

**Diageo Capital plc**  
**Annual report and financial statements**  
**30 June 2020**

Registered number: SC040795



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## **STRATEGIC REPORT**

The Directors present their strategic report for the year ended 30 June 2020.

### **Activities**

Diageo Capital plc (the "company") is engaged in the provision of treasury risk and cash management for Diageo plc and its subsidiary undertakings (the "group"). Diageo Capital plc's principal activity is to raise external funds, principally using the London and New York financial markets. The company finances other companies of the group via intragroup loans and deposits. Foreign exchange translation hedging, interest rate risk management and cash management are also performed by the company.

### **Business review**

*Development and performance of the business of the company during the financial year and position of the company as at 30 June 2020.*

The results of the company and the development of its business are influenced to a considerable extent by group financing requirements. Further information on the risk management policies of the group is included in the Annual Report 2020 of Diageo plc (see note 15 of the consolidated financial statements of Diageo plc).

Net finance charge was £14 million in the year ended 30 June 2020, which is a £6 million increase from net finance charge of £8 million in the year ended 30 June 2019.

External borrowings increased by £2,186 million in the year ended 30 June 2020 to £6,792 million from £4,606 million in the year ended 30 June 2019, which was mainly due to the issuance of bonds in the amount of £3,296 million offset by the repayment of bonds in the amount of £820 million and by the strengthening of the USD versus GBP.

### *Financial and other key performance indicators*

As the company forms part of the group's treasury operations, the company's performance is measured at the group level.

The company receives management fee income from Diageo plc to reimburse the expenses incurred in relation to treasury services provided to the group.

### *Principal risks and uncertainties facing the company as at 30 June 2020*

The company believes the following to be the principal risks and uncertainties it faces. If any of these risks occur, the company's business, financial condition and operational results could suffer. As the company forms part of the group's financial operations, the financial risk management measures used by management to analyse the development, performance and position of the company's business are mainly similar to those facing the group as a whole and are managed by the group's treasury department.

## **STRATEGIC REPORT (continued)**

In addition, given that the company performs treasury functions for the group, as set out in the detailed description under note 10 'Financial instruments and risk management', it is exposed to foreign currency risk associated with certain foreign currency denominated bonds and interest rate risk arising principally on changes in US dollar and sterling interest rates. The company uses derivative financial instruments to hedge its exposures to fluctuations in interest and exchange rates. Cash flow hedges are carried out to hedge the currency risk of highly probable future foreign currency cash flows, as well as the cash flow risk from changes in interest rates. Fair value hedges are carried out to manage the currency and/or interest rate risks to which the fair value of certain assets and liabilities are exposed.

The negotiation process surrounding the United Kingdom's future financial and trading relationship with the European Union continues. We remain of the view that, the direct financial impact to the group or the company will not be material. The full implications of Brexit will not be understood until future trade, regulatory and tax arrangements to be entered into by the United Kingdom are established.

A cross-functional working group is in place that meets on a regular basis to identify and assess the consequences of Brexit, with all major functions within our business represented, including the function of raising external funding. We continue to monitor this risk area very closely, as well as the broader environment risks, including a continuing focus on identifying critical decision points to ensure potential disruption is minimised, and take prudent actions to mitigate these risks wherever practical.

At the beginning of calendar year 2020 a new coronavirus, referred to as 'Covid-19', emerged and has been classified as a pandemic due to its spread across the world. Given the global nature of the Covid-19 pandemic, and the uncertainty as to the severity and duration of the impact across multiple markets, it is difficult to accurately assess the impact the virus will have on the future financial performance of the group and the company. The directors have assessed that the key impacts on the company would be in respect of any change in credit risk impacting the valuation of derivatives and the effect of Covid-19 on remote working and ability to access IT systems, along with a potentially heightened cyber risk. The global economic outlook remains uncertain currently, as the pandemic has created volatility in the short term as a result of the social restrictions implemented across the world. The impact of the virus on economic conditions over the medium-term (one to three years) is highly uncertain, in sharp contrast to the stable and growing GDP performance across most markets experienced in recent years. As a result, significant volatility in the group's performance is likely to continue or increase as markets face challenging economic conditions and higher levels of unemployment leading to reduced consumer spending.

To mitigate these challenges the group regularly gathers data and obtains insights which enable management to assess conditions in the markets where the group operates and to amend forecasts and investment decisions appropriately. The directors believe that the risk mitigation actions taken in relation to the pandemic have been agile and effective and that the group will maintain adequate liquidity and be strongly positioned for a recovery in consumer demand. Further information on the group's risk management measures are disclosed on pages 38-40 of Diageo plc's 2020 Annual Report.

## **STRATEGIC REPORT (continued)**

### *Statement on Section 172 of the Companies Act 2006*

Section 172 of the Companies Act 2006 requires the directors to promote the success of the company for the benefit of the members as a whole, having regard to the interests of stakeholders in their decision-making. In making decisions, the directors consider what is most likely to promote the success of the company for its shareholders in the long term, as well as the interests of the group's stakeholders. The directors understand the importance of taking into account the views of stakeholders and the impact of the company's activities on local communities, the environment, including climate change, and the group's reputation.

The company is a member of the group of companies whose ultimate holding company is Diageo plc ("Diageo"). In accordance with the requirements of UK company law, Diageo has included in its 2020 Annual Report and Accounts on page 5 a statement as to how the directors of Diageo have had regard to the matters set out in Section 172 of the Companies Act 2006.

In order to ensure consistency in how the group operates with regard to its wider stakeholders, the group has adopted an internal Code of Business Conduct alongside a comprehensive framework of global policies and standards that are designed to ensure, amongst other things, that all companies throughout the group, including the company, have regard to its wider stakeholders in a consistent manner.

The company has therefore had regard to the matters set out in Section 172 of the Act in a manner that is consistent with the approach adopted by Diageo, while at the same time ensuring the directors of the company are fulfilling their duties.

On behalf of the Board



J M C Edmunds  
*Director*  
Edinburgh Park  
5 Lochside Way  
Edinburgh  
EH12 9DT

28 October 2020

## **DIRECTORS' REPORT**

The Directors have pleasure in submitting their Directors' report and audited financial statements for the year ended 30 June 2020.

The Directors foresee no changes in the company's activities. The company is incorporated and domiciled as a public company limited by shares in the United Kingdom. The registered address is Edinburgh Park, 5 Lochside Way, Edinburgh, EH12 9DT.

### **Going concern**

The company's business activities, together with the factors likely to affect its future development and position, are set out in the business review section of the strategic report on pages 2-4. The company is expected to continue to generate profit for its own account and to remain in positive net asset position for the foreseeable future. The company participates in the group's centralised treasury arrangements and the parent and fellow group undertakings are expected to provide financial support for the foreseeable future. The Directors have no reason to believe that a material uncertainty exists that may cast significant doubt about the ability of the company to continue as a going concern. On the basis of their assessment, the company's Directors have a reasonable expectation that the company will be able to continue in operational existence for the foreseeable future as a fellow group undertaking has agreed to provide financial support for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

### **Financial performance**

The result for the year ended 30 June 2020 is shown on page 13.

The profit for the year transferred to reserves was £nil (2019 - £7 million) and the other comprehensive income for the year is £117 million (2019 - £91 million).

No dividend was paid during the year (2019 - £nil) and there was no dividend proposed to be distributed to the shareholders in regard to the financial year (2019 - £nil).

Net financial assets were £261 million at 30 June 2020 (2019 - £115 million). More details on financial instruments and risk management can be found under note 10.

### **Directors**

The Directors of the company who were in office during the year and up to the date of signing the financial statements were:

M Pais  
J M C Edmunds  
P Viswanathan (resigned 1 August 2020)  
Cs Hajos  
K E Major  
C M Lewin (appointed 1 August 2020)

### **Directors' remuneration**

None of the Directors received any remuneration during the year in respect of their services as directors of the company (2019 - £nil).

**Diageo Capital plc**  
**Registered number: SC040795**  
**Year ended 30 June 2020**

## **DIRECTORS' REPORT (continued)**

### **Secretary**

The secretary of the company who was in office during the year and up to the date of signing the financial statements was:

J M C Edmunds

### **Internal control and risk management over financial reporting**

The company operates under the financial reporting processes and controls of the group. Diageo plc's internal control and risk management systems including its financial reporting process, which include those of the company, are discussed in the group's Annual Report 2020 on page 79 at [www.diageo.com](http://www.diageo.com), which does not form part of this report.

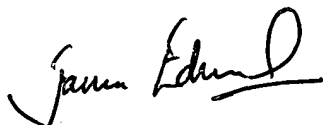
### **Independent auditors**

Pursuant to Section 487 of the Companies Act 2006, the auditors, PricewaterhouseCoopers LLP, have been reappointed and will continue in office as auditors of the company.

### **Disclosure of information to the auditors**

The Directors who held office at the date of approval of this Directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the company's auditors are unaware; and each director has taken all the steps that they ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

On behalf of the Board



J M C Edmunds  
*Director*  
Edinburgh Park  
5 Lochside Way  
Edinburgh  
EH12 9DT

28 October 2020

## **Statement of directors' responsibilities**

The Directors are responsible for preparing the annual strategic report, the Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 'Reduced Disclosure Framework', and applicable law). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period.

In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable United Kingdom Accounting Standards, comprising FRS 101, have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006.

The directors are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.



# ***Independent auditors' report to the members of Diageo Capital plc***

## **Report on the audit of the financial statements**

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### **Opinion**

In our opinion, Diageo Capital plc's financial statements:

- give a true and fair view of the state of the company's affairs as at 30 June 2020 and of its result for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law); and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Annual report and financial statements (the "Annual Report"), which comprise: the Balance Sheet as at 30 June 2020; the Income Statement for the year then ended, the Statement of Comprehensive Income for the year then ended, the Statement of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the directors.

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### **Basis for opinion**

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### *Independence*

We remained independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

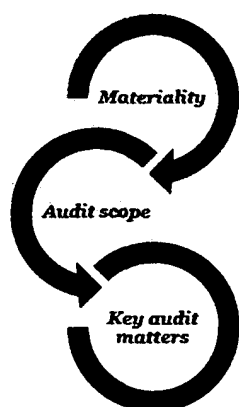
To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the company.

We have provided no non-audit services to the company in the period from 1 July 2019 to 30 June 2020.

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### **Our audit approach**

#### *Overview*



- Overall materiality: £90.5 million (2019: £84 million), based on approximately 1% of total assets.
  - We conducted a full scope audit of the financial statements of Diageo Capital plc.
  - We focused on the most significant areas, being the hedging activity and assessment of hedge effectiveness and valuation of derivative transactions.
  - We assessed the risks of material misstatement in the financial statements and determined the following key audit matters for 2020:
    - Valuation of derivatives.
    - Hedge effectiveness of derivatives.
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#### *The scope of our audit*

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements.

### *Capability of the audit in detecting irregularities, including fraud*

Based on our understanding of the company and industry, we identified that the principal risks of non-compliance with laws and regulations related to the United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework"), and applicable law, the requirements of the Companies Act 2006, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the preparation of the financial statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries to manipulate hedge accounting and management bias in accounting estimates. Audit procedures performed by the engagement team included:

- Discussion with management and internal audit, including consideration of known and suspected instances of non-compliance with laws and regulation and fraud
- Identifying and testing journal entries, in particular any journal entries posted with unusual account combinations or posted by senior management
- Review of the financial statements

There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

### *Key audit matters*

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit.

<b><i>Key audit matter</i></b>	<b><i>How our audit addressed the key audit matter</i></b>
<p><b><i>Valuation of derivatives</i></b></p> <p>The company is engaged in treasury risk and cash management for Diageo plc. The company enters into derivative transactions to hedge foreign exchange and interest rate risk implicit in its borrowings. Valuation of derivatives is a complex calculation due to the estimates associated with the data inputs.</p> <p>Therefore, one of our focus areas was the determination of the fair value of derivative transactions and the associated balance sheet position.</p>	<p>Our audit procedures included understanding and evaluating the controls and systems related to the determination of the fair value of derivatives, and where appropriate obtaining audit evidence through testing operating effectiveness of relevant controls together with substantive audit procedures.</p> <p>Testing of controls included examining appropriate authorisation of deal tickets and contracts for derivatives, as well as an assessment of the completeness of derivative transactions.</p> <p>The substantive audit procedures performed included the following tests, on a sample basis:</p> <ul style="list-style-type: none"><li>• Obtained independent valuations from our specialist treasury team who tested the accuracy and valuation of the derivatives using independent data-feeds;</li><li>• circularising counterparties to confirm the existence, completeness and valuation of derivatives;</li><li>• we assessed the counterparty and own credit risk incorporated in the fair value of derivatives, in particular in light of the impact that Covid-19 has had on the broader economy, and noted no significant issues.</li><li>• we also evaluated whether the derivatives and their values were appropriately disclosed in the financial statements.</li></ul> <p>Based on these procedures we are comfortable with the valuation and of derivatives.</p>
<p><b><i>Hedge effectiveness of derivatives</i></b></p> <p>As a part of risk management activity, the company trades in derivative transactions to hedge the group's</p>	<p>Our audit procedures included understanding and evaluating the controls and systems related to hedge accounting including that the pre-conditions of hedge accounting were met, the</p>

foreign currency and interest rate risk. The company applies hedge accounting in its financial statements. The accounting framework applied by the company requires certain pre-conditions to be met upon designation of a hedge relationship and throughout the term of the relationship, some of which are complex and are subject to management judgement.

Therefore, our areas of focus included hedge accounting applied by the company.

prospective and retrospective assessment of hedge effectiveness were appropriately performed and resulting entries were properly accounted for. Where relevant, we obtained audit evidence through testing operating effectiveness of relevant controls together with substantive audit procedures.

Testing of controls included examining appropriate authorisation of hedge designation, review of hedge effectiveness tests and resulting accounting entries.

The substantive audit procedures performed included the following tests, on a sample basis:

- review of appropriateness of hedge designation documents;
- the independent recalculation of hedge effectiveness tests;
- review of appropriateness of accounting entries relating to hedge accounting.

We also evaluated whether derivative transactions were appropriately disclosed in the financial statements.

Based on these procedures we are comfortable with the hedge effectiveness of derivatives.

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#### *Impact of Covid-19*

Due to the nature of the entity the risks considered applicable were in respect of credit risk, addressed in the valuation of derivatives above, and the impact on operations.

Management's way of working, including the operation of controls, has been impacted by Covid-19 as a result of a large number of staff working remotely. For example, this has meant virtual review meetings have replaced in-person meetings. There is inevitably an increase in risk due the remote accessing of IT systems, and potentially heightened cyber risk.

We performed additional procedures to assess any control implications arising from the impact of Covid-19, including inquiries with respect to the operation of IT and business process controls, and whether there has been any impact on the company given the potentially heightened cyber risk. We performed a detailed assessment of the policies and procedures that management has in place to mitigate cyber risk exposure.

We performed additional procedures to understand if there were any changes to management's planned operation of controls or monitoring activities.

Based on the inquiries performed and the results of our audit procedures, we did not identify any evidence of material deterioration in the control environment.

We considered the appropriateness of management disclosures in the financial statements in respect of the impact of the current environment and the impact of the increased uncertainty and considered the accounting estimates and disclosures to be appropriate.

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#### *How we tailored the audit scope*

We tailored the scope of our audit to ensure that we performed sufficient work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the company, the accounting processes and controls, and the industry in which it operates.

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements.

#### *Materiality*

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

<b>Overall materiality</b>	£90.5 million (2019: £84 million).
<b>How we determined it</b>	Approximately 1% of total assets.
<b>Rationale for benchmark applied</b>	We consider the total asset measure to reflect the nature of the company, which primarily acts as a funding and cash management company for the group's investments and carries out derivatives to hedge the group's financial risks.

We agreed with the directors that we would report to them misstatements identified during our audit above £4.5 million (2019: £4 million) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

## Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the company's ability to continue as a going concern.

## Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Directors' Report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, ISAs (UK) require us also to report certain opinions and matters as described below.

### *Strategic Report and Directors' Report*

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 30 June 2020 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report.

## Responsibilities for the financial statements and the audit

### *Responsibilities of the directors for the financial statements*

As explained more fully in the Statement of Directors' Responsibilities, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

### *Auditors' responsibilities for the audit of the financial statements*

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable

assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: [www.frc.org.uk/auditorsresponsibilities](http://www.frc.org.uk/auditorsresponsibilities). This description forms part of our auditors' report.

#### *Use of this report*

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

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## **Other required reporting**

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### **Companies Act 2006 exception reporting**

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of directors' remuneration specified by law are not made; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

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### **Appointment**

We were appointed by the members on 1 September 2015 to audit the financial statements for the year ended 30 June 2016 and subsequent financial periods. The period of total uninterrupted engagement is 5 years, covering the years ended 30 June 2016 to 30 June 2020.



Christopher Richmond (Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London  
28 October 2020

**Diageo Capital plc**  
**Registered number: SC040795**  
**Year ended 30 June 2020**

**INCOME STATEMENT**

	Notes	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
Other operating income	2	14	15
Finance income	4	350	404
Finance charges	4	(364)	(412)
<b>Operating profit</b>		<u>—</u>	<u>7</u>
<b>Profit before taxation on ordinary activities</b>		<u>—</u>	<u>7</u>
Taxation on profit on ordinary activities	5	—	—
<b>Profit for the year</b>		<u><u>—</u></u>	<u><u>7</u></u>

The accompanying notes are an integral part of these financial statements.

**STATEMENT OF COMPREHENSIVE INCOME**

	Notes	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
<b>Other comprehensive income/(expense)</b>			
<b>Items that may be recycled subsequently to the income statement</b>			
Effective portion of changes in fair value of cash flow hedges			
- gains taken to other comprehensive income	12	221	180
- recycled to income statement	12	(75)	(82)
Tax charge on effective portion of changes in fair value of cash flow hedge	12	(29)	(7)
<b>Other comprehensive income</b>		<b>117</b>	<b>91</b>
Profit for the year		—	7
<b>Total comprehensive income for the year</b>		<b>117</b>	<b>98</b>

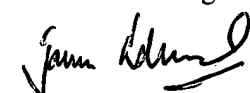
The accompanying notes are an integral part of these financial statements.

**BALANCE SHEET**

	Notes	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
<b>Non-current assets</b>			
Trade and other receivables	7	8,393	7,965
Other financial assets	6	644	371
		<u>9,037</u>	<u>8,336</u>
<b>Current assets</b>			
Trade and other receivables	7	14	36
Other financial assets	6	—	6
		<u>14</u>	<u>42</u>
<b>Total assets</b>		<u>9,051</u>	<u>8,378</u>
<b>Current liabilities</b>			
Trade and other payables	11	(1,955)	(3,616)
Other financial liabilities	6	—	(3)
Borrowings and bank overdrafts	9	(566)	(1,306)
		<u>(2,521)</u>	<u>(4,925)</u>
<b>Non-current liabilities</b>			
Borrowings	9	(6,226)	(3,300)
Other financial liabilities	6	(43)	(38)
Deferred tax liability	8	(36)	(7)
		<u>(6,305)</u>	<u>(3,345)</u>
<b>Total liabilities</b>		<u>(8,826)</u>	<u>(8,270)</u>
<b>Net assets</b>		<u>225</u>	<u>108</u>
<b>Equity</b>			
Called up share capital	12	—	—
Share premium		250	250
Fair value and hedging reserves		155	38
Other reserves		70	70
Accumulated losses		(250)	(250)
<b>Total equity</b>		<u>225</u>	<u>108</u>

The accompanying notes are an integral part of these financial statements.

These financial statements on pages 13 to 37 were approved by the Board of Directors on 28 October 2020 and were signed on its behalf by:



J M C Edmunds  
Director



**STATEMENT OF CHANGES IN EQUITY**

**ATTRIBUTABLE TO SHAREHOLDERS OF THE COMPANY**

	<b>Share premium £ million</b>	<b>Hedging reserve £ million</b>	<b>Other reserves £ million</b>	<b>Subtotal Other reserves £ million</b>	<b>Accumulated losses £ million</b>	<b>Total £ million</b>
<b>Balance at 30 June 2018</b>	<b>250</b>	<b>(53)</b>	<b>70</b>	<b>17</b>	<b>(257)</b>	<b>10</b>
Other comprehensive income for the year	—	91	—	91	—	91
Profit for the financial year	—	—	—	—	7	7
<b>Balance at 30 June 2019</b>	<b>250</b>	<b>38</b>	<b>70</b>	<b>108</b>	<b>(250)</b>	<b>108</b>
Other comprehensive income for the year	—	117	—	117	—	117
Profit for the financial year	—	—	—	—	—	—
<b>Balance at 30 June 2020</b>	<b>250</b>	<b>155</b>	<b>70</b>	<b>225</b>	<b>(250)</b>	<b>225</b>

The accompanying notes are an integral part of these financial statements.

## **NOTES TO THE FINANCIAL STATEMENTS**

### **1. ACCOUNTING POLICIES**

#### **Basis of preparation**

These financial statements are prepared in accordance with Financial Reporting Standard 101 *Reduced Disclosure Framework* (FRS 101).

In preparing these financial statements, the company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards as adopted by the EU (IFRS) but makes amendments where necessary in order to comply with Companies Act 2006 and sets out below where the FRS 101 disclosure exemptions have been taken.

These financial statements are prepared on a going concern basis under the historical cost convention, except that certain financial instruments are stated at their fair value.

The company is a wholly owned subsidiary of Diageo plc and is included in the consolidated financial statements of Diageo plc which are publicly available.

The company has taken advantage of the following exemptions from the requirements of IFRS in the preparation of these financial statements, in accordance with FRS 101:

- A cash flow statement and related notes;
- Disclosures in respect of transactions with wholly owned subsidiaries;
- The effects of new but not yet effective IFRSs;
- Disclosures in respect of the compensation of Key Management Personnel.

These financial statements are separate financial statements.

#### **Functional and presentational currency**

These financial statements are presented in sterling (£), which is the company's functional currency.

All financial information presented in sterling has been rounded to the nearest million unless otherwise stated.

#### **Finance costs**

Finance costs which are not capitalised are recognised in the income statement based on the effective interest method.

#### **Going concern**

The financial statements have been prepared on a going concern basis as a fellow group undertaking has agreed to provide financial support for the foreseeable future.

#### **Foreign currencies**

Transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the financial year end exchange rates and these foreign exchange differences are recognised in the income statement.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 1. ACCOUNTING POLICIES (continued)

#### Financial assets and liabilities

Financial assets and liabilities are initially recorded at fair value including, where permitted by IFRS 9, any directly attributable transaction costs. For those financial assets that are not subsequently held at fair value, the company assesses whether there is evidence of impairment at each balance sheet date. The company classifies its financial assets and liabilities into the following categories: financial assets and liabilities at amortised cost, financial assets and liabilities at fair value through profit and loss and financial assets at fair value through other comprehensive income. Under IFRS 9, classification and measurement of financial assets depend on the company's business model for managing the asset and the cash flow characteristics of the assets. The business model and cash flow characteristics assessment is carried out on instrumental basis. Where financial assets or liabilities are eligible to be carried at either amortised cost or fair value the company does not apply the fair value option.

**Trade and other receivables** Amounts owed by other group companies are initially measured at fair value and are subsequently reported at amortised cost. Non-interest bearing trade receivables are stated at their nominal value as they are due on demand. Allowance for expected credit losses are made based on the risk of non-payment taking into account ageing, previous experience, economic conditions and forward-looking data. Such allowances are measured as either 12-months expected credit losses or lifetime expected credit losses depending on changes in the credit quality of the counterparty.

**Borrowings** Borrowings are initially measured at fair value net of transaction costs and are subsequently reported at amortised cost. Certain bonds are designated as being part of a fair value hedge and/or a cash flow hedge relationship. In these cases, the amortised cost is adjusted for the fair value of the risk being hedged, with changes in value recognised in the income statement. The fair value adjustment is calculated using a discounted cash flow technique based on unadjusted market data.

**Trade and other payables** Amounts owed to other group companies are initially measured at fair value and are subsequently reported at amortised cost.

#### Derivative financial instruments

Derivative financial instruments are carried at fair value using a discounted cash flow technique based on market data applied consistently for similar type of instruments. Gains and losses on derivatives that do not qualify for cash flow hedge accounting treatment are taken to the income statement as they arise.

The company designates and documents certain derivatives as hedging instruments against changes in fair value of recognised assets and liabilities (fair value hedges) and the cash flow risk from a change in exchange or interest rates (cash flow hedges). The effectiveness of such hedges is assessed at inception and at least on a quarterly basis, using prospective testing. Methods used for testing effectiveness include dollar offset, critical terms, regression analysis and hypothetical derivative method.

**Fair value hedges** are used to manage the currency and/or interest rate risks to which the fair value of certain assets and liabilities are exposed. Changes in fair value of the derivatives are recognised in the income statement, along with any changes in the relevant fair value of the underlying hedged asset or liability.

If such a hedge relationship is de-designated or no longer meets hedge accounting criteria, fair value movements on the derivative continue to be taken to the income statement while any fair value adjustments made to the underlying hedged item to that date are amortised through the income statement over its remaining life using the effective interest rate method.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 1. ACCOUNTING POLICIES (continued)

*Cash flow hedges* are used to hedge the foreign currency risk of highly probable future foreign currency cash flows, as well as the cash flow risk from changes in exchange or interest rates. The effective portion of the gain or loss on the hedges is recognised in the other comprehensive income, while any ineffective part is recognised in the income statement. Amounts recorded in the other comprehensive income are recycled to the income statement in the same period in which the underlying foreign currency or interest exposure affects the income statement.

Derivative financial instruments are presented in the financial statements as 'Intra-group derivative assets/(liabilities)' as these transactions are entered into by Diageo Finance plc, a fellow group undertaking, and subsequently passed to the company.

#### **Taxation**

Current tax is based on taxable profit for the year. Taxable profit is different from accounting profit due to temporary differences between accounting and tax treatments, and due to items, that are never taxable or tax deductible. Tax benefits are not recognised unless it is probable that the tax positions are sustainable. Once considered to be probable, tax benefits are reviewed each year to assess whether a provision should be taken against full recognition of the benefit on the basis of potential settlement through negotiation and/or litigation. Tax provisions are included in current liabilities. Penalties and interest on tax liabilities are included in profit before taxation.

Full provision for deferred tax is made for temporary differences between the carrying value of assets and liabilities for financial reporting purposes and their value for tax purposes. The amount of deferred tax reflects the expected recoverable amount and is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using the basis of taxation enacted or substantively enacted by the balance sheet date. Deferred tax assets are not recognised where it is more likely than not that the asset will not be realised in the future.

#### **Judgements in applying accounting policies and key sources of estimation uncertainty**

The Directors make estimates and judgements concerning the future of the company. The resulting accounting estimates will, by definition, seldom equate to actual results. The company's Directors are of the opinion that there are no estimates and assumptions that have a significant risk of casting material adjustment to the carrying value of the assets and liabilities for the company within the next financial year due to the nature of the business.

The critical accounting policy, which the Directors consider is of greater complexity and particularly subject to estimates, is set out in detail in the accounting policy for derivative financial instruments. A critical accounting estimate, specific to the company, is the estimation of fair valuation of derivative assets and liabilities (see detailed description under note 10. Financial instruments and risk management (f) Fair value measurements).

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**2. OTHER OPERATING INCOME**

	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
Intercompany management income	14	15
	<u>14</u>	<u>15</u>

The auditors' remuneration of £10,489 (2019 - £10,201) was paid on behalf of the company by a fellow group undertaking. There were no fees payable to the auditors in respect of non-audit services (2019 - £nil).

**3. EMPLOYEES**

The company did not employ any staff during either the current or prior year.

None of the Directors received any remuneration during the financial year in respect of their services as directors of the company (2019 - £nil).

**4. FINANCE INCOME AND CHARGES**

	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
<b>Net interest</b>		
Interest income from fellow group undertakings	248	305
Fair value gain on external derivative financial instruments	1	1
Fair value gain on intra-group derivative financial instruments	97	96
Fair value adjustment on borrowings	2	—
Amortisation of bonds	2	2
<b>Total interest income</b>	<u>350</u>	<u>404</u>
Interest charge to fellow group undertakings	(62)	(149)
Interest charge on all other borrowings	(188)	(155)
Fair value loss on intra-group derivative financial instruments	(28)	(31)
Fair value adjustment on borrowings	(73)	(66)
Discount and fee amortisation	(13)	(11)
<b>Total interest charges</b>	<u>(364)</u>	<u>(412)</u>
<b>Net finance charges</b>	<u>(14)</u>	<u>(8)</u>

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**5. TAXATION**

	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
<b>(a) Analysis of taxation (charge)/credit for the year</b>		
Current tax	—	—
Deferred tax	—	—
<b>Taxation on profit on ordinary activities</b>	<u>—</u>	<u>—</u>
	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
<b>(b) Tax charge included in other comprehensive income</b>		
Current tax	—	—
Deferred tax	(29)	(7)
<b>Total tax charge included in other comprehensive income</b>	<u>(29)</u>	<u>(7)</u>
	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
<b>(c) Factors affecting total tax (charge)/credit for the year</b>		
Profit on ordinary activities before taxation	—	7
Taxation on profit on ordinary activities at UK corporation tax rate of 19% (2019 - 19%)	—	(1)
Group relief received for nil consideration	—	1
<b>Total tax charge for the year</b>	<u>—</u>	<u>—</u>

The UK tax rate is 19% effective from 1 April 2017 which is applied for the year ended 30 June 2020. In the Spring Budget 2020, the Government announced that from 1 April 2020 the corporation tax rate would remain at 19% (rather than reducing to 17%, as previously enacted). This new law was substantively enacted on 17 March 2020.

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**6. OTHER FINANCIAL ASSETS AND LIABILITIES**

	<b>Assets due after one year £ million</b>	<b>Assets due within one year £ million</b>	<b>Liabilities due within one year £ million</b>	<b>Liabilities due after one year £ million</b>
<b>30 June 2020</b>				
<b>Intra-group derivative assets/liabilities</b>				
Designated in cash flow hedge	469	—	—	—
Designated in fair value hedge	132	—	—	—
Not designated in a hedge relationship	43	—	—	(43)
<b>Total derivative assets/(liabilities)</b>	<b>644</b>	<b>—</b>	<b>—</b>	<b>(43)</b>

Diageo Finance plc, a fellow group undertaking, entered into external cross currency interest rate swaps on behalf of Diageo Capital plc, market value of which amounted to £469 million at the balance sheet date (2019 - £271 million). The external deals are mirrored through Diageo plc to Diageo Capital plc, the ultimate beneficiary. Market value of intra-group cross currency interest rate swaps amounts to a net asset of £469 million (2019 - £271 million).

	<b>Assets due after one year £ million</b>	<b>Assets due within one year £ million</b>	<b>Liabilities due within one year £ million</b>	<b>Liabilities due after one year £ million</b>
<b>30 June 2019</b>				
<b>Intra-group derivative assets/(liabilities)</b>				
Designated in cash flow hedge	283	—	—	(12)
Designated in fair value hedge	60	3	—	—
Not designated in a hedge relationship	28	3	(3)	(26)
<b>Total derivative assets/(liabilities)</b>	<b>371</b>	<b>6</b>	<b>(3)</b>	<b>(38)</b>

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**7. TRADE AND OTHER RECEIVABLES**

	30 June 2020		30 June 2019	
	Due within one year £ million	Due after one year £ million	Due within one year £ million	Due after one year £ million
Amounts owed by fellow group undertakings	14	8,393	36	7,965
	<b>14</b>	<b>8,393</b>	<b>36</b>	<b>7,965</b>

Amounts owed by fellow group undertakings include accrued and capitalised interest on the underlying balances at 30 June 2020 and at 30 June 2019. These balances bear interest at fixed and variable rates from 0.0861% to 8.11% for the year ended 30 June 2020 (2019 - from 0.4914% to 8.11%).

Amounts owed by fellow group undertakings represent transactions with companies in the group with which the company has a long-term financing relationship. These financing relationships are expected to continue for the foreseeable future. Certain amounts owed by fellow group undertakings are reclassified to non-current assets as they are not expected to be repaid in the foreseeable future. Amounts owed by group undertakings are considered to have a fair value which is not materially different to the book value.

**8. DEFERRED TAX LIABILITY**

	Fair value and hedging reserves £ million	Total £ million
<b>At 30 June 2018</b>	—	—
Recognised in other comprehensive income	7	7
<b>At 30 June 2019</b>	7	7
Recognised in other comprehensive income	29	29
<b>At 30 June 2020</b>	<b>36</b>	<b>36</b>

The deferred tax liability arose from temporary timing differences on cross currency swaps designated as a cash flow hedge relationship. The amount of deferred tax liability on temporary differences is £36 million (2019 - £7 million).



**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**9. BORROWINGS AND BANK OVERDRAFTS**

	<b>30 June 2020</b>	<b>30 June 2019</b>
	<b>£ million</b>	<b>£ million</b>
Bank overdrafts	—	27
Commercial paper	—	492
US\$ 500 million 3% bonds due 2020	—	393
US\$ 500 million 2.565% bonds due 2020	—	394
US\$ 696 million 4.828% bonds due 2020	566	—
<b>Borrowings due within one year and bank overdrafts</b>	<b>566</b>	<b>1,306</b>
US\$ 696 million 4.828% bonds due 2020	—	538
US\$ 500 million 3.5% bonds due 2023	405	393
US\$ 1,350 million 2.625% bonds due 2023	1,096	1,060
US\$ 600 million 2.125% bonds due 2024	487	—
US\$ 750 million 1.375% bonds due 2025	606	—
US\$ 500 million 3.875% bonds due 2028	404	391
US\$ 1,000 million 2.375% bonds due 2029	804	—
US\$ 1,000 million 2% bonds due 2030	807	—
US\$ 750 million 2.125% due 2032	603	—
US\$ 600 million 5.875% bonds due 2036	483	468
US\$ 500 million 3.875% bonds due 2043	400	387
Fair value adjustment to borrowings	131	63
<b>Borrowings due after one year</b>	<b>6,226</b>	<b>3,300</b>
<b>Total external borrowings</b>	<b>6,792</b>	<b>4,606</b>

The interest rates of external borrowings shown in the table above are those contracted on the underlying borrowings before taking into account any interest rate hedges. Bonds are stated net of unamortised finance costs of £45 million (2019 - £29 million). Bonds are reported at amortised cost with a fair value adjustment shown separately. All bonds, medium term notes and commercial paper issued by the company are fully and unconditionally guaranteed by Diageo plc.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The company's funding, liquidity and exposure to foreign currency and interest rate risks are managed at group level by the group's treasury department.

The treasury department uses a range of financial instruments to manage these underlying risks.

Treasury operations are conducted within a framework of board-approved policies and guidelines, which are recommended and monitored by the finance committee, chaired by the Chief Financial Officer. The policies and guidelines include benchmark exposure and/or hedge cover levels for key areas of treasury risk which are periodically reviewed by the Board following, for example, significant business, strategic or accounting changes. The framework provides for limited defined levels of flexibility in execution to allow for the optimal application of the board-approved strategies. Transactions arising from the application of this flexibility may give rise to exposures different from the defined benchmark levels that are separately monitored on a daily basis using Value at Risk analysis. These transactions are carried at fair value and gains or losses are taken to the income statement as they arise. In the year ended 30 June 2020 and 30 June 2019 gains and losses on these transactions were not material. The company does not use derivatives for speculative purposes. All transactions in derivative financial instruments are initially undertaken to manage the risks arising from underlying business activities.

The finance committee receives monthly reports on the activities of the treasury department, including any exposures different from the defined benchmarks.

#### (a) Currency risk

The company presents its financial statements in sterling (which is the functional currency of the entity) and conducts business in many currencies. As a result, it is subject to foreign currency risk due to exchange rate movements, which will affect the company's transactions. To manage the currency risk the company uses certain financial instruments. Where hedge accounting is applied, hedges are documented and tested for effectiveness on an ongoing basis. The company expects hedges entered into to continue to be effective and therefore does not expect the impact of ineffectiveness on the income statement to be material.

#### *Hedge of foreign currency debt*

The company uses cross currency interest rate swaps to hedge the foreign currency risk associated with certain foreign currency denominated borrowings.

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

**(b) Interest rate risk**

The company has an exposure to interest rate risk, arising principally on changes in US dollar and sterling interest rates. To manage interest rate risk, the company manages its proportion of fixed to floating rate borrowings within limits approved by the Board, primarily through issuing fixed and floating rate borrowings and commercial paper, and by utilising interest rate swaps. These practices aim to minimise the company's net finance charges with acceptable year on year volatility. To facilitate operational efficiency and effective hedge accounting, the group's policy is to maintain fixed rate borrowings within a band of 40% to 60% of forecast net borrowings. In September 2019 the Board approved to temporarily amend the approved 40% – 60% fixed debt band to 40% – 70% for a period of 15 months until 31 December 2020. For these calculations, net borrowings exclude interest rate related fair value adjustments. The majority of the group's existing interest rate derivatives are designated as hedges and are expected to be effective. Fair value of the company's existing interest rate derivatives is recognised in the income statement, along with any changes in the relevant fair value of the underlying hedged asset or liability.

**(c) Market risk sensitivity analysis**

The company uses a sensitivity analysis that estimates the impacts on the income statement and other comprehensive income of either an instantaneous increase or decrease of 0.5% in market interest rates or a 10% strengthening or weakening in sterling against all other currencies, from the rates applicable at 30 June 2020 and 30 June 2019, for each class of financial instruments with all other variables remaining constant. The sensitivity analysis excludes the impact of market risks on the corporate tax payable. This analysis is for illustrative purposes only, as in practice interest and foreign exchange rates rarely change in isolation.

The sensitivity analysis estimates the impact of changes in interest and foreign exchange rates. All hedges are expected to be highly effective for this analysis and it considers the impact of all financial instruments, including financial derivatives, cash and cash equivalents, borrowings and other financial assets and liabilities. The results of the sensitivity analysis should not be considered as projections of likely future events, gains or losses as actual results in the future may differ materially due to developments in the global financial markets which may cause fluctuations in interest and exchange rates to vary from the hypothetical amounts disclosed in the table below.

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

	<b>0.5 % decrease in interest rates £ million</b>	<b>0.5 % increase in interest rates £ million</b>	<b>10 % weakening of sterling £ million</b>	<b>10 % strengthening of sterling £ million</b>
<b>30 June 2020</b>				
Impact on income statement - gain/(loss)	18	(18)	4	(3)
Impact on other comprehensive income - gain/(loss)	26	(24)	52	(43)
<b>30 June 2019</b>				
Impact on income statement - gain/(loss)	12	(12)	5	(4)
Impact on other comprehensive income - gain/(loss)	13	(11)	23	(30)

Impact on the statement of comprehensive income includes the impact on the income statement.

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

**(d) Credit risk**

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the company. Credit risk arises on cash balances (including bank deposits and cash and cash equivalents), derivative financial instruments, trade and other receivables, loans, financial guarantees and committed transactions. The carrying amount of financial assets represents the company's exposure to credit risk at the balance sheet date as disclosed in section (i), excluding the impact of any collateral held or other credit enhancements. A financial asset is in default when the counterparty fails to pay its contractual obligations. Financial assets are written-off when there is no reasonable expectation of recovery. The gross carrying amount of the financial asset has to be reduced (written off) in case there is no reasonable expectation of recovering the contractual cash flows on the asset in its entirety or its portion only. Expected recovery of contractual cash flows is assessed individually, on instrumental basis. Credit risk is managed separately for financial and business-related credit exposures.

***Financial credit risk***

The group aims to minimise its financial credit risk through the application of risk management policies approved and monitored by the Board. Counterparties are limited to major banks and financial institutions, primarily with a long-term credit rating within the A band or better, and the policy restricts the exposure to any one counterparty by setting credit limits taking into account the credit quality of the counterparty. The group's policy is designed to ensure that individual counterparty limits are adhered to and that there are no significant concentrations of credit risk. The Board also defines the types of instruments for currency and interest rate risk management is estimated with reference to the fair value of contracts with a positive value, rather than the notional amount of the instruments themselves. The group annually reviews the credit limits applied and regularly monitors the counterparties' credit quality reflecting market credit conditions.

When derivative transactions are undertaken with bank counterparties, the group may, where appropriate, enter into certain agreements with such bank counterparties whereby the parties agree to post cash collateral for the benefit of the other if the net valuations of the derivatives are above a predetermined threshold.

***Business related credit risk***

Since trade and other receivables principally include balances with fellow group undertakings, the risk of non-performance is considered remote. Under IFRS 9, the significant increase in credit risk of financing relationships with fellow group undertakings is determined based on the group's internal credit rating assessment. The assessment practice takes into account as inputs the historical default of the financial instruments, currently available information about fellow group undertakings' financial performance and forward-looking information. The total balance of trade and other receivables is qualified as performing in accordance with internal credit rating assessment. As a result of low risk credit risk these financial assets have a very low risk of default (probability of default (PD)) and the 12-months expected credit loss is considered to be immaterial.

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

**(e) Liquidity risk**

Liquidity risk is the risk that the group may encounter difficulties in meeting its obligations associated with financial liabilities that are settled by delivering cash or other financial assets. The company uses short term commercial paper to finance its day-to-day operations. The group's policy with regard to the expected maturity profile of borrowings is to limit the amount 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, the group's policy is to maintain backstop facilities with relationship banks to support commercial paper obligations. The following tables provide an analysis of the anticipated contractual cash flows including interest payable for the company financial liabilities and derivative instruments on an undiscounted basis. Where interest payments are on a floating rate basis, rates of each cash flow until maturity of the instruments are calculated based on the forward yield curve prevailing at 30 June 2020 and 30 June 2019. In order to align with the group reporting the cash flows of cross currency swaps are presented on a gross basis while all other derivative contracts are presented on a net basis. Financial assets and liabilities are presented gross in the balance sheet, although in practice, the group uses netting arrangements to reduce its liquidity requirements on these instruments.

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

**Contractual cash flows**

	Due within 1 year £ million	Due between 1 and 3 years £ million	Due between 3 and 5 years £ million	Due after 5 years £ million	Total £ million	Carrying amount at balance sheet date £ million
<b>2020</b>						
Borrowings	(566)	(1,098)	(894)	(4,146)	(6,704)	(6,792)
Interest on borrowings	(197)	(341)	(257)	(923)	(1,718)	(44)
Trade and other financial liabilities	(1,911)	—	—	—	(1,911)	(1,911)
<b>Non derivative financial liabilities</b>	<b>(2,674)</b>	<b>(1,439)</b>	<b>(1,151)</b>	<b>(5,069)</b>	<b>(10,333)</b>	<b>(8,747)</b>
Cross currency swaps (gross)						
- Receivable	65	902	89	1,506	2,562	—
- Payable	(41)	(824)	(56)	(1,014)	(1,935)	—
Other derivative instruments (net)	35	73	30	19	157	—
<b>Derivative instruments</b>	<b>59</b>	<b>151</b>	<b>63</b>	<b>511</b>	<b>784</b>	<b>601</b>
<b>2019</b>						
Borrowings	(1,307)	(548)	(1,457)	(1,260)	(4,572)	(4,606)
Interest on borrowings	(148)	(213)	(165)	(698)	(1,224)	(35)
Trade and other financial liabilities	(3,581)	—	—	—	(3,581)	(3,581)
<b>Non derivative financial liabilities</b>	<b>(5,036)</b>	<b>(761)</b>	<b>(1,622)</b>	<b>(1,958)</b>	<b>(9,377)</b>	<b>(8,222)</b>
Cross currency swaps (gross)						
- Receivable	63	125	854	1,503	2,545	—
- Payable	(41)	(82)	(811)	(1,042)	(1,976)	—
Other derivative instruments (net)	10	25	20	15	70	—
<b>Derivative instruments</b>	<b>32</b>	<b>68</b>	<b>63</b>	<b>476</b>	<b>639</b>	<b>336</b>

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)

The company had, along with other financing companies in the group, available undrawn committed bank facilities as follows:

	30 June 2020	30 June 2019
	£ million	£ million
Expiring within one year <sup>(i)</sup>	2,439	—
Expiring between one and two years	610	—
Expiring after two years	2,236	2,756
	<b>5,285</b>	<b>2,756</b>

(i) the group has the rights to extend £813 million of the committed facilities expiring within one year to May 2022.

The facilities can be used for general corporate purposes and, together with cash and cash equivalents, support the group's commercial paper programmes. There are no financial covenants on either of the group's or the company's material short- and long-term borrowings. Certain of these borrowings contain cross default provisions and negative pledges. Negative pledge states that neither Diageo plc ('the guarantor') nor any of its subsidiaries (including the company) shall create encumbrances without the permission of the banks. The committed bank facilities are subject to a single financial covenant, being the guarantor's minimum interest cover ratio of two times (defined as the ratio of operating profit before exceptional items, aggregated with share of after tax results of associates and joint ventures, to net interest). They are also subject to pari passu ranking and negative pledge covenants, applicable to both the guarantor and the borrowers, including the company. Any non-compliance with covenants underlying group'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 borrowings and the inability to access committed facilities. Both the group and the company were in full compliance with its financial, pari passu ranking and negative pledge covenants in respect of its material short- and long-term borrowings throughout each of the years presented.

#### (f) Fair value measurements

Fair value measurements of financial instruments are presented through the use of a three-level fair value hierarchy that prioritises the valuation techniques used in fair value calculations.

The group maintains policies and procedures to value instruments using the most relevant data available. If multiple inputs that fall into different levels of the hierarchy are used in the valuation of an instrument, the instrument is categorised on the basis of the most subjective input.

Foreign currency forwards and swaps, cross currency swaps and interest rate swaps are valued using discounted cash flow techniques. These techniques incorporate inputs at levels 1 and 2, such as foreign exchange rates and interest rates. These market inputs are used in the discounted cash flow calculation incorporating the instrument's term, notional amount and discount rate, and taking credit risk into account. As significant inputs to the valuation are observable in active markets, these instruments are categorised as level 2 in the hierarchy.



**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

The company's financial assets and liabilities measured at fair value are categorised as follows:

	<b>30 June 2020</b>	<b>30 June 2019</b>
	<b>£ million</b>	<b>£ million</b>
Derivative assets	644	377
Derivative liabilities	(43)	(41)
Valuation techniques based on observable market input (Level 2)	<b>601</b>	<b>336</b>

There were no transfers between levels during the two years ended 30 June 2020 and 30 June 2019.

**(g) Results of hedge relationships**

The company targets a one-to-one hedge ratio. Strengths of the economic relationship between the hedged item and the hedging instrument is analysed on an ongoing basis. Ineffectiveness can arise from subsequent change in the forecast transactions as a result of timing, cash flows or value except when the critical terms of the hedging instrument and hedged item are closely aligned. The change in the credit risk of the hedging instruments or the hedged items is not expected to be the primary factor in the economic relationship.

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

The notional amounts, contractual maturities and rates of the hedging instruments designated in hedging relationship as of 30 June 2020 by the main risk categories are as follows:

	<b>Notional amounts £ million</b>	<b>Maturity</b>	<b>Range of hedged rates</b>
<b>2020</b>			
<b>Cash flow hedges</b>			
Derivatives in cash flow hedge (foreign currency debt)	1,667	April 2023 - April 2043	US dollar 1.22 - 1.88
<b>Fair value hedges</b>			
Derivatives in fair value hedge (interest rate risk)	2,831	July 2020 - April 2030	1.38 - 4.83%
<b>2019</b>			
<b>Cash flow hedges</b>			
Derivatives in cash flow hedge (foreign currency debt)	1,614	April 2023 - April 2043	US dollar 1.22 - 1.88
<b>Fair value hedges</b>			
Derivatives in fair value hedge (interest rate risk)	1,560	May 2020 - May 2028	1.84 - 3.08%

With respect to hedges of the cash flow risk from a change in forward foreign exchange rates using cross currency interest rate swaps, the retranslation of the related bond principal to closing foreign exchange rates and recognition of interest on the related bonds will affect the income statement in each year until the related bonds mature in 2023, 2036, 2043. Foreign exchange retranslation and the interest on the hedged bonds in the income statement are expected to offset those on the cross currency swaps in each of the years.

In respect of cash flow hedging instruments, a gain of £221 million (2019 - £180 million) has been recognised in other comprehensive income due to changes in fair value. A gain of £75 million in the income statement has been transferred out of comprehensive income to other finance income (2019 - a gain of £82 million).

The gain on fair value hedging instruments in respect of interest rate swaps for the year was £71 million (2019 - £66 million) and the loss on the hedged items of underlying bonds attributable to the hedged risks was £71 million (2019 - £66 million).

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

**(h) Reconciliation of financial instruments**

The table below sets out the company's accounting classification of each class of financial assets and liabilities.

	<b>Fair value through income statement £ million</b>	<b>Assets and liabilities at amortised cost £ million</b>	<b>Total £ million</b>	<b>Current £ million</b>	<b>Non- current £ million</b>
<b>2020</b>					
Trade and other receivables	—	8,407	8,407	14	8,393
Intra-group derivatives in cash flow hedge	469	—	469	—	469
Intra-group derivatives in fair value hedge	132	—	132	—	132
Intra-group derivatives not designated in a hedge relationship	43	—	43	—	43
<b>Total financial assets</b>	<b>644</b>	<b>8,407</b>	<b>9,051</b>	<b>14</b>	<b>9,037</b>
Borrowings	—	(6,792)	(6,792)	(566)	(6,226)
Trade and other payables	—	(1,955)	(1,955)	(1,955)	—
Intra-group derivatives not designated in a hedge relationship	(43)	—	(43)	—	(43)
<b>Total financial liabilities</b>	<b>(43)</b>	<b>(8,747)</b>	<b>(8,790)</b>	<b>(2,521)</b>	<b>(6,269)</b>
<b>Total net financial assets/(liabilities)</b>	<b>601</b>	<b>(340)</b>	<b>261</b>	<b>(2,507)</b>	<b>2,768</b>

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

**(h) Reconciliation of financial instruments (continued)**

	<b>Fair value through income statement £ million</b>	<b>Assets and liabilities at amortised cost £ million</b>	<b>Total £ million</b>	<b>Current £ million</b>	<b>Non- current £ million</b>
<b>2019</b>					
Trade and other receivables	—	8,001	8,001	36	7,965
Intra-group derivatives in cash flow hedge	283	—	283	—	283
Intra-group derivatives in fair value hedge	63	—	63	3	60
Intra-group derivatives not designated in a hedge relationship	31	—	31	3	28
<b>Total financial assets</b>	<b>377</b>	<b>8,001</b>	<b>8,378</b>	<b>42</b>	<b>8,336</b>
Borrowings	—	(4,606)	(4,606)	(1,306)	(3,300)
Trade and other payables	—	(3,616)	(3,616)	(3,616)	—
Intra-group derivatives in cash flow hedge	(12)	—	(12)	—	(12)
Intra-group derivatives not designated in a hedge relationship	(29)	—	(29)	(3)	(26)
<b>Total financial liabilities</b>	<b>(41)</b>	<b>(8,222)</b>	<b>(8,263)</b>	<b>(4,925)</b>	<b>(3,338)</b>
<b>Total net financial assets/(liabilities)</b>	<b>336</b>	<b>(221)</b>	<b>115</b>	<b>(4,883)</b>	<b>4,998</b>

At 30 June 2020 and 30 June 2019, the carrying values of cash and cash equivalents, other financial assets and liabilities approximate to fair values. At 30 June 2020 the fair value of borrowings, based on unadjusted quoted market data, was £7,324 million (2019 - £4,831 million).

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 10. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)

#### (i) Capital management

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 deliver continued improvement in the return from those investments and by managing the capital structure. The group manages its capital structure to achieve capital efficiency, provide flexibility to invest through the economic cycle and give efficient access to debt markets at attractive cost levels.

### 11. TRADE AND OTHER PAYABLES

	Year ended 30 June 2020 £ million	Year ended 30 June 2019 £ million
Amounts owed to fellow group undertakings	1,911	3,581
Interest payable	44	35
	<b>1,955</b>	<b>3,616</b>

Amounts owed to fellow group undertakings include accrued and capitalised interest on the underlying balances at 30 June 2020 and at 30 June 2019. These balances are repayable on demand and bear interest at fixed and variable rates from 0.0861% to 3.8175% for the year ended 30 June 2020 (2019 - from 0.4914% to 3.8675%).

Amounts owed to fellow group undertakings represent transactions with companies in the group with which the company has a long-term financing relationship. These financing relationships are expected to continue for the foreseeable future. Amounts owed to group undertakings are considered to have a fair value which is not materially different to the book value.

### 12. CALLED UP SHARE CAPITAL AND RESERVES

#### (a) Share capital

	30 June 2020 £	30 June 2019 £
<b>Allotted, called up and fully paid:</b>		
200,000 (2019 - 200,000) ordinary shares of £1 each	200,000	200,000

NOTES TO THE FINANCIAL STATEMENTS (continued)

12. CALLED UP SHARE CAPITAL AND RESERVES (continued)

(b) Hedging reserve

	Hedging reserve £ million
<b>At 30 June 2018</b>	<b>(53)</b>
Effective portion of changes in fair value of cash flow hedges	
- gains taken to other comprehensive income	180
- recycled to income statement	(82)
Tax charge on effective portion of changes in fair value of cash flow hedge	(7)
<b>At 30 June 2019</b>	<b>38</b>
Effective portion of changes in fair value of cash flow hedges	
- gains taken to other comprehensive income	221
- recycled to income statement	(75)
Tax charge on effective portion of changes in fair value of cash flow hedge	(29)
<b>At 30 June 2020</b>	<b>155</b>

13. IMMEDIATE AND ULTIMATE PARENT UNDERTAKING

The immediate and ultimate parent undertaking of the company is Diageo plc which is the ultimate controlling party of the group. Diageo plc is incorporated and registered in England. The consolidated financial statements of Diageo plc can be obtained from the registered office at Diageo, Lakeside Drive, Park Royal, London NW10 7HQ.