A Year of Growth

McDowell & Company Limited

Annual Report 2002-2003

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MERA No.1

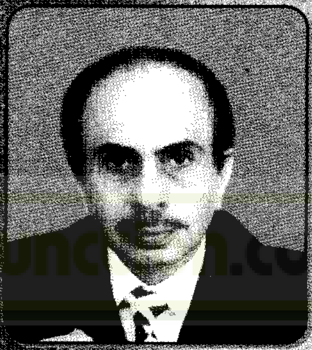
The Year of Growth

McDowell's growth has been exponential. And exceptional ! The primary growth driver at McDowell's has been the ability to change, and the strength to make it happen. As the undisputed leader of the Indian Alcoholic Beverages sector, McDowell's have raised the bar each year to map their performance which has translated into an unbeatable competitive edge. An exhaustive brand portfolio across all flavors, segments and regions, world-class manufacturing facilities, an effective sales, marketing and distribution network - all add to McDowell's potency as India's No.1 beverage alcohol company.

Board of Directors

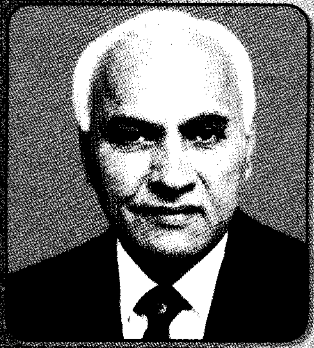
S. R. GUPTE

V. K. REKHI



[illegible] B. GODREJ

B. M. LABROO



[illegible] IYENGAR

P. K. KAKODKAR

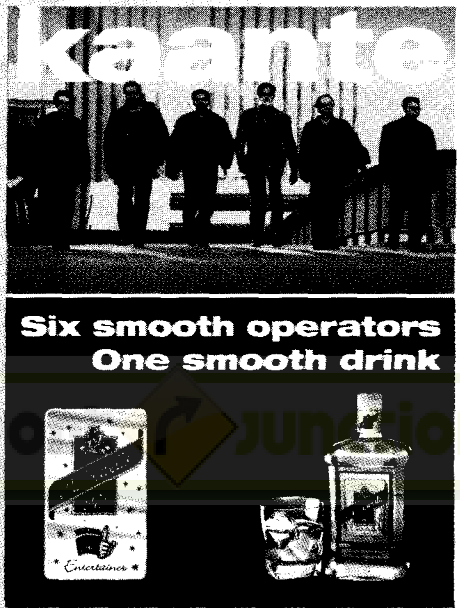
VIJAY MALLYA

Chairman's Statement

Dear Shareholders,

The fiscal year 2002-03 has witnessed a return to fast track growth by McDowell. With sales of 21.2 million cases during the year, your company has recorded a growth of 17% in volumes against a backdrop of the industry that grew approximately by 8%.

Additionally, the year witnessed the acquisition by McDowell of the business of the Gilbey's range of whiskies and allied products from United Distillers and Vintners. This acquisition, which included the popular Gilbey's Green Label brand, adds another millionaire to your company's portfolio, with sales exceeding 2 million cases.



Together with Herbertsons, a sister company, and this acquisition, Group Spirit Sales exceeded 32 million cases thereby positioning UB's Spirits Division as the 5th largest Spirits Company in the world.

Overall growth during the year has been embellished by record breaking performances by various individual brands. I will highlight the signal achievement of selling over 10 million cases under the McDowell's No.1 umbrella comprised of whisky, brandy and rum during the year.

The repositioning of Signature has been another significant success and this brand today has captured a market share of 21%, challenging the long standing leadership of Shaw Wallace's Royal Challenge in this category.

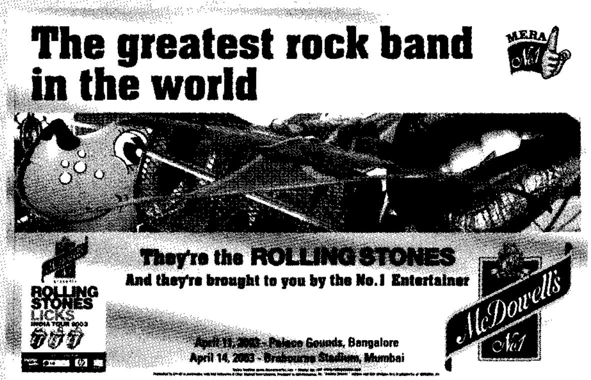
These milestones have been made possible by continual investments by your company, on the one hand in brand development, and on the other in enhanced manufacturing facilities. While the brand imagery has created levels of expectation for products on the house of McDowell, it has been your company's constant endeavor to ensure that products of high quality are delivered consistently from the most efficient manufacturing source to the consumers. In pursuance of this objective, McDowell now manufactures its products from nearly 40 distilleries spread across the country. The Group units are ISO certified and your company is in the process of ensuring quality and process certification for contract bottling units as well. Investments are being made both in the manufacturing capacity as well as to ensure that your company nurtures the environment in which it operates through safe discharge of effluents. Recent investments into manufacturing and effluent treatment facilities have totaled nearly Rs 55 crores.

To appreciate these achievements of your company it is necessary to understand the harsh and sometimes hostile environment in which the Beverage Alcohol Industry continues to operate. With 29 States and Union Territories framing their own regulations and tax policies, which often change dramatically from year to year, the industry is often at a loss in planning for growth and investment.

65% of the industry is directly controlled by State Governments in as much as the entire off-take is canalized through parastatal Corporations who are the sole intermediaries. The traditional reluctance of the governments to increase purchase prices coupled with the power of monopoly buying and the well known penchant of bureaucrats to frame infructuous regulations combine to make a lion's share of the industry unattractive and challenging. An even more pernicious system of private monopolies encouraged by the State exists in certain parts of north India, notably in Rajasthan, Haryana and Punjab. In these States the Government auctions retail territorial monopolies to individuals or cartels who then engage in ruthless profiteering at the cost of denying the consumers any choice at all. The industry then falls victim to the greed of these monopolies. Indeed, in some cases, your company has taken a conscious decision not to supply its products rather than succumb to the demands of these cartels. Your company's sales growth, therefore, needs to be appreciated in this context.

There has been dramatic consolidation in the glass bottle industry in India, consequent to which one player now dominates the industry with over 50% market share. It is understood that this company is engaged in discussions to further adding to its capacity and consequently enhance its dominance. This near monopoly has resulted in a steep increase in input costs for the industry as a whole. Various alternatives and options are under active consideration.

The uncertainties caused by the announcement of a VAT regime, combined by differing stands taken by various states with regard to the inclusion of the Alcohol Beverage Industry in the scheme of VAT, had led to a near paralysis of the industry in the early period of the current fiscal year. Although the imposition of the VAT has been postponed for the time being, grave concerns persist as to the implications of a national VAT on a State tax subject which however, depends on key inputs from sources outside the manufacturing state. Once again, this issue is being addressed with the Union Government.



Your company has long championed the need for a level playing field between the domestic manufacturers and international distilleries who have been lobbying intensively with the Central Government to bring down the levels of import duty. The domestic industry is subject not only to a wide variety of taxes and levies, but also to a number of non financial burdens, such as the need to print state of origin and state of consumption on packaging. Multilingual printing of labels is yet another example of a non fiscal burden imposed upon the domestic industry which is currently not applicable to imported products. Various representations have been made in this regard.

It would be readily appreciated from what I have said that the fortunes of your company, and indeed all other companies in the Beverage Alcohol space, are highly dependent on the vicissitudes of the regulatory frame work in which we operate. Recognizing the important role that the Government has to play in the future of the industry, McDowell is working closely within industry bodies to ensure that the regulatory authorities are sufficiently equipped with facts and data to ensure a more consistent and practical frame work for the future.

At the same time, your company remained focused on its primary objectives of delivering to the consumer the widest possible choice across flavours and price segments, ensuring at all times the highest quality, at the most affordable prices. Given the significant incidents of spurious products, largely made possible by over regulation and loose policing, McDowell has been leading efforts to protect its consumers. Apart from educating consumers on ways to spot spurious products, your Company is investing in multiple technologies to ensure that its packaging is pilfer and tamper proof. This is an ever evolving process and McDowell is using the latest available technology in the world to ensure safety and originality of its offerings.

Keeping with its international appeal, your Company has recently associated itself with mega events featuring Sir Elton John and the Rolling Stones. These are precursors of a well conceived marketing effort which will seek to reinforce the imagery of your Company's brands by association with global icons.

The profit for the year was depressed by the need to provision a large amount due from a contract bottling unit whose business was taken over by the Government of Bihar. In keeping with the current emphasis on conservative accounting, your Board considered it prudent to make a provision of almost Rs 7 crores on this account.

Despite the constraints and travails facing the industry, your company is better placed than others to ensure sustainable growth in both top and bottom lines in the future.

In conclusion, I would like to record my appreciation to my colleagues on the Board as also various Stakeholders of the company including Employees, Consumers, Distributors, Shareholders and the Financial Community.

Vijay Mallya
Chairman

Team


V. K. REKHI


RAVI NEDUNGADI


ASHWIN MALIK


ASHOK CAPOOR


P. A. B. SARGUNAR


D. BANERJEE


NAVRATAN DUGAR


HARISH BHAT


GERALD G. D'SOUZA


ALOK GUPTA


DR. B. K. MAITIN


ANANT IYER


J. P. SURESH MENON


V. S. VENKATARAMAN


VIVEK PRAKASH

DIRECTORS

VIJAY MALLYA,
Chairman

S.R. GUPTE,
Vice Chairman

V.K. REKHI,
Managing Director

M.R. DORAISWAMY IYENGAR

A.B. GODREJ

P.K. KAKODKAR

B.M. LABROO

GROUP CHIEF FINANCIAL OFFICER
RAVI NEDUNGADI

COMPANY SECRETARY
V.S. VENKATARAMAN

AUDITORS
DELOITTE HASKINS & SELLS, CHARTERED ACCOUNTANTS, BANGALORE

REGISTERED & CORPORATE OFFICE
51, RICHMOND ROAD
BANGALORE - 560 025

REPORT OF THE DIRECTORS

Your Directors have pleasure in presenting the Annual Report of your Company and the audited accounts for the year ended 31st March, 2003.

FINANCIAL RESULTS

Rupees in Millions

	2002-03	2001-02
The working of your Company for the year under review resulted in		
• Profit from operations	415.906	397.965
Less :		
• Depreciation	(125.263)	(108.787)
• Taxation (including deferred tax liability)	(159.501)	(131.484)
• Profit after tax	131.142	157.694
Profit B/F from previous year	382.199	340.445
Profit available for appropriation	513.341	498.139
Your Directors have made the following appropriations :		
To General Reserve	(13.500)	(12.500)
Proposed Dividend	(103.440)	(103.440)
Corporate Tax on Proposed Dividend	(13.253)	—
Balance carried to the Balance Sheet	383.148	382.199
EPS – Basic - Rupees	2.54	3.05

Your Directors propose a Dividend on equity shares @ 20%.

CAPITAL

During the year under review the Authorised and Issued, Subscribed and Paid Up Capital of the Company remained unchanged at Rs. 600,000,000 and at Rs. 517,200,280 respectively.

PERFORMANCE OF THE COMPANY

The year 2002-03 saw your Company extending its leadership position in the country's IMFL market with volumes of 21.22 million, recording a growth of 17% over the previous year. The industry, on a comparable basis grew by around 8% enabling your Company to enhance its market share to 26%.

McDowell's No. 1 range comprising of whisky, rum and brandy achieved a significant milestone crossing 10 million cases with a combined growth of 14%. McDowell's No.1 Whisky with an individual record of 4.24 million cases remains the flagship brand of the Company. McDowell's No. 1 Celebration Rum which grew by 21% to 3.53 million cases has been recognized as among the fastest growing regional brands in the world.

As part of its ongoing process of focusing on key brands, your Company conducted internal exercise in brand transformation. This has seen the revamping in the packaging of some of the major brands and identification of key brands such as McDowell's No.1 Whisky and McDowell's Signature with unique and prestigious events such as the music concerts featuring Sir Elton John and the Rolling Stones and the Signature Golf Club Championship.

Building on your Company's established strengths in distribution and manufacturing, your Company has expanded total manufacturing facilities under its control to 38 spread across all consuming states. All the owned manufacturing units are ISO certified. Your Company's Technical Centre has developed a range of ready to drink low alcohol beverages and manufacturing capacity has been created for the purpose of encashing on this fast expanding segment.

Your Company continues to be on the forefront of the battle against spurious manufacture of alcohol beverage products. It has taken the lead in working with suppliers of packaging materials to introduce tamper proof packaging making duplication difficult.

PROSPECTS

Sales in the initial period of the current year were disrupted by certain regulatory changes primarily the anticipated introduction of VAT and the imposition of a new Tax Collection at Source.

Despite these, sales of your Company's products during the first quarter were higher than the corresponding period of the previous year.

Barring unforeseen circumstances, operations are expected to be satisfactory.

ENTERPRISE RESOURCE PLANNING (ERP)

Your Company has gone live with SAP R/3 at all locations in South India. Implementation for the entire organization is scheduled to be completed by December 2003.

Once fully implemented, the system will help in managing costs, increasing transparency and consistency of information for the benefit of both the Management and the Shareholders.

SUBSIDIARIES

During the year under review the following Companies became wholly owned subsidiaries of your Company:

1. Phipson Distillery Limited, consequent upon the purchase of 50,000 Equity Shares of Rs.10 each from the existing shareholders of the Company and

REPORT OF THE DIRECTORS (Contd.)

2. Asian Opportunities and Investments Limited in Mauritius, consequent upon the purchase of 8 Ordinary Shares of USD 1 each from the existing shareholders. Your Company further subscribed to 4,998,698 new Ordinary Shares of USD 1 each in the share capital of Asian Opportunities and Investments Limited.

During the year under review, your Company subscribed to 49,400 new Equity Shares of Rs.10 each in the share capital of McDowell International Brands Limited, your Company's wholly-owned subsidiary.

Triumph Distillers and Vintners Private Limited became an ultimate subsidiary of your Company consequent upon it becoming a subsidiary of Phipson Distillery Limited, your Company's wholly-owned subsidiary.

In December 2002, your Company's ultimate subsidiary, Triumph Distillers & Vintners Private Limited acquired the Indian and Middle East businesses of Gilbeys from UDV. Gilbey's Green Label is a popular brand of whisky in the regular segment with sales of over 2 million cases. It was seen as a useful addition to your Company's portfolio brands as it enjoyed certain price advantages in the whisky category. The business of Gilbey's Green Label and other allied brands is carried out under the banner of Triumph Distillers and Vintners Private Limited which is 85% owned by Phipson Distillery Limited, your Company's wholly-owned subsidiary. The balance 15% is owned by management, though a Call Option of this 15% shares exercisable at the end of 2 years is retained.

The business of this newly acquired brand has shown strong growth and is expected to add to the profitability and cash flows of your Company in future.

In terms of the Income Tax Act of Nepal, the accounting year of Nepal Liquors Limited (NLL), the Company's subsidiary is from mid July to mid July every year. Accordingly, the accounting year 2001-02 of NLL ended on July 16, 2002 and the accounting year 2002-03 ended on July 16, 2003 i.e. after the end of the close of the financial year of the Company which ended on March 31, 2003.

For the purpose of compliance under AS-21 "Consolidated Financial Statement", the accounts of NLL has been drawn up to March 31, 2003.

In terms of the approval received from the Government of India pursuant to Section 212(8) of the Companies Act, 1956, the Balance Sheet, Profit & Loss Account, Directors' Report, Auditors' Report and other particulars of the subsidiary companies have not been attached with the accounts of the Company. The documents/details will be made available to any Member upon request to the Company.

For the purpose of compliance under AS-21 – "Consolidated Financial Statement" presented by the Company includes the financial information of its subsidiaries.

DEPOSITORY SYSTEM

The trading in the shares of your Company are under compulsory dematerialisation mode. As of date, shares representing 87% of the share capital are in dematerialised form. As the depository system offers numerous advantages, members are requested to take advantage of the same and avail of the facility of dematerialisation of the Company's shares.

DIRECTORS

Mr. M.R.Doraiswamy Iyengar and Mr. P.K. Kakodkar retire by rotation and being eligible, offer themselves for re-appointment.

AUDITORS

M/s. Deloitte Haskins & Sells, your Company's Auditors are not seeking re-appointment at the forthcoming Annual General Meeting. Your Directors place on record their appreciation of the valuable services rendered by them during their tenure as Auditors of your Company. It is proposed to appoint in their place, M/s. Price Waterhouse, Chartered Accountants, as the Statutory Auditors to hold office from the conclusion of this Annual General Meeting till the conclusion of the next Annual General Meeting.

M/s. Price Waterhouse, Chartered Accountants, have consented to be the Auditors of the Company if appointed by the Members at the Annual General Meeting and have also confirmed that their appointment would be within the limits specified under Section 224 (1-B) of the Companies Act, 1956.

AUDITORS' REPORT

With regard to the observations of the Statutory Auditors in the accounts for the year ended March 31, 2003 in regard to

a) dues from toll manufacturers; these toll manufacturers continue to be a source for substantial volume for the Company. Consequently, the Company has been able to make some progress in reducing the outstandings during 2002-03. Steps are also being taken during the current financial year to recover the dues including current dues in a phased manner.

b) advances to third parties; the Company expects to recover/settle dues during the current financial year.

c) diminution in value of investments; The diminution in value of investments is considered to be temporary in nature, in view of the strategic nature of the investments and the operating plans of the Company.

REPORT OF THE DIRECTORS (Contd.)

LISTING OF SHARES OF THE COMPANY

The shares of your Company are listed on Bangalore Stock Exchange Limited (Regional Exchange), The Stock Exchange - Mumbai, National Stock Exchange of India Ltd., Madras Stock Exchange Limited, The Delhi Stock Exchange Association Ltd., The Calcutta Stock Exchange Association Ltd. and The Stock Exchange - Ahmedabad. The listing fees for the year 2003-04 have been paid to all these Stock Exchanges.

CORPORATE GOVERNANCE

A report on Corporate Governance is annexed separately as part of the report along with a Certificate of Compliance from the Auditors.

FIXED DEPOSITS

Fixed Deposits from the public and shareholders stood at Rs. 543.013 million as at March 31, 2003. The amount included Rs. 3.686 million representing matured deposits for which disposal instructions had not been received from concerned depositors. Of this a sum of Rs. 0.191 million has been since paid as per instructions received after the year end.

TRANSFER TO INVESTOR EDUCATION AND PROTECTION FUND

In terms of Section 205C of the Companies Act, 1956 an amount of Rs. 6,274,992.13 being the unclaimed Dividend, Debentures and Deposits remaining unclaimed and unpaid for more than 7 years, were transferred to the Investor Education and Protection Fund.

HUMAN RESOURCES

Employee relations remained cordial at all Company's locations.

Particulars of employees drawing an aggregate remuneration of Rs. 2,400,000 or above per annum or Rs. 200,000 or above per month, as required under Section 217 (2A) of the Companies Act, 1956 are annexed.

EMPLOYEE STOCK OPTION SCHEME

The Company has not offered any stock option to the Employees during the year 2002- 03 either under the McD ESOP Scheme or McD - Employee Stock Option Scheme – 2002.

CONVERTIBLE WARRANTS

Your Company held 2,640,500 Convertible Warrants of United Breweries (Holdings) Limited [formerly United Breweries Limited] of Re.1 each with right to apply for by March 31, 2003 and be allotted 2,640,500 Equity Shares of Rs.10 each at a premium of Rs. 25 per share. These warrants have since lapsed by efflux of time.

CONSERVATION OF ENERGY & TECHNOLOGY ABSORPTION ETC.

In accordance with the provision of Section 217(1) (e) of the Companies Act, 1956, the required information relating to Conservation of Energy, Technology Absorption and Foreign Exchange Earnings and Outgo is annexed.

DIRECTORS' RESPONSIBILITY STATEMENT

Pursuant to Section 217 (2AA) of the Companies Act, 1956, in relation to financial statements for the year 2002-03, the Board of Directors reports that:

- in the preparation of the annual accounts, the applicable accounting standards have been followed along with proper explanation relating to material departures;
- accounting policies have been selected and applied consistently and that the judgements and estimates made are reasonable and prudent so as to give a true and fair view of the state of affairs of the Company as at the end of the financial year and of the profit of the Company for the year ended March 31, 2003;
- proper and sufficient care have been taken for the maintenance of adequate accounting records in accordance with the provisions of the Companies Act, 1956, for safeguarding the assets of the Company and for preventing and detecting fraud and other irregularities;
- *the annual accounts have been prepared on a going concern* basis.

THANK YOU

Your Directors place on record their sincere appreciation for the continued support from shareholders, customers, suppliers, banks and financial institutions and other business associates. A *particular note of thanks to all employees of your Company,* without whose contribution, your Company could not have achieved the year's performance.

By Authority of the Board

Bangalore
August 19, 2003

DR. VIJAY MALLYA
Chairman