Guarantees As of 31 December 2010 the group has no material performance guarantees or indemnities to third parties.

(b) Colombian litigation An action was filed on 8 October 2004 in the United States District Court for the Eastern District of New York by the Republic of Colombia and a number of its local government entities against Diageo and other spirits companies. The complaint alleges several causes of action. Included among the causes of action is a claim that the defendants allegedly violated the Federal RICO Act by facilitating money laundering in Colombia through their supposed involvement in the contraband trade to the detriment of government owned spirits production and distribution businesses. Diageo is unable to quantify meaningfully the possible loss or range of loss to which the lawsuit may give rise. Diageo intends to defend itself vigorously against this lawsuit.

(**c) Turkish customs litigation** In common with other beverage alcohol importers, litigation is ongoing against Diageo s Turkish subsidiary (Diageo Turkey) in the Turkish Civil Courts in connection with the methodology used by the Turkish customs authorities in assessing the importation value of and ad valorem import duty payable on the beverage alcohol products sold in the domestic channel in Turkey between 2001 and April 2009. The matter involves multiple cases against Diageo Turkey at various stages of litigation, including a group of cases under correction appeal following an adverse finding at the Turkish Supreme Court, and a group of cases decided on correction appeal against Diageo Turkey that are now under further appeal. Diageo Turkey is unable to quantify meaningfully the possible loss or range of loss to which these cases may give rise. If all of these cases were finally to be decided against Diageo Turkey, the aggregate loss could exceed £100 million. Diageo Turkey has been using available opportunities to indicate to the Turkish authorities that, if suitable enabling legislation were in place, Diageo Turkey would be amenable to agreeing a settlement at a level that is proportionate to the scale of Diageo Turkey s business, which earns annual operating profit of less than £10 million. In November 2010, the Turkish government announced the proposed restructuring of its public receivables law, which would allow the settlement of outstanding tax claims (including custom duties). Once the law becomes effective, Diageo will evaluate its position under the new legislation. Diageo believes that any eventual liability is unlikely to be material to the Diageo group as a whole. Diageo recognises that, in absence of settlement, the ongoing situation creates potential uncertainty regarding Diageo Turkey s continuing operations in Turkey. Diageo Turkey intends to defend its position vigorously.

(d) SEC investigation Diageo Korea and several of its current and former employees have been subject to investigations by Korean authorities regarding various regulatory and control matters. Convictions for improper payments to a Korean customs official have been handed down against two former Diageo Korea employees, and a former and two current Diageo Korea employees have been convicted on various counts of tax evasion. Diageo had previously voluntarily reported the allegations relating to the convictions for improper payments to the US Department of Justice and the US Securities and Exchange Commission (SEC). The SEC has commenced an investigation into these and other matters, and Diageo is in the process of responding to the regulators enquiries regarding activities in Korea, Thailand, India and elsewhere. Diageo s own internal investigation in Korea, Thailand, India and elsewhere remains ongoing. The US Foreign Corrupt Practices Act (FCPA) and related statutes and regulations provide for potential monetary penalties, criminal sanctions and may result in some cases in debarment from doing business with governmental entities in connection with FCPA violations. Diageo is unable to quantify meaningfully the possible loss or range of loss to which these matters may give rise.

(e) Korean customs litigation Litigation is ongoing at the Korean Tax Tribunal in connection with the application of the methodology used in transfer pricing on spirits imports since 2004. On 24 December 2009, Diageo Korea received a final customs audit assessment notice from the Korean customs authorities, covering the period from 1 February 2004 to 30 June 2007, for Korean won 194 billion or approximately £107 million (including £13 million of value added tax). In order to preserve its right to appeal, Diageo Korea is required to pay the full amount of the assessment. Diageo Korea paid £4 million to the Korean customs authorities in the year ended 30 June 2009, £57 million in the year ended 30 June 2010 and £46 million in the six month period ended 31 December 2010, in respect of the period prior to 30 June 2007. On 22 January 2010, Diageo Korea appealed this customs audit assessment to the Korean Tax Tribunal. No assessments have been received for any period subsequent to 30 June 2007. Diageo Korea is unable to quantify meaningfully the possible loss or range of loss to which these claims may give rise. Diageo Korea intends to defend its position vigorously.

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(f) Potential Chinese acquisition On 1 March 2010, Diageo entered into an equity transfer agreement to acquire an additional 4% equity stake in Sichuan Chengdu Quanxing Group Company Ltd. (Quanxing) from Chengdu Yingsheng Investment Holding Co., Ltd. The consideration for the additional 4% equity stake is RMB 140 million (£14 million). The acquisition of the 4% equity stake, which is subject to a number of regulatory approvals, would bring Diageo s shareholding in Quanxing to 53%. Quanxing is a holding company controlling a 39.7% stake in Sichuan ShuiJingFang Co., Ltd. (ShuiJingFang), a super premium Chinese white spirits company listed on the Shanghai Stock Exchange. If the acquisition of the 4% equity stake is approved, Diageo would become the indirect controlling shareholder of ShuiJingFang and, in accordance with Chinese takeover regulations, would be required to make a mandatory tender offer to all the other shareholders of ShuiJingFang. Were all other ShuiJingFang shareholders to accept the tender offer, the amount payable would be RMB 6.3 billion (approximately £614 million). As required by Chinese law, 20% of the maximum consideration payable under the tender offer (£123 million) was deposited with China s securities depositary and clearing agency, Shanghai branch.

(g) Other The group has extensive international operations and is defendant in a number of legal, tax and customs proceedings incidental to these operations. There are a number of legal, tax and customs claims against the group, the outcome of which cannot at present be foreseen.

Save as disclosed above, neither Diageo, nor any member of the Diageo group, is or has been engaged in, nor (so far as Diageo is aware) is there pending or threatened by or against it, any legal or arbitration proceedings which may have a significant effect on the financial position of the Diageo group.

14. Related party transactions

The group s significant related parties are its associates, joint ventures, key management personnel and pension plans, as disclosed in the annual report for the year ended 30 June 2010. There have been no transactions with these related parties during the six months ended 31 December 2010 that have materially affected the financial position or performance of the group during this period.

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UNAUDITED COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES

	Six months ended 31 December		Year ended 30 June				
	2010	**2009**	**2010**	**2009**	**2008**	**2007**	**2006**
	£ million	**£ million**	**£ million**	**£ million**	**£ million**	**£ million**	**£ million**
Earnings							
Income before taxes on income, non-controlling interests and discontinued operations	**1,612**	1,393	2,239	1,990	2,078	2,096	2,133
Less: Share of associates income	**(104)**	(94)	(142)	(164)	(176)	(149)	(131)
Add: Dividend income receivable from associates	**5**	6	111	179	143	119	106
Add: Fixed charges	**383**	472	966	869	549	400	284
	1,896	1,777	3,174	2,874	2,594	2,466	2,392
Fixed charges							
Interest payable and other finance charges (note (1))	**364**	455	931	836	523	378	261
Add: Interest capitalized	**2**	2	5	4			
Add: One third of rental expense	**17**	15	30	29	26	22	23
	383	472	966	869	549	400	284

Ratio	**4.9**	3.8	3.3	3.3	4.7	6.2	8.4

Notes:

(1) Interest payable and other finance charges for the six months ended 31 December 2010 includes a £81 million charge (31 December 2009 - £129 million charge; 30 June 2010 - £275 million charge; 30 June 2009 - £164 million charge; 30 June 2008 - £75 million charge; 30 June 2007 - £30 million charge; 30 June 2006 - £15 million charge) in respect of fair value adjustments to the group s derivative instruments and a £1 million charge (31 Dec 2009 - £nil; 30 June 2010 - £nil; 30 June 2009 - £11 million charge; 30 June 2008 - £6 million charge; 30 June 2007 - £nil; 30 June 2006 - a £2 million charge) in respect of exchange movements on net borrowings not in a hedge relationship and therefore recognised in the income statement. In the six months ended 31 December 2010 there was a £nil charge (31 Dec 2009 - £11 million charge; 30 June 2010 - £10 million charge; 30 June 2009 - £33 million charge; 30 June 2008 - £nil; 30 June 2007 - £nil; 30 June 2006 - £2 million charge) in respect of exchange rate translation differences on inter-company funding arrangements that do not meet the accounting criteria for recognition in equity ..

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorised.

Diageo plc

(Registrant)

/s/ D Mahlan
Deirdre Mahlan
Chief financial officer
16 February 2011