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> ECONOMIC SUSTAINABILITY

2.1 Reporting basis

The information presented in this chapter relates to 2002 and 2003 and the operating companies and participating interests included in the consolidated financial statements.

Heineken N.V. and the operating companies and participating interests with which it forms a group are fully included in the consolidated balance sheet and profit and loss account, with minority interests in group equity and group profits shown separately. Proportional consolidation is applied in the case of participating interests in which Heineken has a direct interest and exercises a controlling influence on management decisions together with other shareholders.

2.2 Economic policy and governance

Responsibility for management within the Heineken group of companies is centralised at Heineken N.V. Executive Board level. Reporting lines are short: all corporate directors and managers of the larger operating companies in the group report directly to the Executive Board.

Regular meetings are held between the members of the Executive Board, corporate directors and operating company managers at which operating performance and other important topics are discussed. Each year, the operating companies prepare a three-year operational plan, in which targets are defined in terms of a series of performance indicators, such as EBIT (earnings before interest and taxes), EBITDA (earnings before interest, taxes, depreciation and amortisation), market share, brand volume, ENP (economic net profit) and RIOC (return on invested capital).

The larger operating companies report weekly on production volumes. Profit and loss statements are

submitted monthly and reports on cash flow, balance sheet and performance indicators are submitted quarterly.

2.3 Dialogue with stakeholders

In maintaining its dialogue with the various target groups which it addresses around the world, Heineken pursues an active communication and investor relations policy and provides full and accurate information. Heineken aims to publish both financial and non-financial information on time and in a consistent manner. This is done via a wide range of communication media, including press releases, presentations and webcasts via its website (www.heinekeninternational.com), which guarantees simultaneous access to the information.

The information which Heineken provides to shareholders includes current and historical share prices and stock calculations, important facts and figures and brokers' forecasts. The company also maintains regular contact with analysts. On the basis of surveys of existing shareholders, potential investors and analysts, a number of presentations for institutional investors and financial analysts are held each year, in Amsterdam and in the main financial centres outside the Netherlands.

Dozens of investor relations presentations were given in 2003. The analysts' meeting held at the time of publication of the full-year and interim results were broadcast directly via the website. Heineken also held presentations at many major international conferences for institutional investors, the most important of which were also relayed via the website. In addition to the annual general meeting of shareholders, Heineken organised other activities in 2003 for private shareholders, most of whom are from the Netherlands, including a number of presentations and site visits. Heineken took part in several meetings

2.4 Key Figures

Results in millions of euros	2003	2002*	%
Net turnover	9,255	8,482	9.1
Operating profit	1,222	1,282	-4.7
EBITDA ¹	1,866	1,811	3.0
Net profit	798	795	0.4
Dividend	157	157	-
Cash flow from operating activities	1,637	1,184	38.3

Balance sheet in millions of euros

Total assets	10,897	7,781	40.0
Group assets	3,899	3,030	28.7
Shareholders' equity	3,167	2,637	20.1
Issued capital	784	784	-

Per share of €2.00

Number of shares issued	391,979,675	391,979,675	-
Cash flow from operating activities	4.18	3.02	38.3
Net profit	2.04	2.03	0.4
EBITDA ¹	4.76	4.62	3.0
CEPS ²	2.11	2.03	3.9
Dividend	0.40	0.40	-
Shareholders' equity	8.08	6.73	20.1

Net turnover including interregional sales, in millions of euros

Western Europe	6,560	6,232	5.3
Central/Eastern Europe	1,145	898	27.5
The Americas	1,501	1,361	10.3
Africa/Middle East	876	819	7.0
Asia/Pacific	467	489	-4.5

Tangible fixed assets in millions of euros

Investments less disposals	611	696	-12.2
Amortisation, depreciation and value adjustments	560	481	16.4

Staff in numbers

Average number of employees	61,271	48,237	27.0
of whom, employed by Dutch operating companies	5,256	5,527	-4.9

¹ Earnings before interest, taxes, depreciation and amortisation

² Cash earnings per share (net profit on ordinary activities per share before amortisation of goodwill)

* The 2002 figures have been restated for comparison purposes

Ratios	2003	2002*
Operating profit as % of net turnover	13.2	15.1
Operating profit as % of total assets	11.2	16.5
Net profit as % of shareholders' equity	25.2	30.1
Dividend as % of net profit	19.7	19.7
Group equity/other borrowed capital	0.56	0.64
Group equity/fixed assets	0.54	0.61
Current assets/current liabilities	1.25	1.10
Interest coverage ratio	9.5	12.2



Geographical distribution excluding affiliated breweries

Region	Volume		Operating profit		Employees	
	1,000 hl		€ million		average FTEs	
	2003	2002	2003	2002	2003	2002
Western Europe	44,727	42,242	584	553	20,076	19,460
Central/Eastern Europe	20,611	15,671	83	78	14,829	8,507
The Americas	12,511	8,380	358	416	1,534	1,451
Africa/Middle East	12,706	10,558	149	188	11,378	10,462
Asia/Pacific	8,413	7,997	48	47	1,316	1,377
Total	98,968	84,848	1,222	1,282	49,133	41,257

for private shareholders which were organised by third parties. With the placing of the bond loan in the second half of 2003, a start was made on extending the investor relations programme to include bondholders.

2.5 Risk management

Heineken’s activities centre around a single product: beer. Although the resulting consistency, comparability and standardisation have a positive impact on Heineken’s overall risk profile, its operating companies work in many different environments, markets and cultures and its activities worldwide are exposed to varying degrees of risk and uncertainty. Some of the key risks, as identified by Heineken, are discussed below.

Net turnover 2003 in billions of euros

Beer	7.3
Soft drinks	1.0
Wines and spirits	0.6
Other	0.3

Reputational risk

Heineken enjoys a sound corporate reputation and most, if not all, of our operating companies are well respected in their region. The Heineken brand is key to Heineken’s growth strategy. Anything that adversely affects consumer confidence in the Heineken

brand could have a negative impact on the overall business. Production and logistics are subject to rigorous quality standards and monitoring procedures. Constant management attention is directed towards enhancing Heineken’s social and environmental reputation. A set of standards, including a crisis management policy, and regular monitoring procedures have been put in place or are being established to achieve this.

Currency risk

Heineken has operations in over 170 countries and reports in euros. Exchange-rate movements can have a material impact on Heineken’s financial results, particularly movements in the exchange rate between the euro and the US dollar and related currencies.

Exchange rate and interest rate hedging operations are governed by strict rules. Because of the historically low interest rates in 2003, Heineken opted to fix the interest rates on a large proportion of the contracted loans. Transaction risks are limited to some extent by financing in local currencies. Transaction risks arise mainly on cash flows in foreign currencies generated by export activities. The most important foreign currency cash flow is in US dollars. After deduction of dollar-denominated costs, a net cash flow in US dollars remains. This cash flow is hedged well in advance by means of a combination of forward contracts and options. This policy reduces the volatility of export results due to short-term fluctuations in the value of the US dollar against the euro. Transactions are entered into with a limited number of counterparties with excellent credit ratings. The activities are closely monitored, independently of implementation.

The foreign exchange hedging operations in 2003 produced an average exchange rate of 0.96 US dollars to the euro on a total of 795 million US dollars. The expected net cash flow in 2004 amounts to approximately 800 million US dollars. As at 31 December 2003, 544 million US dollars of the expected 2004 cash flow had been hedged at an average exchange rate of 1.09 US dollars to the euro. The expected cash flow for 2005 was unhedged as at 31 December 2003.

Brau Union environmental reporting

Brau Union Austria’s transparency earns respect



Brau Union Austria goes well beyond the minimum legal requirements by publishing both external and internal environmental reports. By comparing the performance of the various breweries, the internal report sets a benchmark to which all aspire. Brau Union Austria also presents three annual awards, one for the best-performing brewery, one for the most-improved brewery and one for individual effort.

Interest rate risk

Heineken attempts to hedge results and cash flows against interest rate fluctuations as far as possible by financing either at fixed rates or at variable rates combined with the use of interest rate instruments, namely interest rate swaps, forward rate agreements, caps and floors.

Taxation risk

Heineken and its operating companies are subject to a variety of local excise and other tax regulations. In principle, Heineken's sales prices are adjusted to reflect changes in the rate of excise duty, but increased rates may have a negative impact on sales volume.

Internal governance

Internal governance is based on the underlying principle of local management's accountability for managing performance and the underlying risks, within the boundaries set by the Executive Board. Local management is responsible for an effective internal control system, which is designed to provide reasonable assurance of achieving the business objectives and prevent or ensure early identification of potential material errors and losses and misrepresentation of circumstances.

Policies for the control of worldwide risks in areas such as marketing, production, human resources, finance, IT, environmental and social responsibility and legal affairs are in place or are being developed. These elements are part of the reporting cycle. Heineken is making good progress with the development and implementation of uniform group-wide processes and systems, in order to ensure consistency and standardisation based on best practices.

The Executive Board, under the supervision of the Supervisory Board and more particularly its Audit Committee, oversees the effectiveness of internal governance, including managing risks and monitoring the effectiveness of internal controls. Group Internal Audit, together with local internal audit departments, plays a critical role in the objective and independent assessment of business processes and the effectiveness of internal control.

2.6 Quality assurance

The raw materials from which our beer is produced are required to meet high quality standards laid down in our recipes and specifications. The packaging materials in which our beer is sold are also subject to strict quality standards which comply as a minimum with the statutory guidelines. The Heineken Values and Principles are enshrined in policy statements and translated into instruction which define how policy is implemented and compliance is monitored.

In accordance with Heineken's product safety policy, appropriate measures are taken in our brewing process to prevent product contamination. Our breweries are required to implement the principles of the HACCP (Hazard Analysis and Critical Control Points) system. Our raw materials policy requires suppliers to operate a system based on these principles and compliance is verified by supplier audits. We work with farmers to minimise their pesticide inputs and we pursue a biotechnology policy that prohibits the use of genetically modified raw materials, which is monitored. Consumables likewise must present no product safety hazard, and we conduct audits of suppliers to identify and minimise risks. The water used by our breweries must comply with all EU or WHO drinking-water standards. To ensure that our beer reaches the consumer in perfect condition, we operate a freshness policy, which relates mainly to our distribution channels. All products are coded so that they can be traced throughout the supply chain, facilitating the identification of the source of any problems which may arise.

Alcohol Policy Day

Heineken Nederland brings home to students the importance of responsible alcohol use



Many student clubs in the Netherlands have no policy for explaining to their members the importance of responsible alcohol consumption. This year, Heineken Nederland organised an Alcohol Policy Day for student clubs, to explain why such a policy is essential. Heineken Nederland has since been asked by several clubs to provide training in this area for the mentors who run the induction programmes for first-year students.

The effectiveness with which these policy measures are implemented at local level is monitored centrally by analysing beer samples and conducting organoleptic tests in the laboratory and checking the 'best before' dates on samples of products on sale, thus ensuring that the product delivered to the consumer is safe and fresh. Consumer complaints are recorded and dealt with in accordance with our complaints procedure. A recall is ordered if, despite all our efforts, a defective product finds its way to the market.

To encourage our breweries to make an extra effort to give the consumer an excellent product, our breweries take part in an internal Quality Awards programme, under which the quality of the beer and packaging on the market is assessed by an independent external body.

2.7 Code of conduct

Heineken's policies on ethical business practices, in particular with regard to corruption, gifts, fraud and conflicts of interest, has been reviewed in the past few years. When a survey revealed that not all operating companies had addressed these issues with equal rigour, a programme was set up to establish more consistent standards of business ethics and to formulate a code of business conduct which would be implemented worldwide. One of the principal aims was to explain to employees more clearly what is expected of them in a given situation.

Principles

In no circumstances will corruption and fraud be tolerated by Heineken, which considers that corruption must be eliminated from society and has programmes in place to prevent it. In the case of gifts and conflicts of interest, however, it is not always possible to lay down hard and fast rules, one reason being that society's perception of the value and significance of a business gift varies widely from country to country. Heineken has formulated principles of ethical conduct at a central level which are implemented locally. These prevent employees allowing business and personal interests to conflict or accepting or making personal gifts which might impair ethical business relations or jeopardise decisions.

Results

Heineken's anti-corruption policy, which prohibits employees from committing any corrupt act on behalf of the company, was adopted worldwide in 2002. In addition to this central policy, many of Heineken's operating companies are developing activities to promote ethical conduct. 61 per cent of the employees of our operating companies are aware of their responsibilities regarding the giving and receiving of gifts and a slightly larger proportion, 75 per cent, are aware that purchases on behalf of the company must not be made from suppliers with which they have a personal relationship or from which they expect a personal reward. 81 per cent of the operating companies have introduced anti-fraud measures.


While the absence of a local policy does not, of course, imply that the operating companies in question perform poorly in terms of ethical conduct, it is necessary to reinforce the initiatives undertaken to promote ethical conduct in order to minimise the risks to the company.

Internal dialogue

Because it is important that the international code of conduct we have formulated is consistent with local standards and values, the business conduct programme largely takes the form of a local internal dialogue in which the operating companies define the rules

Heineken/BBAG integration

Heineken/Brau Union HR combines the best of both worlds

 <p>KURT HERLER</p>	<p>The integration of BBAG following its acquisition by Heineken was a massive task that demanded a new approach. The first step was to define a set of principles, to protect the interests of customers, employees and other stakeholders, before teams from the two companies met to draw up a plan for the integration process, based on respect for each other's culture. Thanks to this new approach, cultural differences have caused no problems so far.</p>
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on selected issues themselves within central frameworks imposed by Heineken N.V. Two trial projects were launched as part of this programme in 2003, one in Ghana and one in Réunion, which immediately highlighted the complexity of this subject and the cultural differences in the way in which terms are defined. They also revealed that clear assignment of responsibilities within the organisation and measurable results were critical factors in the successful implementation of a code of conduct.

New method

On the basis of the two trial projects, a new method has been developed which takes account of the operating companies' local circumstances in implementing the code. This new method will be tested in the course of 2004 and modified where needed, before being implemented worldwide. Heineken also plans to publish the code of business conduct internally and externally by the end of 2004. The programme for the introduction of the new code will then be finalised in 2005.

2.8 Customer and consumer relations

It is vitally important to Heineken that its trade customers (retailers) and end-users (consumers) are satisfied and continue to be satisfied with the products and services it provides. 74 per cent of our operating companies have policies and procedures in place to carry out periodic customer and consumer satisfaction surveys, the findings of which are used to improve the company's performance on a continuous basis.

The findings of regular brand perception surveys serve as input to the continuous process of refining our marketing strategy and developing new attributes.

Heineken does not yet have a global policy on safeguarding consumer privacy and we do not monitor infringements of privacy legislation. As a general rule, Heineken has access to little or no privacy-sensitive information on consumers apart from that obtained via brand competitions, consumer information lines or website visits. This information is not used actively and is never made available to third parties. Furthermore, our products are always traded via retailers. Heineken is currently working on formulating and implementing

a worldwide code to place protection of privacy on a more structured basis. This code will cover the privacy of employees, customers and consumers.

We provide the consumer with product information via our labelling. In some countries, including the EU member states, labelling is subject to statutory regulations. It is Heineken's policy to comply with these regulations and to take immediate steps to rectify any infringements. 89 per cent of our operating companies have product information and labelling policies and procedures in place.

Improper use of some of the packaging used for our products may cause personal injury, for example during transportation, storage and handling. It is Heineken's policy to comply fully with local statutory and other regulations concerning protection of the safety and health of users and to take immediate steps to rectify any infringements. A total of four infringements of statutory regulations were reported by our operating companies worldwide in 2003. 72 per cent of our operating companies have specific policies in place to protect users at all levels. In the on-trade sector, for example, this includes giving instruction in the use and care of beer dispensing equipment and technical requirements such as the installation of carbon dioxide sensors in beer cellars.

Heineken Italia switches emphasis to growth

Pepper Project focuses on individual performance



MASSIMO VON WUNSTER
PIERGIORGIO GIUNTI

Having integrated the major acquisitions it made in the late 1990s, Heineken Italia has switched its focus back to growth. For a company that is already market leader, this means maximising its management resources. The Pepper Project enables the company to measure individual performance, improve assessment procedures and define career potential, while the mentorship programme fosters the development of selected graduate trainees.