

The logic behind Diageo

Diageo, the product of a £23.8bn merger between Grand Metropolitan and Guinness in December 1997, is one of the world's top 20 consumer goods companies. Andrew Don met John McGrath, the 60-year old chief executive of Britain's 9th biggest company and the world's largest alcoholic drinks business.

John McGrath presents well - affable, charming, almost grandfatherly. And the grandfather of Diageo is exactly how he sees himself. The executives running the four constituent companies are the fathers and everyone reporting into them are the grandchildren.

"If you change any of the grandchildren it's done with my agreement. If you want to promote anyone into a grandchild position or change their salary, I get involved," he says.

Break through the veneer and you get the feeling he has state-of-the-art micro-processors behind his spectacles - a Mr Spock of the business world, if you like.

His 1st class honours in applied physics and mathematics from Brunel University is clue to his intellect and his logic. He enthuses the people who work with him but some say he can be a bit overpowering, too. "He's on a different level to the rest of us," one analyst says. "I wouldn't want to be on the other side of the negotiating table with him," says another.

McGrath takes this positively. "I'm a half-full glass man rather than a half-empty one. When people ask me to describe myself I tend to say I'm firm but fair. I'm not actually in a negotiation interested in really screwing the other side. If you are trying to come to an agreement the best are usually those which are a balance to both sides."

The merger between Guinness and Grand Metropolitan was announced on May 12 1997 and completed December 17. It bought together big international brands such as Johnnie Walker, Smirnoff, J&B, Gordon's, Old El Paso, Haagen-Dazs, Guinness and Green Giant, within four divisions, UDV, Pillsbury, Guinness and Burger King.

It boasts a reach across more than 200 countries and figures in a first division of world-class consumer goods giants such as Unilever, Nestlé, McDonald's, Coca-Cola and Procter & Gamble.

McGrath's ambition is to catapult the company into the top five of a peer group



of 20 of the world's leading consumer goods companies in terms of the total return generated for shareholders. It is currently in about 12th place.

He plans to double shareholder value by 2002 by setting what has been coined Hairy Audacious Targets (HATS) - not one of his own expressions but a term coined by group strategy director Jim Grover - and by utilising a technique called managing for value.

"Managing for value measures the profit and loss accounts and the balance sheet in one number so it takes account of the efficiency of the capital you employ as well as the profitability," he explains. He believes it is "a powerful weapon" to help group profits organically.

HATS are a system of aggressive targets which he sees as motivational and behaviour - changing. "Incremental behaviour such as I am going to grow by 7% is not on people's horizons any longer - why not 12% or 15% - that sort of thing - and we have slayed some of the sacred cows as we are going along. These are things where you say, well we've always done it that way."

McGrath has had a varied career path which has taken in the United Kingdom Atomic Energy Authority and the National Coal Board. He has worked for Ford Motor Company, Jaguar Cars, British Leyland,

Stone-Platt, CompAIR, IC Gas and Cookson.

His path to Diageo began in 1988 when he moved to International Distillers and Vintners (IDV), the drinks division of Grand Metropolitan as joint managing director, responsible for GrandMet Brewing, IDV UK and Heublien.

He became managing director and chief operating officer of IDV at the beginning of 1991 and a year-and-a-half later was appointed chief executive of IDV and a director of Grant Metropolitan.

He rose to become chairman and chief executive of the former and chief executive of the latter in March 1996. When the merger between Guinness and GrandMet was announced, McGrath was the obvious choice to head it up.

SO WHAT GOT HIM THERE?

He says if you look at the background to people running big businesses they come from all sorts of disciplines.

"I think one serious benefit in having a degree in applied physics and mathematics is that you are very logical which is extremely annoying to one's wife but is extremely valuable in business because you are much more able than some people to decide very quickly what is more significant and what isn't."

He says the downside is that people who are more logical are potentially less emotional but adds he can be emotional too when needed. He believes he was probably born with his logic but that the disciplines of applied physics and mathematics enforced this.

He hated working for UK Energy Atomic Energy Authority. He was conducting research in small areas of big projects and disliked not having any idea of the big picture.

It was at Ford that he came into his own. "It was the best thing I ever did," he says.

In the late 1960s Ford was known as the best business school in Europe. "I remember John Barber [finance director of Ford of Britain] saying that in Ford you

can produce extraordinary results from ordinary people and that is true because the system was so powerful I thought it was invaluable training. It taught me accountability. If anything was done you could always nail it to one person."

He says Ford taught him how tough he needed to be in business not just with people but with decisions and acquiring the correct facts to make correct decisions. "I will never forget that experience," he says.

McGrath claims he had no inkling that he would end up as head of such a large business empire. "I thought at about 30 when I was at Ford and in the finance function that I would like to run something but I had not actually sorted it out in my own mind at that time."

When asked what it is that has driven him he replies: "I suppose I am pretty determined. I try and identify two or three things that have to be done and concentrate on them. I am not very good at going for hundreds of different things but you can find out a few things that are fairly fundamental and undo them."

He does not like to know all the minutiae and people in the company who earn a fair amount of autonomy get it, he says. "I've got four chief executives of the four business reporting to me. The first rule is they must not surprise me. If there are issues they must alert me early on. I don't want to hear the problems only. I want to hear the problems with what they intend to do about them. They get a fair amount of space and most people like that."

"At the end of the day I don't spend much of my life on day-to-day operational issues because it is the job of the guys running the businesses to deliver the profits."

What interests him are the strategies which they are developing and if there are changes of direction to understand why.

"At the end of the day there are a bunch of people keeping the wheels turning but it is the direction you are going in that really matters."

He spends a lot of time on people issues, on their selection and being satisfied or otherwise with their

performance. "What I have found is that the fastest way of turning businesses around is to get the right people in the job. I am a great believer that the fish stinks from the head. If the guy at the top is wrong you've got a cascade of problems."

"You get the person at the top right and he starts changing people. When new ones come in, they start looking at their people"

He says Burger King was plagued with problems until Dennis Malamatinas went in 21 months ago as chief executive. "The transformation that company's made is tremendous.

"You see a lot of companies that just put up with mediocrity and what do you finish up with? Mediocre results."

McGrath hires an industrial psychologist to find out what staff think of him.

One of the comments that came back was that McGrath tends to express views strongly

which can deter people from coming forward.

"Because I have lived in very challenged cultures in the past then you have to be slightly more sensitive but you have to be forceful."

Diageo's focus is to develop main brands that are first or second in their markets. Burger King was third in France so it got out in the second quarter of 1998.

Some analysts question the potential for brown spirits but McGrath points out that Johnnie Walker Black is doing well in the US in the premium sector and J&B a standard scotch whisky is performing well in Spain and Johnny Walker Red in Greece.

He admits the economic crisis in Asia-Pacific had wounded the company but gives Jack Keenan, chief executive of UDV, much credit for minimising the damage.

Some in the market bought back their goods for fear they would flood other markets cheaply devaluing their brands. But McGrath said Diageo bought back spirits from one distributor because he had too much stock and would have had difficulty with liquidity.

"We got virtually no bad debts and our inventories are under control."



Analysts are disappointed with Pillsbury where volumes were down last year mainly because of declines in lower margin categories in North America.

McGrath says Pillsbury has come under competitive pressures in Mexican Foods, desserts, baked mixes and canned vegetables, but it is just a temporary blip. Action has been taken to put it right and Pillsbury will be back on track in 1999.

About 3% of Pillsbury brands and 5% of spirits brands by sales value will probably be shed in the first half of next year.

He is keen to buy a food service business in the US in dough-based technology and he wants to pick up businesses in the international market for Pillsbury dough-based products similar to small acquisitions it has made in Brazil, Argentina, Hong Kong and Australia."

DIAGEO'S PEER GROUP:

WORLD LEADING CONSUMER GROUP COMPANIES

	Market cap.* £ billion
Coca-Cola	105
Procter & Gamble	66
Philip Morris	63
Johnson & Johnson	61
Unilever	45
Nestlé	42
Pepsi-Co	39
Gillette	38
Diageo	24
McDonald's	23
Campbell Soup	16
Anheuser Busch	14
Heinz	13
Kellogg	11
Best Foods	10
Seagram	8
Heineken	7
Allied Domecq	6
Tricon	3
Carlsberg	2

*based on share prices and exchange rates as at 13.3.98

"If groups of restaurants become available in small numbers to enlarge where we have grown with Burger King I would not mind that."

He is doubtful that Diageo will make acquisitions in spirits although he envisages established joint ventures with local companies in developing countries.