



Chemring Group PLC

Annual report and accounts 2008



Delivering global protection

CHEMRING

World leaders in defence

Chemring is a global group of companies that specializes in the manufacture of energetic material products and decoy countermeasures. We provide unique solutions for specific customer requirements in defence, security and safety markets.

Contents

Summary Financial Information	1
Financial Highlights	1
Statement by the Chairman	2
Review by the Chief Executive	6
Review by the Finance Director	14
Business Review	18
Corporate Responsibility Report	28
Directors and Professional Advisers	32
Directors' Report	34
Directors' Remuneration Report	38
Statement on Corporate Governance	47
Independent Auditors' Report to the Members of Chemring Group PLC	52
Consolidated Income Statement	53
Consolidated Statement of Recognised Income and Expense	54
Consolidated Balance Sheet	55
Consolidated Cash Flow Statement	56
Notes to the Consolidated Cash Flow Statement	57
Notes to the Group Financial Statements	58
Independent Auditors' Report on the Parent Company Financial Statements	90
Parent Company Balance Sheet	91
Parent Company Statement of Total Recognised Gains and Losses	92
Notes to the Parent Company Financial Statements	93

Summary Financial Information

Continuing operations	2008 £m	2007 £m	2006 £m	2005 £m
Revenue				
Energetics - continuing operations	177.1	128.2	69.3	30.2
- acquired	19.6	-	-	-
Energetics total	196.7	128.2	69.3	30.2
Countermeasures	157.5	126.5	118.4	90.8
Total revenue	354.2	254.7	187.7	121.0
Underlying operating profit*				
- continuing operations	79.6	61.2	38.5	22.9
- acquired	5.3	-	-	-
Total underlying operating profit*	84.9	61.2	38.5	22.9
Underlying profit before tax*	74.2	53.2	32.5	19.2
Operating profit	68.4	57.8	37.8	22.9
Profit before tax	57.7	49.8	31.8	19.2
Underlying basic earnings per ordinary share*	160p	112p	72p	47p
Basic earnings per ordinary share	123p	105p	70p	47p
Diluted earnings per ordinary share	123p	104p	70p	46p
Dividend per ordinary share	35p	25p	16p	10.5p
Net debt (£m)	116.7	99.6	70.6	52.9
Shareholders' funds (£m)	230.6	124.0	94.1	56.9

Financial Highlights



*Before goodwill adjustment arising from recognition of tax losses, intangible amortisation arising from business combinations and loss on fair value movements on derivatives of £16.5 million (2007: £3.4 million)

K C Scobie
CHAIRMAN



Statement by the Chairman

43% increase
in underlying
earnings per
share* to 160p

Once again I have the pleasure to announce another year of excellent performance, with a 39% increase in underlying profit before tax* to £74.2 million and a 43% increase in underlying earnings per share* to 160p.

The Board has given careful consideration to an appropriate dividend payment in the current economic environment but with the continuing strong growth in the Group's earnings, record cash flow and a solid balance sheet, the Board is recommending a final dividend of 25p. This gives a total for the year of 35p, an increase of 40% over last year.

Results	2008 £m	2007 £m	2006 £m	2005 £m
Total revenue	354.2	254.7	187.7	121.0
Underlying operating profit* - continuing operations - acquired	79.6 5.3	61.2 -	38.5 -	22.9 -
Underlying profit before tax*	74.2	53.2	32.5	19.2
Operating profit	68.4	57.8	37.8	22.9
Profit before tax	57.7	49.8	31.8	19.2
Underlying basic earnings per ordinary share*	160p	112p	72p	47p
Basic earnings per ordinary share	123p	105p	70p	47p



During the year, the Group acquired Richmond Electronics & Engineering Limited in the UK and completed three further acquisitions in the US – Scot, Inc., Martin Electronics, Inc. and Titan Dynamics Systems, Inc. The acquisition of Non-Intrusive Inspection Technology, Inc. (NIITEK) was completed in December 2008. These acquisitions were funded by £12 million in cash, utilising existing bank facilities, and the issue of £61 million equity. Each of the acquired businesses further strengthen the Group's presence in our target markets.

The Energetics division grew strongly, with revenue increasing by 54% to £196.7 million and underlying operating profit increasing by 64% to £45.7 million, now making it our largest division in revenue and profit terms. Countermeasures had a record year, driven by an exceptional performance from Chemring Countermeasures in the UK and strong revenue growth at Kilgore in the US.

A reconciliation of the underlying results to the statutory results is set out in the Review by the Finance Director on page 15.

Balance sheet, cash flow and debt

At this time of global economic and monetary stress, shareholders will inevitably be concerned to ensure that the Company's funding position is secure and adequate for both current and future plans. In recent years, the Board has focused on ensuring that the Group had a sound cash position and debt structure. This strategy has proved to be beneficial.

In November 2007 the Company completed a \$150 million private placement in the US of ten year fixed interest loan notes, with an interest rate of approximately 6.30%. In August 2008, although the Company had sufficient bank facilities to acquire Scot and Martin Electronics for cash, the Company issued new equity to raise £60 million. This helped to reduce the Group's gearing, which now stands at 51% (2007: 80%), and enabled the Group to maintain a good level of headroom on its established bank facilities.

With a record operating cash flow of £83.7 million in the year, the expectation that this trend will continue in 2009 and an easily managed debt repayment profile, the Board believes that the Group has more than adequate financial resources to meet its current expansion plans, including significant planned capital expenditure and continuing research and development investment.

Energetics

The Group is driving forward its programme of product and plant reorganisation within its production facilities in the UK, Germany, Italy, Norway, Spain, Australia and the US, whilst continuing to grow revenue and earnings to record levels. The expansion of our Energetics activities is enabling an increasing number of our product components to be sourced internally, particularly in those parts of the business where technology transfer restrictions across national borders are not as stringent as have historically applied in the countermeasures business.

Record operating
cash flow of
£83.7 million

Statement by the Chairman

CONTINUED

In NIITEK we believe we have acquired the world's foremost vehicle mounted mine detection system

Of particular significance during the year was the development of our training rounds business, where the combination of Chemring Defence (formerly Comet) in Germany and Titan Dynamics Systems in the US makes the Group the clear market leader in the area of battlefield simulation products. Titan's products, in particular, are in great demand in the US.

The Group has also expanded its capabilities in the supply of equipment for detecting and responding to improvised explosives devices (IEDs), unexploded ordnance clearance and demilitarisation of munitions. With Chemring EOD in the UK (comprising BDL Systems and Richmond) and with the recent addition of NIITEK in the US, the Group now has a significant presence in this sector. In NIITEK we believe we have acquired the world's foremost vehicle mounted mine detection system.

Countermeasures

Our UK business, Chemring Countermeasures, followed its record achievement in 2007 with another record year, delivering growth in revenue of 37%. Although the business continues to sell and export a wide range of decoys, its recent success emanates principally from the development of a spectral flare for the UK armed forces. This flare, which is in great demand, has a number of export variants which it is anticipated will generate excellent sales in the immediate future.

Kilgore, which is in a very strong position as the designated supplier of advanced flares for new aircraft such as the F-22 and the Joint Strike Fighter, also had a record year, with growth in revenue of 48%. However, the business was affected by delays in customer testing of certain products, which resulted in some revenue and margin being deferred into the first quarter of the current financial year. During the year Kilgore commissioned a new advanced flare production facility.

Alloy Surfaces, the most profitable business in the Countermeasures division, had another solid year of earnings and cash generation. However, we have had to recognise that its dramatic growth in recent years cannot continue indefinitely, and we anticipate more modest growth for the next few years pending the introduction of the next generation of special material decoys.

The strong relationship between our two US businesses and the US Department of Defense has developed further over the last year and culminated in the award of several five year IDIQ (Indefinite Delivery, Indefinite Quantity) contracts, with a total value of up to \$731 million. Whereas these may not necessarily translate into committed orders in that quantum over the next five year period, it does give a clear indication of the long term potential of our expendable countermeasures business.

During the year, our Australian business was awarded a ten year contract by the Australian Government, worth A\$160 million (£67 million), for the supply of a range of countermeasures and pyrotechnics. This is a great success and establishes us as the principal supplier of these products in the region. As part of the arrangement, we have committed to building a new, state-of-the-art decoy manufacturing facility near Melbourne, as well as creating a research and development centre for the design of future products.

Group strategy

Our Group strategy remains unchanged. We will continue to concentrate on our two segments of Energetics and Countermeasures, combining organic growth with acquisitions which fit our designated market sectors and product offering.

With the continuing development of the Group around the world, the Board has identified the need to strengthen the senior executive team with the appointment of a third divisional managing director. This individual will head up the Group's international business outside of the UK, Europe and the US; in particular, in Australia, India, Korea, Japan and the Middle East.

The Group already has customers in India, Korea and Japan but we believe that permanent production facilities in each of these countries will be required in the future in order to maintain and increase our presence in both Countermeasures and Energetics. We recognise that in these countries some form of joint venture is likely to be the required structure.

Health and safety

The Group has not only maintained its commitment to health and safety throughout the year but has recently strengthened it through the appointment of a new senior executive to concentrate full time on all aspects of this discipline. The new Group Director of Safety is now a member of the Executive Committee which runs the day to day activities of the Group. In a Group which works every day with sensitive, explosive materials, our attention to the protection of our employees cannot be emphasised enough.

Board of directors

The composition of the Board in terms of the number of members, their length of service and their skills is kept under continuing review. The Board does not consider that there is any need for immediate action.

Staff and employees

In recent years we have grown to over 3,000 employees across the world. Although this is still not a large number in terms of international businesses, it has been a rapid increase for the Group. In these difficult economic times, it is understandable that employees may be apprehensive over the security of their jobs. In this statement, I have attempted to set out my convictions for the future of the Group and its current sound financial position. The Board can set the scene and determine the "big picture" for the Group but it needs the commitment of all members of staff and employees to deliver that potential. If we do so, as we have done in the past, our employees can feel comfortable about their continuing employment prospects.

The Board extends its thanks to all employees, including those in recently acquired companies, for their efforts that have made 2008 another very successful year for the Group.

Pensions

Whilst the assets held by our defined benefit pension schemes have inevitably been impacted by the recent fall in stock markets, the deficit on the schemes is not significant in the context of the Group and we remain comfortable with the future funding requirements.

Dividends

The Board is recommending a final dividend of 25p per ordinary share, a 40% increase on the final dividend for 2007. This, together with the interim dividend of 10p paid in August 2008, gives a total dividend for the year of 35p, a 40% increase over 2007. The dividend is over 4.6 times covered on underlying profits after tax of the continuing operations. The shares will be marked "ex dividend" on 25 March 2009 and the dividend is payable on 17 April 2009 to shareholders on the register at the close of business on 27 March 2009.

Prospects

Our ongoing commitment to delivering total shareholder return has inevitably been restricted by the performance of the Company's shares, although I believe that shareholders will recognise that the external influences of the economic and financial dramas were outside of our control. In the circumstances, I believe our share price has held up relatively well compared to the stock market as a whole.

The Board has examined thoroughly not only the plans for the current year but also the next five years, and whilst recognising that we cannot remain completely immune to economic recession, we are convinced that our growth strategy, consistent with that articulated in previous years, is still soundly based. Furthermore, as mentioned earlier in this statement, we believe that the Group has adequate financial resources to deliver this strategy.

We enter 2009 with an excellent order book, an Energetics division growing rapidly but still in its youth, and several newly-acquired businesses determined to show the Group what they can achieve. The Countermeasures division will continue to produce solid earnings and cash flow.

As a leading defence business, the issues associated with the current military operations around the world make many judgments difficult but looking to the future of the Group, these international tensions do not make the world look a safer place. In rapidly changing economic circumstances there are many imponderables which could affect the outcome for the next year. However, once again I believe we will experience another year of above average growth, with all-round solid financial performance.



K C Scobie
CHAIRMAN
20 January 2009

I believe we
will experience
another year of
above average
growth

Dr D J Price
CHIEF EXECUTIVE



Review by the Chief Executive

Revenue
increased
by 39% to
£354.2 million

Group results

The Group performed strongly throughout the year and revenue from continuing operations increased by 39% to £354.2 million. Growth of 17% was achieved from our existing businesses, 14% from the full year trading of acquisitions made in 2007 and 8% from the four acquisitions completed in 2008. The Energetics division had another excellent year, achieving a 54% increase in revenue to a record level of £196.7 million, in spite of a disappointing performance from our US subsidiary, Technical Ordnance. The Countermeasures division increased its sales to a record level of £157.5 million, with very strong growth at both Kilgore and Chemring Countermeasures in the UK. The second half performance of the Group was particularly good, generating £204 million of revenue, £57 million of underlying operating profit* and £75 million of operating cash flow.

Underlying operating margins* for the Group remained steady at 24% for the full year, with the strong second half performance (28%) compensating, as expected, for the lower margins achieved in the first half. Operating margins in the Energetics Division improved to 23%, due to the introduction of automated manufacturing and the operational gearing achieved from higher volumes of activity. However, margins in our Countermeasures division reduced slightly to 29%, as the material cost of magnesium and higher sales of naval countermeasures affected the businesses. Consequently, underlying operating profit* rose by 39% to £84.9 million. We remain confident that this level of profitability is sustainable into the future.

The operating cash inflow during the year was excellent at £83.7 million, equivalent to a cash conversion rate of 99%. Our operating cash inflow in the second half of the year was particularly strong, with an equivalent cash conversion of over 130%. Capital expenditure increased by 113% to £34 million as the Group continued to invest significantly in improved automation, additional manufacturing facilities and important improvements in manufacturing safety. Research and development (R&D) also increased by 39% to £9.3 million, driven by a significant increase in customer funding. Company funded R&D grew at a more modest 7%. Our new five year research partnership with the Defence Academy at Shrivenham has started well with four doctoral research programmes and three major product studies.

At the year end, the Group had a record order book of £409 million, some 38% higher than the previous year. This level of order cover continues to underpin the prospects for 2009. I am pleased to report that the order book for the Energetics division at the year end was £281 million, 58% higher than the previous year, continuing to provide a real foundation for further strong growth in the future.

Since the year end, the order book has increased by a further 43% to a record current order book of £585 million.

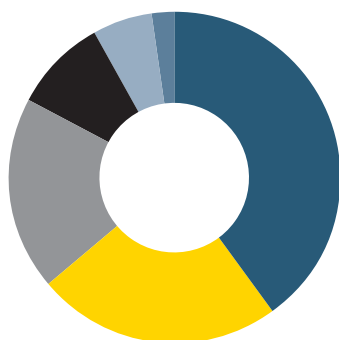
Health and safety

Following the detailed investigation into the incident that occurred in October 2007 in a manufacturing building at the Simmel Difesa site in Colleferro, Italy, a detailed restart process was implemented to ensure that appropriate lessons were learned and that risks were reduced to as low as reasonably practicable, in line with the Group's commitment to achieving the highest levels of safety in both its products and its manufacturing facilities.



The restart process was reviewed by independent experts and then implemented prior to commencing any operation, including all buildings and operations not involved in the incident. It included the use of a forty seven point checklist which ensured that all risks were adequately considered, mitigated and managed.

Simmel Difesa has now safely begun production in all areas, with the exception of the building in which the incident occurred, which was substantially damaged. Production was affected during the first four months of the year but the impact was minimised by ensuring that key production items were sub-contracted to alternative manufacturing facilities whilst the restart process was being implemented. These alternative manufacturing facilities were fully qualified by the customer and have performed well during the remainder of the year.



Revenue by destination (2008)

US	£142m	(40%)
UK	£86m	(24%)
Europe	£67m	(19%)
Middle East	£30m	(9%)
Far East	£23m	(6%)
Rest of world	£7m	(2%)

Energetics

- Orders: £249.2 million
- Revenue: £196.7 million
- Operating profit: £45.7 million
- Operating margin: 23%

Pyrotechnics and explosive ordnance disposal (EOD)

Our pyrotechnics and EOD business continues to grow strongly, with revenue up 45% year-on-year to £110.8 million. Our Italian subsidiary, Simmel Difesa, was a great success during its first full year of ownership, generating £25.8 million of pyrotechnic business. Demand for its pyrotechnic illumination mortar rounds continued to be strong, driven by continued high levels of operational use during peacekeeping operations by the UK Army. Over 60,000 rounds were delivered this year and the award of a multi-year contract for the supply of another 140,000 white-light and 50,000 black-light illumination rounds will maintain volume production throughout 2009 and 2010.

Chemring Defence also performed well, with encouraging growth in the sales of both pyrotechnic and demolition stores products. Production of smoke products, for signalling or screening, grew by 26% to record levels with over 800,000 units delivered to the UK Ministry of Defence and other NATO countries. Qualification of the L96/L97 vehicle discharge grenades for the US Army was completed to schedule and volume production continues in line with the multi-year requirements. Sales of demolition stores grew by 20% year-on-year, with a significant expansion of our customer base in Europe and the Middle East. In particular, our portable mine-breaching system, PEMBS, continued to be in demand, with new orders from Australia, Spain, Poland and Slovenia.

Revenue up 45% to £110.8 million for our pyrotechnics and EOD business

Review by the Chief Executive

CONTINUED

The US Army believes that realistic training conditions are a vital component of maintaining readiness

Battlefield training products have also continued to be in strong demand. The customer base for our MECS (multiple effects cartridge system) battlefield simulation ammunition continued to expand, with France and Saudi Arabia becoming important new customers. Record production levels were achieved for thunderflash products, with deliveries of in excess of 1 million units to European and Far Eastern customers. US Army usage continued to be strong and production reached 1.5 million units during the year. The US Army believes that realistic training conditions are a vital component of maintaining readiness, and plans to significantly expand the capabilities of its training ranges. Towards the end of the year, Chemring Defence received a \$5 million contract from Unitech in the US for the delivery of the new Improvised Explosive Devices (IED) simulator launchers for installation at various US Army training ranges. Further opportunities for the system and the associated MECS ammunition are expected to emerge over the next twelve months as a large number of countries involved in peacekeeping activities evaluate what type of training is needed prior to the deployment of troops.



Chemring Marine also grew strongly in 2008, expanding sales of its maritime distress signals by 16%, with a significant increase in deliveries to the US market to satisfy cruise liner requirements. Worldwide qualification of both its new Mk8 parachute distress rocket and its new day and night distress flare were achieved in the year and these new products should maintain our competitive position for the future.

Chemring Energetics saw lower production volumes of pyrotechnics during the year, principally due to a one-off change by Martin Baker in their manufacturing inventory policy that led to a short-term stop in demand for pyromechanisms and rocket motors used during their ejector seat production. A greater emphasis has been placed on growing the munitions component and sub-system opportunities.

Our US subsidiary, Technical Ordnance, had a disappointing year, with sales of pyrotechnics substantially lower than the previous year. Multi-year contracts for the delivery of BBU-35, BBU-36 and CCU-45 impulse cartridges for the US Air Force and US Navy were completed during the year but there has been a significant delay in the follow-on competitive process. The consequent gap in production reduced annual volumes by 30% to 4.2 million units, which had a substantial impact on revenue. The new multi-year contracts are now under negotiation.

All of our new acquisitions performed strongly during 2008. Richmond Electronics was acquired at the start of the financial year and has made an encouraging start, with a record level of sales and the successful capture of major orders from the UK, Italy, Bangladesh and Kuwaiti governments. Titan Dynamics, in Texas, has also made great progress since its acquisition, with a further 400 BES (battlefield effects systems) launchers installed at US Army ranges to take the installed base to more than 1,500. The production of BES cartridges has also been increased to 65,000 per month using the automated manufacturing expertise at Technical Ordnance. Further increases to 100,000 per month are planned to occur in 2009.

Scot also performed well, delivering strong sales and operating margins during the latter part of 2008. It secured new contracts for the supply of BBU-63 impulse cartridges for use on the B-2 stealth bomber and a substantial contract from Lockheed Martin for the aft and forward thrusters used on the Atlas V heavy lift launch vehicle. The business also won some important contracts (canard actuator, separation nuts) on the Orion Crew Expeditionary Vehicle, which is the NASA successor to the Space Shuttle.



Munitions

Our munitions business also grew strongly, with revenue up 66% year-on-year to £85.9 million. The full year of trading from Simmel Difesa was an important component of this growth, generating £26 million of revenue. Naval ammunition continued to be the most important aspect of the business, with deliveries of 40mm ammunition to a number of Italian and Middle Eastern customers. Production of 76mm naval ammunition remained steady during the year with deliveries to several Far Eastern and South American countries. Simmel was also awarded its first contract from the French Navy for the qualification of a range of 76mm ammunition for the French Horizon and FREMM frigates.

Simmel had further success in its other niche markets. It delivered the first batch of 120mm tank ammunition to a NATO customer to schedule, and received a significant award for the supply of 125mm tank ammunition to a Middle East customer. A qualification programme for the dual-mode warhead of the ASTER air defence missile was also successfully completed during the year and volume production has now started.



The munitions part of Chemring Energetics grew strongly in 2008, with good progress made on the development of our rocket motor business. The qualification of the NLAW rocket motors was completed in the early part of the year and production increased to its steady-state requirement. A new rocket motor for an 84mm anti-tank weapon was developed in the year and the first batch delivered to the European customer. In addition, good progress continues to be made to extend our partnership with BAE Systems for the supply of detonators, primers and energetic components for a wide range of their ammunition products.



Chemring Energetics is also working with BAE Systems and other prime contractors on the development of new explosive materials, particularly those that are insensitive to fire or high velocity impacts. During the year, we received a substantial contract from Nexter for insensitive explosive material for use in the new French 155mm ammunition.

Technical Ordnance also expanded its component supply business with the principal US ammunition prime contractors, ATK and General Dynamics. Production of explosive detonators, pellets and tracers increased by 24% year-on-year and we continue to explore the opportunity for more sub-system contracts, such as complete fuzes.

The newly acquired Martin Electronics performed well during the last few months of the year, increasing production and capturing a number of important new orders. Production of the M228 training grenade fuze continued strongly at 300,000 units per month in its semi-automated facility. Full automation of the assembly, inspection and packaging was introduced during 2008 and has successfully completed all qualification testing. Contract options in excess of \$22 million were also awarded.

Martin Electronics also successfully manufactured 40mm illumination rounds for the two US system prime contractors. Two further pyrotechnic rounds passed their factory acceptance testing and will begin production shortly. \$17 million of new orders were also received, giving Martin a strong order book with which to start the new financial year.

Revenue
up 66% to
£85.9 million
for our
munitions
business

Review by the Chief Executive

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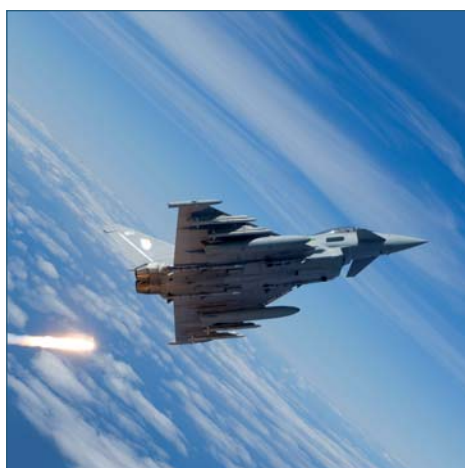
The Countermeasures division showed strong growth during the year, with revenue up 25%

Countermeasures

- Orders: £155.2 million
- Revenue: £157.5 million
- Operating profit: £45.5 million
- Operating margin: 29%

Our Countermeasures division showed strong growth during the year, with revenue up 25% year-on-year to £157.5 million. However, some of this growth can be attributed to the strength of the dollar during the last quarter and the growth on a constant exchange rate is much closer to 20%, broadly in line with the growth in the global market.

Chemring Countermeasures, our UK business, had another excellent year, generating £42.4 million of revenue, which was 37% higher than the previous year. This growth was driven by a record production of 240,000 spectral flares for use by the UK and coalition partners in peacekeeping operations to protect helicopters, transport aircraft and combat aircraft. Production of conventional flare types also continued at record levels, with growing interest being shown for our range of 26mm and 50mm flares for use on Russian made helicopters and aircraft. A substantial number of flares for Typhoon were delivered to the participating nations and good progress was made on the development of some advanced flares for future qualification on that platform.



Revenue from 130mm naval countermeasures grew by over 170% year-on-year with major deliveries to Denmark, Norway, Spain and Chile. Interest in both IR and chaff rounds continues to grow, particularly for countries looking to operate in crowded littoral operational theatres.

Historically, the operating margins from our naval countermeasures business have been considerably lower than that usually associated with our aircraft countermeasures. The strong growth in this area has, therefore, contributed to the small decrease in operating margins compared with 2007. However, company-funded programmes to develop alternative options to the existing bought-in rocket motors and electronics sub-systems are underway and should lead to higher margins over the next few years.

Kilgore also delivered a strong performance, with sales up 48% year-on-year to a record level of \$76.8 million. Production of the three high volume, conventional MTV flares ran extremely well throughout, with total production exceeding 1.6 million flares. This performance would have been even stronger but for the fact that production volumes had to be reduced during the latter part of the year, as a consequence of administrative delays in the award of follow-on options.

Three new flares were scheduled to enter production in 2008. A flare for C-17 transport aircraft successfully passed flight qualification and factory acceptance testing (FAT) during the year; full production started at the end of the year and will continue throughout the current financial year. A set of advanced flares for the B-52 also successfully passed its flight test and factory acceptance testing but the US Air Force customer requested that a new high altitude test be completed before volume production commenced. Since this flight test could only be scheduled at the very end of the financial year, the start of production was delayed into 2009. Similarly, problems with the technical data package on the advanced flare for the F-18 aircraft have taken a considerable length of time to resolve and production has been delayed until 2009.

Considerable progress has, however, been made on the advanced flares for the F-22 and F-35 aircraft. Production of the flare set for F-22 increased steadily to 700 units per month, although a problem with the US Government test facility delayed delivery of several batches of flares in the last six weeks of the year. The construction of the new advanced material facility at Kilgore, with its highly efficient fully automated production process, was completed and fully commissioned during the year. All F-22 production has now been transferred to this new facility. Successful validation testing of the flares for the Joint Strike Fighter (JSF) has been completed and the test results exceed expectations. The transition to low rate initial production is now expected to occur in 2009.

Another major success for Kilgore in 2008 was the capture of the multi-year award to supply the M212 flare, which is a component of the current flare suite used by the US Army and the US Air Force to protect helicopters from infra-red guided missiles. This contract, with a maximum value of \$382.9 million, is the largest framework contract ever placed with the Group by the US Government. The first delivery order was for just over 200,000 flares, production of which is expected to begin in the latter part of 2009.



Finally, Alloy Surfaces had another satisfactory year, generating \$128.5 million of revenue, which was similar to last year. Decoy production rose to a record level of over 1.7 million flares but a change of product mix affected total revenue. The US Army awarded Alloy a multi-year contract to supply the M211 flare, which is another component of the current flare suite used by the US Army for the protection of helicopters. This contract, with a maximum value of \$347.9 million, provides the framework for continued production of this product over the next five years. However, the US Air Force recently selected a modified design, called the MJU64, for its future airlift protection requirements and has placed an initial contract on Alloy for \$22.9 million. This change in requirement and the reduced demand from operations in Iraq, following the apparent success of the US and Iraqi forces "surge" initiative, resulted in a gradual decrease in the monthly production rate throughout 2008. Production of the MJU64 is now 10,000 units per month and is likely to stay at this rate for the foreseeable future.



In May 2008, the US Air Force awarded Alloy a \$30 million contract for the continued supply of MJU-50 decoys for protection of its transport aircraft. Production has been ramped up to 33,000 units per month and negotiations for a follow-on contract at higher rate production in 2009 have now started. The UK Ministry of Defence has placed additional contracts for the BOL/IR special material decoys and production has been increased to 40,000 units per month; this level of production should continue throughout 2009.

The Group received its largest ever framework contract from the US Government

Future prospects

Energetics - Pyrotechnics and explosive ordnance disposal (EOD)

The global market for pyrotechnics and EOD is estimated to be in excess of £3 billion per annum and to be growing steadily at over 10% per annum. In 2008, the Group had sales of £110.8 million, which represents a 3.5% market share. The market remains fragmented with a large number of small players, many of whom are nationally focused and with limited product ranges. Our recent acquisitions of Richmond, Titan, Scot and NIITEK have considerably enhanced our capabilities and market presence particularly in the US. We continue to believe that the opportunities for further growth are excellent.

There is growing interest in the use of white-light and black-light illumination payloads for use in peacekeeping operations and for training requirements. Demand for our 81mm mortar rounds remains high but many of our customers are looking for alternative delivery systems. We are adapting our payloads for 60mm and 120mm mortar rounds and expect demand for the product to grow strongly over the next few years.

Review by the Chief Executive

CONTINUED

Our opportunities within the US have been significantly enhanced by the acquisition of Martin Electronics

Signalling and screening smokes are used regularly during operational duties and training exercises, and there is growing interest in lower toxicity and multi-spectral performance. Demand for our products continues to grow within UK and NATO customers but we are starting to see growing export interest, particularly from Middle East and Far East customers. There are a number of large multi-year contracts that will be placed in 2009, which could significantly enhance our production volumes over the next few years.

Realistic battlefield simulation is considered essential for the preparation of troops prior to tours of active duty. The number of sophisticated training ranges continues to grow, particularly in the US, with our MECS and BES launchers as standard installations. Over the next five years, the installed launcher base will triple in number and this will lead to a substantial increase in the consumption of both MECS and BES pyrotechnic cartridges.

In October, we announced the acquisition of NIITEK, a leading developer of robot and vehicle-mounted mine and Improvised Explosive Device (IED) detection systems, incorporating its advanced Ground Penetrating Radar (GPR) and metal detection technologies. This acquisition, completed in December, is a critical step in the development of our EOD business and provides a platform to access the £500 million mine detection market. NIITEK has developed its sensor technology into an operationally proven, vehicle-mounted system and is in the process of delivering \$33.8 million worth of orders for thirty systems to the US Army in support of its counter-IED operations. Future developments of the technology include a robot-mounted sensor which will remove the human operator from hazardous mine detection activities in both peacekeeping operations and post-conflict reconstruction.



Energetics - Munitions

The global market for munitions remains comparatively stable at about £10 billion per annum and is not expected to change significantly over the next three years.

Simmel continues to maintain its position as world leader in naval ammunition and is looking to substantially expand its order book in South America and the Far East.

A major contract from the Italian MOD for medium calibre ammunition should be awarded shortly and there are a number of attractive export opportunities over the next eighteen months. Of particular note is the US 40mm ammunition programme for the C130 gunships, where Simmel is working in collaboration with General Dynamics.



Our opportunities within the US have been significantly enhanced by the acquisition of Martin Electronics. Full year trading from the automated production of the M228 training grenade fuze will give immediate growth and the competition for the next multi-year contract has now started. Full production of the three pyrotechnic 40mm variants will also take place in 2009, and there is growing interest in our medium velocity family for longer range, high accuracy engagements.

Collaboration between Martin Electronics and Simmel will also ensure that any technology transfer into US will be done as efficiently as possible.

Countermeasures

The market outlook for our expandable countermeasures business continues to be positive, although there are signs that the rate of market growth is starting to subside. Over the next three years, we believe that the global market will continue to expand at between 15% and 20% per annum, driven by strong demand from the US Air Force for advanced decoys to combat the latest air-to-air missile threats and the continued demand from NATO forces for the protection helicopters and transport aircraft during peacekeeping missions. Our successful track record in recent competitive procurements, such as the M212 contract, continues to give confidence that we can maintain our 50%+ market share position.

In Iraq, the enhanced security position has seen a gradual reduction in the operational consumption of decoys, particularly by the US Army. Moreover, the Iraqi government has now reached agreement with the US that all combat troops will be withdrawn by the end of 2011. However, the Iraqi government is starting to procure significant improvements in its military equipment, and has recently submitted requests to the US Government to acquire quite sizeable numbers of helicopters and combat aircraft.

In Afghanistan, the total number of US and NATO troops assigned to ISAF and Operation Enduring Freedom has increased to 79,000, and they continue to conduct extensive operations against the insurgents across the south of the country and on the border with Pakistan. The new US administration has indicated its intention to bolster the force with additional troops currently allocated to Iraq. The UK Ministry of Defence and other NATO nations also appear to be committing higher numbers of helicopters and aircraft to the mission, which will further increase demand for our products.

A number of important new aircraft will enter service over the next ten years. In Europe, the introduction of Typhoon will have a major impact on demand for decoys, particularly for our BOL/IR special material decoys and other advanced technologies to combat sophisticated surface-to-air or air-to-air threats. However, the biggest growth is expected to be in the US market, where procurement of advanced flares for new combat aircraft, namely the F-22 and the F-35, is planned.



Record order book of £585 million and prospects for 2009 continue to be excellent

F-22 decoy production will start full sustainment funding in 2010, when the full complement of aircraft and the need to establish a war reserve will significantly increase annual procurement quantities. Decoys for the F-35 start low rate production in 2009 and production volumes are expected to grow steadily over the next ten years as substantial numbers of aircraft enter service with the US, UK, Australia and other JSF partner nations.

The Australian Government has just awarded Chemring Australia a ten year contract, worth A\$160 million, for the supply of countermeasures and pyrotechnics. As part of the arrangement, we will invest A\$18 million in the build of a new state-of-the-art manufacturing facility near Melbourne and create a research and development centre for the design of future products. This new capability will allow Chemring Australia to bid for the second source supply for the F-35 decoys, and the additional production capacity will be used as part of the Group operations network to satisfy our global export flare requirements.

Overall, the future outlook remains encouraging and many opportunities exist for growth. The Group has a strong order book, which now stands at a record level of £585 million, up 46% since January 2008. This large order book, our healthy cash flow and strong balance sheet make the Board confident that the prospects for the Group in 2009 continue to be excellent.

Dr D J Price
CHIEF EXECUTIVE
20 January 2009

P A Rayner
FINANCE DIRECTOR



Review by the Finance Director

Total underlying operating profit* was £84.9 million, an increase of 39%

Results

Total revenue was £354.2 million (2007: £254.7 million), an increase of 39%. Total underlying operating profit* was £84.9 million (2007: £61.2 million), an increase of 39%.

Revenue, excluding acquisitions, increased 31% to £334.6 million (2007: £254.7 million). Underlying operating profit*, excluding acquisitions, increased 30% to £79.6 million (2007: £61.2 million). Net underlying operating margins*, excluding acquisitions, were 24% (2007: 24%).

Revenue from businesses acquired in the year was £19.6 million and £5.3 million of underlying operating profit* was generated at a margin of 27%.

An analysis of total revenue and underlying operating profit* by business segment is set out below.

The revenue of the Energetics division grew 54% and the operating profit grew 64%. The revenue of the Countermeasures division grew 25% and the operating profit grew 18%.

Interest income in the year was £1.8 million (2007: £0.6 million). The interest charge for the year was £12.6 million (2007: £8.7 million). Included within interest is £0.7 million (2007: £0.6 million) for retirement benefit obligations. Net interest was covered 7.9 times (2007: 7.6 times) by underlying operating profit*.

Underlying profit before tax* was £74.2 million (2007: £53.2 million), an increase of 39%.

Tax on the underlying profit before tax* was £20.7 million (2007: £17.1 million), representing a rate of 28% (2007: 32%).

Underlying profit after tax* on continuing operations was £53.5 million (2007: £36.1 million), an increase of 48%.

Segment	2008			2007		
	Revenue £m	Underlying operating profit* £m	Margin	Revenue £m	Underlying operating profit* £m	Margin
Energetics	196.7	45.7	23%	128.2	27.9	22%
Countermeasures	157.5	45.5	29%	126.5	38.6	30%
Share-based payments		(1.7)			(2.4)	
Unallocated head office costs		(4.6)			(2.9)	
Total	354.2	84.9	24%	254.7	61.2	24%

Reconciliation of statutory operating profit to underlying operating profit

Underlying profit is used by the Board to measure and monitor the underlying performance of the Group. Set out below is a reconciliation of statutory operating profit and underlying operating profit.

	2008 £m	2007 £m
Statutory operating profit	68.4	57.8
Add back:		
Goodwill adjustment arising from recognition of tax losses	1.8	-
Intangible amortisation arising from business combinations	6.0	3.4
Loss on fair value movements on derivatives	8.7	-
Underlying operating profit*	84.9	61.2

Profit before tax and underlying profit before tax also vary by the above amounts.

All references in this report are to underlying operating profit and underlying profit before tax.

Shareholder returns

Underlying basic earnings per ordinary share* from continuing operations were 160p (2007: 112p), an increase of 43%. Basic earnings per share from continuing operations were 123p (2007: 105p), an increase of 17%. Total basic earnings per ordinary share for continuing and discontinued operations were 123p (2007: 99p), an increase of 24%.

The total dividend per ordinary share of 35p (2007: 25p) is covered 4.6 times (2007: 4.2 times) by the underlying profit after tax* of the continuing operations.

Shareholders' funds at the year end were £230.6 million (2007: £124.0 million).

Pensions

The deficit on the Group's defined benefit pension schemes before associated tax credits, as defined by IAS19 *Accounting for pension costs*, was £13.6 million (2007: £13.3 million), a slight increase of 2%.

During the year, the April 2006 actuarial valuation for the UK Staff Pension Scheme was agreed with the scheme trustees, together with a funding plan to address the deficit on the scheme over the period to June 2014. The Group's ongoing contributions to the scheme were reduced under the funding plan. However, the Group agreed to provide a £6 million bank guarantee to the scheme, which can be called upon in certain events of default by the Company. In addition, £5 million has been placed in an escrow account, to provide additional security to the scheme in the event of a default.

The next triennial valuations of the UK Executive Pension Scheme and the Staff Pension Scheme will be carried out as at 6 April 2009.

The Executive Pension Scheme is closed to new entrants. The Staff Pension Scheme remains open for future accrual for current members but is only open to new employees at the discretion of the Board.

A new defined contribution pension scheme was introduced in the UK during the year. This scheme is now the main source of pension provision for the Group's UK employees. The majority of our overseas pension arrangements are defined contribution, save in those European countries where certain defined benefit retirement payments are required.

Research and development

Research and development expenditure totalled £9.3 million (2007: £6.7 million), an increase of 39%. An analysis of expenditure is set out below:

	2008 £m	2007 £m
Customer funded research and development	3.4	1.3
Internally funded research and development	3.3	4.1
Capitalised development costs	2.6	1.3
Total research and development expenditure	9.3	6.7

The Group's policy is to write-off capitalised development costs over a three year period. Amortisation of development costs was £0.8 million (2007: £0.6 million).

Acquisitions

During the year the Group acquired 100% of the issued share or stock capital of the following businesses:

	Date acquired	Consideration (including costs) £m
Richmond Electronics & Engineering Limited	2 Nov 07	12.5
Titan Dynamics Systems, Inc.	17 Mar 08	2.6
Scot, Inc.	2 Jul 08	20.8
Martin Electronics, Inc.	1 Aug 08	37.1
Total consideration		73.0

Review by the Finance Director

CONTINUED

A summary of the fair value of assets acquired and the goodwill arising on acquisitions is as follows:

	2008 £m
Intangible assets	37.6
Fixed assets	8.1
Cash	3.8
Working capital	6.2
Tax	(0.2)
Provisions	(5.2)
Fair value of assets acquired	50.3
Consideration (including costs)	73.0
Goodwill arising	22.7

Impact of acquisitions on revenue growth

During 2007 the Group acquired Simmel Difesa S.p.A. and the Chemring Nobel AS business. The businesses were owned for seven and five months respectively, and contributed £20.4 million to the Group's revenue in 2007.

The table below reconciles the Group's 2007 revenue on a proforma basis, assuming the above two businesses had been owned for a full year, and 2008 revenue.

	2008 £m
Actual revenue 2007	254.7
Additional revenue from acquired businesses if owned for a full year	17.7
Proforma 2007 revenue	272.4
Businesses acquired in 2008	19.6
Growth of businesses acquired in 2007	24.8
Organic growth	37.4
Actual revenue 2008	354.2

Cash flow

Operating cash flow was £83.7 million (2007: £60.6 million), which represents a conversion rate of underlying operating profit* to operating cash of 99% (2007: 99%). Working capital balances were well controlled in the year and were kept below increases in Group revenues.

Fixed asset expenditure across the Group was £34.2 million (2007: £16.0 million).

Cash flow from operating activities was £36.1 million (2007: £32.6 million), which represents a conversion rate of underlying operating profit* to cash flow of 43% (2007: 53%).

A summary of Group cash flow is set out below:

	2008 £m	2007 £m
Operating cash flow	83.7	60.6
Capital expenditure	(34.2)	(16.0)
Tax	(13.4)	(12.0)
Cash flow from operating activities	36.1	32.6
Interest	(8.2)	(7.4)
Dividends	(9.3)	(6.0)
Net cash inflow before acquisitions and disposals	18.6	19.2

Net debt, facilities and going concern

Net debt at the year end was £116.7 million (2007: £99.6 million), an increase of 17%.

Gearing at the year end was 51% (2007: 80%). A summary of debt is set out below:

	2008 £m
Cash	69.6
Term loans	(96.9)
US loan notes	(89.4)
	(116.7)

A summary of the Group's main committed bank facilities and repayment dates is set out below:

Facility type	Total facility £m	Repayment dates	Required repayments £m	Renewal dates
Working capital	50.0			2012
Term loans	96.9	2009 2010 2011 2012	19.7 21.2 34.9 21.1 <u>96.9</u>	
US loan notes	89.4	2017	89.4	

At the end of October 2008 the working capital facility was unutilised, due to the availability of net cash balances. Terms loans and the US loan notes were fully drawn.

On 14 November 2007, the Group completed a \$150 million private placement of ten year fixed interest loans in the US with a number of institutional investors. The loan notes, which mature in 2017, carry an interest rate of approximately 6.30%. The proceeds were used to repay existing US dollar debt and provide additional working capital facilities for the Group.

The directors have acknowledged the latest guidance on going concern. Whilst the current volatility in financial markets has created general uncertainty, the Group has significant working capital headroom, strong covenant compliance and a record order book. Accordingly, the directors have a reasonable expectation that adequate financial resources will continue to be available for the foreseeable future.

Share capital

A summary of the increases in the Company's ordinary share capital is set out below:

Date	Event	No. of shares	Amount raised before costs £m
2 Nov 07	Issue of vendor consideration shares on acquisition of Richmond Electronics & Engineering Limited	50,107	-
27 Jun 08	Placing of shares to fund acquisitions	1,111,112	25.0
1 Aug 08	Vendor placing of shares to fund acquisitions	1,555,555	35.0
	Exercise of share options in the year	127,798	0.5
		2,844,572	60.5

The amount raised includes £59.3 million of share premium. The costs of the share placings amounted to £2.0 million.

Foreign exchange

The results of overseas subsidiary undertakings are translated into sterling at weighted average exchange rates.

Currency denominated net assets are translated at year end rates.

Effective translation rates were as follows:

	2008	2007	% change
Average rates			
US dollar	1.87	1.99	6
Euro	1.26	1.44	12
Year end rates			
US dollar	1.63	2.08	22
Euro	1.27	1.44	12

Underlying profit before tax* was improved in 2008 by approximately £3.7 million, primarily as a result of US dollar and Euro appreciation against sterling.

Post balance sheet events

Acquisition of NIITEK (Non-Intrusive Inspection Technology, Inc.)

On 12 December 2008, the Group purchased the entire stock capital of NIITEK for an initial consideration of \$30 million. Further deferred contingent consideration of up to \$10 million is payable upon achievement of certain financial targets.

The initial consideration was funded from existing bank facilities.



P A Rayner
FINANCE DIRECTOR
20 January 2009

*Before goodwill adjustment arising from recognition of tax losses, intangible amortisation arising from business combinations and loss on fair value movements on derivatives of £16.5 million (2007: £3.4 million)

This Business Review, together with the Statement by the Chairman, the Review by the Chief Executive and the Review by the Finance Director set out on pages 2 to 17, and the Corporate Responsibility Report set out on pages 28 to 31, provides a fair review of the Group's business development, performance and position at the end of the financial year; its strategy and likely future developments; key performance indicators; and a description of the principal risks and uncertainties facing the business.

Business Review

Chemring Group PLC is an international leader in energetic materials, components and systems, and expendable countermeasures, with manufacturing operations in the UK, the US, Europe and Australia.

United States of America

Alloy Surfaces Company, Inc., Pennsylvania
Kilgore Flares Company LLC, Tennessee
Martin Electronics, Inc., Florida
Non-Intrusive Inspection Technology, Inc., Virginia
Scot, Inc., Illinois
Technical Ordnance, Inc., South Dakota
Titan Dynamics Systems, Inc., Texas



Revenue by destination (2008)

US	£142m	(40%)
UK	£86m	(24%)
Europe	£67m	(19%)
Middle East	£30m	(9%)
Far East	£23m	(6%)
Rest of world	£7m	(2%)

Europe

Chemring Countermeasures Ltd, United Kingdom
Chemring Defence Germany GmbH, Germany
Pirotecnia Oroquieta S.L., Spain
Chemring Defence UK Ltd, United Kingdom
Chemring Energetics UK Ltd, United Kingdom
Chemring EOD Ltd, United Kingdom
Chemring Marine Ltd, United Kingdom
Chemring Nobel AS, Norway
Simmel Difesa S.p.A, Italy

**Australia**

Chemring Australia Pty Ltd

Business Review

CONTINUED

Energetics: The Group is a centre of excellence for the design, development and production of energetic materials, sub-systems and systems for military, OEM and safety customers. Our energetics products can be categorised as follows:

Collaboration between Chemring Defence in the UK and Martin Electronics resulted in *Mercury*, 40mm medium velocity ammunition that has created a new market by increasing the effective range of under-slung rifle grenade launchers

Pyrotechnics and explosive ordnance disposal (EOD)

Military pyrotechnics

- Smoke and flares
- Distraction and screening grenades
- Markers
- Smoke payloads
- Battlefield simulation products
- Impulse cartridges

Demolition stores

- RF and hard-wired electrical initiators
- Percussion initiators
- Detonators and charges
- Minefield clearance systems
- Recoilless de-armers/disrupters
- ROV weapon carriers

Marine pyrotechnics

- Smokes and flares
- Rockets
- Line throwers

Aircrew egress

- Rocket propellant
- Canopy cutting charges
- Linear explosives
- Cartridge actuated devices

Munitions

Energetic sub-systems

- Propellants and rocket motors
- Fuze and safe/arm units
- Flight termination systems
- Pyro-mechanisms and actuators
- Warheads and charges
- Primers

Ammunition and components

- Medium and large calibre ammunition
- Fuzes
- Propellants
- Manufacture of base high explosives
- Insensitive HE material



Our businesses

Chemring Australia

Chemring Australia Pty Ltd is based in Victoria, Australia, and supplies a range of pyrotechnics, countermeasures, military training and marine safety products.

Chemring Defence

Chemring Defence comprises of three companies: Chemring Defence UK Ltd, based in Derby, UK; Chemring Defence Germany GmbH, based in Bremerhaven, Germany and Pirotécnia Oroquieta S.L., based in Pamplona, Spain. Chemring Defence is a centre-of-excellence for the design, development and production of defence material and sub-systems for military, OEM and safety customers.

Chemring Energetics UK

Chemring Energetics UK Ltd is based on the Ardeer Peninsula in Scotland and in Corsham, UK and specialises in the design and manufacture of energetic materials, rocket motors, actuated devices and demolition stores.

Chemring EOD

Chemring EOD Ltd (formerly BDL Systems Ltd and Richmond EEI Ltd) is based in Dorset and Norfolk and manufactures a range of products for detection, assessment and neutralisation of explosive threats for improved explosive device defeat (IEDD) and unexploded ordnance (UXO) clearance.

Chemring Marine

Chemring Marine Ltd is based in Fareham, UK and is the world's leading supplier of marine distress signals to the commercial and leisure markets, under the brand names of Pains Wessex and Comet.

Chemring Nobel

Chemring Nobel AS High Energy Materials is based in Saetre, Norway, and manufactures and supplies RDX and HMX, and other niche energetic materials for explosives and propellant applications.

Kilgore Flares

Kilgore Flares Company LLC is based in Toone, Tennessee, USA, and manufactures pyrotechnic and ammunition products, as well as expendable decoys for air and sea platforms.

Martin Electronics

Martin Electronics, Inc. based in Perry, Florida, USA, is a specialist manufacturer of ammunition, fuzes, signalling and other pyrotechnically activated devices for use in the defence sector.

NIITEK

Non-Intrusive Inspection Technology, Inc. based in Virginia, USA, is a leading developer of robot and vehicle-mounted mine detection systems incorporating its advanced Ground Penetrating Radar (GPR) and metal detection technologies.

Simmel Difesa

Simmel Difesa S.p.A. is based in Colleferro, Italy and is a leading supplier of medium calibre ammunition and components including fuzes, safety and arming devices, warheads and modular charges.

Technical Ordnance

Technical Ordnance, Inc. is based in South Dakota, USA, and manufactures initiators, impulse cartridges, safety and arming components, and cutting charges.

Scot

Scot, Inc. is based in Downers Grove, Illinois, USA, and is a leading manufacturer of cartridge-actuated and propellant-actuated devices (CAD/PADs) used in aircraft emergency systems, aircrew egress and space launcher separation. Scot's products include actuators, valves and sequencers, separation nuts and bolts, and aircraft weapon ejector systems.

Titan Dynamics Systems

Titan Dynamics Systems, Inc. is based in Marshall, Texas, USA, and is a leading manufacturer of battlefield effects simulators ("BES"). Titan's proprietary launchers and cartridges provide realistic simulation for "force on target" training. It has a range of new products to meet the evolving requirements from current deployments including improvised explosive device ("IED") effects simulators, and a missile launch simulator which replicates the characteristics of shoulder-launched weapons against land or air targets.

Business Review

CONTINUED

Countermeasures: The Group is the world's leading producer of expendable decoy countermeasures for protecting air, sea and land platforms against guided missile threats. Our countermeasures products can be categorised as follows:

Our portfolio is constantly developing to meet counter-solutions for emerging threat technologies, reflecting our commitment to meet new needs and situations

Air countermeasures

- Conventional MTV flares
- Advanced decoys
- Special material decoys
- Chaff

Naval countermeasures

- RF decoys
- IR decoys

Our businesses

Alloy Surfaces

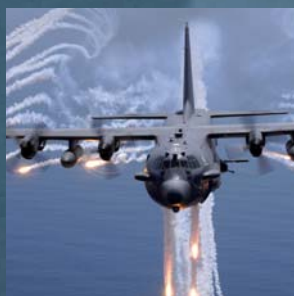
Alloy Surfaces Company, Inc. is based in Philadelphia, USA, and manufactures special material decoys (SMD) for protecting aircraft against IR missile threats.

Chemring Countermeasures

Chemring Countermeasures Ltd is based in Salisbury, UK and manufactures IR and RF decoys for air, sea and land platforms.

Kilgore Flares

Kilgore Flares Company LLC is based in Toone, Tennessee, USA, and manufactures expendable decoys for air and sea platforms, as well as a range of pyrotechnic and ammunition products.



Strategy

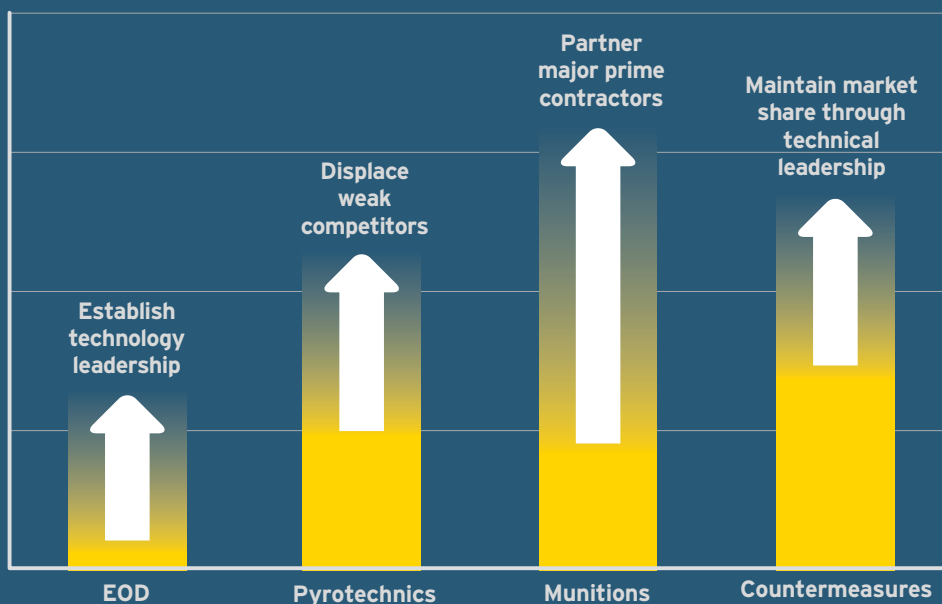
Group strategy

The Group strategy remains focused on our two core sectors of operations - Energetics and Countermeasures.

Our core strategy over the next five years looks for the development of excellence within our key three core competencies:

- **Energetic materials** - we will focus the business on products where we can exploit our extensive expertise in explosive, pyrotechnic and pyrophoric materials. We will address niche, highly profitable markets with significant, value-added manufacture and assembly where barriers to entry are strong.
- **High reliability and safety** - our products require the highest levels of safety in manufacture and use. Manufacturing and product safety must be one of our highest priorities.
- **High volume manufacturing** - we currently manufacture many of our products in significant quantities and have built up strong expertise in automated manufacturing. Our strategy is to consolidate manufacturing centres, where possible, to give high volumes. Expertise in automation and flexible manufacture will drive down our cost base and maintain competitive advantage.

Our vision is to be the leading producer of energetic material products and countermeasures for the global defence market



Business Review

CONTINUED

Energetics strategy

Pyrotechnics and explosive ordnance disposal (EOD)

Our strategy is to become the world leader in pyrotechnics, through focused investment in new products that displace existing incumbents and better meet our customers' requirements. We also intend to consolidate the market through carefully selected acquisitions in both Europe and the US.

We aim to become the world leader in demolition stores, and significantly expand our expertise in EOD. We will become a major European competitor in the demilitarisation of unwanted ammunition and munitions, and we will develop a world-leading position in counter-mine and counter-IED technologies.

Munitions

Our strategy is to develop a position as the preferred supplier of energetic materials to the key prime contractors for ammunition and missiles in Europe and the US. This will be achieved through investment in new products, by targeted competition against existing sole-source suppliers, and by further complementary acquisitions. We will maintain our position as the world market leader in naval ammunition, and we will develop our focus as a prime contractor in certain special niche markets that are complementary to those of our principal customers.

Countermeasures strategy

The core strategy for the Countermeasures business is to maintain our share of the expendable countermeasures market and expand the business in line with the size of that market, which is expected to grow steadily over the next five years. We will increase our investment in new products and technologies, and will build on our current leadership in special material, spectral and thrusted flare technologies. We will continue to invest in new fully automated production facilities that will improve operator safety, significantly enhance our operational efficiency, and maintain our lead role in the development of new products for the next generation of fixed wing and rotary aircraft.

Geographic strategy

Our geographic strategy has five components:

- We will maintain our US operations as 50% of the Group.
- We intend to manufacture in the US for the US market and in Europe for the European market.
- We will use our excellent worldwide sales network to export both the Group's and third parties' products to global markets from both Europe and the US.
- We will establish local manufacturing facilities in countries where we need to do so in order to access certain key national markets.
- We will increase our regional marketing presence in the Far East and the Middle East.

Strengths and resources

The Group has core competencies in the design and manufacture of energetic materials; the development of highly reliable and safe products; and high volume manufacturing.

Market position and reputation

The Group is the world's leading manufacturer of countermeasure decoys, with over 50% market share. The special material decoys manufactured by our US countermeasures business are unique to the Group, and we are currently leading the field in the development and manufacture of other advanced technology products, such as spectral and kinematic decoys.

In our growing Energetics division, we are building on the Group's reputation as an expert manufacturer of products containing energetic materials, and we are developing a prominent position in several niche market areas, including pyrotechnics for screening, signalling and illumination, battlefield effects simulators, key components of aircrew egress systems, explosive ordnance disposal equipment, advanced fuzing and naval ammunition.

Customer relationships

The Group has an extensive customer base, comprising governments, armed forces, prime contractors and OEMs across the globe. The US Department of Defense is our largest single customer. We have an extensive distribution network and, with worldwide market access, our businesses currently supply to over eighty countries.

Manufacturing operations

The Group continues to benefit from significant efficiency improvements achieved through enhanced automation and rationalisation of manufacturing capabilities across the Group, and we have an ongoing investment plan for new plants and technologies. Our operational structure is now geared to leverage strongly from future sales growth.

Solid financial base

The Group enjoys healthy operating margins across its businesses. Our focus on working capital management in recent years has manifested itself in excellent cash conversion and produced a sound balance sheet for the Group.

Management

Management resource and expertise have been strengthened at all levels across the Group during the last three years, and we continue to develop our operational skills to ensure that we remain a world class manufacturer. We have an experienced team working on business development and acquisitions, and we are focusing heavily on our post-acquisition plans to ensure that new acquisitions are effectively integrated within the Group and we achieve maximum value from our growth strategy.

Operating performance

Continuing operations	2008 £m	2007 £m
Revenue		
Energetics - continuing operations	177.1	128.2
- acquired	19.6	-
Energetics total	196.7	128.2
Countermeasures	157.5	126.5
Total revenue	354.2	254.7
Underlying operating profit*		
- continuing operations	79.6	61.2
- acquired	5.3	-
Total underlying operating profit*	84.9	61.2
Underlying profit before tax*	74.2	53.2
Operating profit	68.4	57.8
Profit before tax	57.7	49.8
Underlying basic earnings per ordinary share*	160p	112p
Basic earnings per ordinary share	123p	105p

*Before goodwill adjustment arising from recognition of tax losses, intangible amortisation arising from business combinations and loss on fair value movements on derivatives of £16.5 million (2007: £3.4 million)

Key performance indicators

The Group's strategy is underpinned by focusing on a number of key financial performance indicators. The key indicators that the Board utilises to assess Group financial performance are set out below. Similar indicators are used to review performance in the two divisions. Details of non-financial performance indicators are set out in the Corporate Responsibility Report.

The Board considers that the measurement of underlying and divisional operating profit provides additional useful information to users.

Orders received and order book

Continuing operations	Orders received		Order book	
	2008 £m	2007 £m	2008 £m	2007 £m
Energetics	249.2	172.0	281.0	177.8
Countermeasures	155.2	123.0	128.0	119.5
Total	404.4	295.0	409.0	297.3

The closing order book at the year end of £409 million represents a 38% increase on the previous year end. This reflects the significant increase in demand for the Group's products during the year, and provides a solid base for performance in the current financial year.

Business Review

CONTINUED

Operating profit**

Continuing operations	2008 £m	2007 £m
Energetics	45.7	27.9
Countermeasures	45.5	38.6
Total	91.2	66.5

** Operating profits of the divisions are stated before charges for share-based payments, unallocated head office costs and goodwill adjustment arising from recognition of tax losses, intangible amortisation arising from business combinations and loss on fair value movements on derivatives of £22.8 million (2007: £8.7 million)

The operating profit on continuing operations increased by 37% during the year, reflecting the strong operating performance of both divisions.

Return on sales

Continuing operations	2008 %	2007 %
Energetics	23	22
Countermeasures	29	30
Total	26	26

The return on sales percentage as a whole is consistent with the prior year.

Interest cover

	2008	2007
Total	7.9 times	7.6 times

Net finance expense was covered 7.9 times by underlying operating profit* at the year end. The Board aims to keep interest cover at a prudent level.

Operating cash flow

	2008 £m	2007 £m
Total	83.7	60.6

Group operating cash flow increased by 38% to £83.7 million during the year. This represents a conversion rate of underlying operating profit* to operating cash of 99%.

Contractual arrangements

As referred to above, the Group contracts with a wide range of customers, comprising governments, armed forces, prime contractors and OEMs across the globe. The US Department of Defense is the largest single customer, and procures the Group's products under a significant number of separate contracts placed with individual Group businesses.

The Group's businesses utilise many suppliers across the world, and arrangements are in place to ensure that businesses are not totally reliant on single suppliers for key raw materials or components.

Principal risks and uncertainties

As described on page 50 and 51, the Board is responsible for the Group's systems of internal control and its risk management systems. The Board has constituted a Risk Management Committee, which meets quarterly, to review the key risks associated with the achievement of the annual budget and the five year plan for each business; the top five health and safety risks identified at each site; and the risk control procedures implemented. The Committee reports biannually to the Audit Committee and the Board and, through this process, the Board has identified the following principal risks currently facing the Group. The Group mitigates its risk exposure through an insurance programme that covers property and liability risks, where it is appropriate and cost effective to do so.

Health and safety risks

The nature of the Group's operations, involving energetic materials, is such that the Board considers health and safety to be a key area of focus in managing risk. Accordingly, health and safety is included on the agenda at every Board meeting and is also discussed at the monthly Group Executive Committee meeting. The Board believes that responsibility for the delivery of world class safety standards is an integral part of the operational management accountability, and managers are therefore expected to embrace a positive safety culture and to demonstrate leadership and commitment in the workplace. All employees are encouraged to report potential hazards, and to raise any health and safety concerns through the appropriate channels.

Our stated aim is to achieve zero injuries and to reduce health and safety risks, where they cannot be eliminated altogether, to a level which is "as low as reasonably practicable". All businesses are expected to proactively manage their own risks but in addition, the top five site risks at each business and their associated mitigation programmes are reviewed on a monthly basis by the Group Executive Committee and quarterly by the Risk Management Committee. Technology and automation roadmaps support the Group's strategy for risk reduction through increased automation and remote operations included within its five year plan.

Further details on the Group's approach to health and safety are set out in the Corporate Responsibility Report.

Management resource

The Group requires competent management if it is to achieve its growth expectations, successfully integrate its acquired businesses and meet its aggressive order capture targets. Accordingly, the Group Executive Committee reviews the strengths and weaknesses of the management team at each business twice a year. We continue to strengthen the management organisation across the Group, and a number of new senior appointments have been made during the year. We have undertaken a detailed review of our future sales and marketing resource requirements, and a recruitment drive is now under way in this area. A similar review of engineering resource is in progress.

A bespoke management development programme for our senior management will be delivered in 2009 by Henley Management College, with the intent that this will be rolled out to the next tier of management during 2010.

Competitors

Defence is a global industry, which is constantly challenged to counter ever-changing threats. The Group's strategy is to focus on targeted niches in energetic materials and systems,

where the nature of the products and the requisite production and qualification processes provide significant barriers to new entrants. However, as threats evolve, new businesses offering new solutions may enter the market.

The nature of the threat from missiles and other weapons is continually changing, particularly as new platforms are introduced in different countries, and countermeasures solutions need to develop on an ongoing basis to meet the enhanced requirements. The number of countermeasures manufacturers is currently small but as technologies change, existing manufacturers compete for new products and new businesses can enter into the market. The Group is currently the world leader in the supply and manufacture of expendable countermeasures, with a number of proprietary products, and we intend to maintain this position through our continued investment in research and development, and world class manufacturing facilities.

Timing of orders

The Group has a very strong order book but in general, the majority of the Group's contracts are of a relatively short duration and, with the exception of framework contracts with key customers, do not usually cover multi-year requirements. This means that an unmitigated delay in the receipt of key orders could affect the Group's earnings, and achievement of its growth targets, in a given financial year. Maximising order intake is therefore a key priority for the Group. We are addressing this through the strengthening of our sales and marketing resources. The development of world class manufacturing facilities, with the ability to transfer manufacture across sites, also provides us with the flexibility to change our manufacturing schedules if anticipated orders are delayed and need to be replaced at short notice, and to satisfy our customers' surge requirements.

Introduction of new products

The Group's approach to innovation and continued research and development activity ensure that we are continually adding new products to the range. During the year, our position was further strengthened in this area by the demand for our countermeasures on a range of new platforms.

In order to satisfy these requirements, we need to ensure that new product development is completed in a timely manner to a standard which allows us to undertake volume manufacturing, and to produce products against high reliability and safety criteria to meet our customers' requirements. New manufacturing facilities have been established in the year to accommodate the production of these new products, and in other areas, there has been a requirement to significantly increase capacity on our existing production lines. This necessitates careful management of contractors - where construction work is being undertaken, suppliers - where new components have to be qualified for use in our products, and employees - where training in new skills is required. We continue to introduce Six Sigma techniques as appropriate within the organisation to improve our manufacturing capabilities. This investment in new facilities is ongoing.

Introduction of new manufacturing facilities

Over the next two years, we will be investing significant capital expenditure in the establishment of new countermeasures manufacturing facilities in the UK and Australia. We need to ensure that these facilities are completed within budget and on time, in order to maximise our manufacturing capacity for our future growth expectations. We have appointed a senior Project Director to oversee the design and construction activities, and progress is being monitored by the Group Executive Committee.

Technology transfers

The formation by the Group of centres-of-excellence for the production of energetic materials has generated considerable interest from major prime contractors in both the US and Europe, who are looking for strategic partners. Progressing the development of these relationships and securing the transfer of technologies from these large prime contractors is a key objective for the Group over the next five years. Accordingly, the Group has been recruiting new personnel to manage these activities, and reviewing manufacturing capabilities and investing capital where necessary, to ensure that we mitigate the risk associated with the technology transfers and maximise the opportunities that are presented.

Management of prime contracts

The Energetics division now has substantial prime contracts with a number of countries, and is planning to secure more. The contracts provide for the supply of an extensive range of our own and third party products over the next three years, and require a particular type of programme management expertise. Dedicated programme managers have been appointed, with a reporting chain through to the Group Executive Committee, which undertakes a regular high level review of programme status and supply chain issues. During the year we appointed additional personnel with specialist knowledge of the management of offset requirements and complex export compliance issues for this growing area of business.

Political risks

It is recognised that the nature of the current military operations around the world may change over the next three to five years. Our energetics activities are less dependent on these military activities, particularly as our product portfolio continues to grow in areas such as training and explosive ordnance disposal (EOD).

We do not believe that the Group's countermeasures business will be significantly impacted by a change in current military operations, as our products will still be required to provide defensive protection during the continuing peacekeeping activities. Growth in the countermeasures business will be delivered as our proprietary products are fitted to a range of new platforms in the US and Europe.

The US Department of Defense is the Group's largest customer. At the present time, we do not foresee any significant change to the level of future demand for the Group's products in the US following the recent change in administration.

Compliance and corruption risks

The Group has committed to adherence to the European Aerospace and Defence Association's Common Industry Standards on Anti-Corruption, and is currently reviewing all of its business processes in order to achieve full compliance.

Economic risks

Fortunately, the Group has not been greatly affected by the difficult economic conditions prevailing in many countries around the world and the Board continues to believe that the future prospects for the Group are very good. However, we will continue to closely monitor our potential exposure to further economic changes.

Financial risks

Details of the financial risks to which the Group is potentially exposed are set out in Note 24 of the financial statements.

Corporate Responsibility Report

Corporate responsibility management and accountability

The Board fully acknowledges its obligation to ensure the responsible operation of the Group's businesses at all times with due regard to the interests of shareholders, employees, customers, suppliers and the wider community. The Board has overall responsibility for establishing and maintaining the Group's policies in this area, and the Chief Executive is accountable to the Board for ensuring that the Group's businesses adhere to these policies.

Business conduct

The Group has adopted a Code of Business Principles, which requires our employees, our businesses and all third parties who act on our behalf to comply with our standards of acceptable business conduct and applicable laws and regulations in all of the countries in which we operate. The managing directors of each business are required to report to the Chief Executive on compliance with the Code of Business Principles on an annual basis.

Ethics and anti-corruption

The Group has committed to adherence with the European Aerospace and Defence Association's Common Industry Standards on Anti-Corruption, and we are currently reviewing all of our business processes across the Group in order to ensure that we achieve full compliance. This involves entering into new arrangements, compliant with the Common Industry Standards, with all of our agents and other third parties who act on behalf of the Group. Our Code of Business Principles has also been updated to incorporate the Common Industry Standards.

Our US businesses have adopted an ethical compliance programme to satisfy US Government requirements for ethical training for employees, compliance audits, an employees' "hotline", and related investigation procedures. We are currently running a similar ethics and anti-corruption training programme for the management of our businesses outside of the US.

The Group has a whistleblowing policy and procedures in place which enable all employees to raise concerns, in confidence, about possible improprieties. These arrangements now reflect the requirements of the Common Industry Standards.

Policy on the sale of goods and services

The Group's strategy is to become the world leader in the manufacture energetic material products and countermeasures for the global defence market, and we are presently delivering significant growth in this area through a combination of organic development and acquisitions. The scope of the Group's activities has significantly widened over the last few years, particularly with regards to the supply of components and sub-systems for various types of munitions, and there is increasing demand for the supply to our customers of third party products. Consequently, the Board has adopted a Policy on the Sale of Goods and Services, which provides guidance to all stakeholders on the products and services that the Group will supply and to which customers, and sets out a clear definition of what we will not supply.

Health and safety

The Board recognises that the highest levels of safety are required in order to protect our employees, whilst achieving growth and maintaining leadership in the Group's chosen markets. The Board believes that all injuries are preventable, and management systems and a long term strategy have been adopted to ensure that we continually improve our performance and reduce risk within the constraints of what is reasonably achievable.

The Chief Executive has overall responsibility for health, safety and environmental matters across the Group. A new Director of Safety was appointed during the year, who reports directly to the Chief Executive, and is responsible for the effective administration and implementation of the Group's health, safety and environmental strategy. Strategic direction is considered by the Group's Risk Management Committee, and the Director of Safety reports to the Executive Committee on the performance of the businesses against agreed objectives. The Chief Executive reports monthly to the Board on all key health and safety issues.

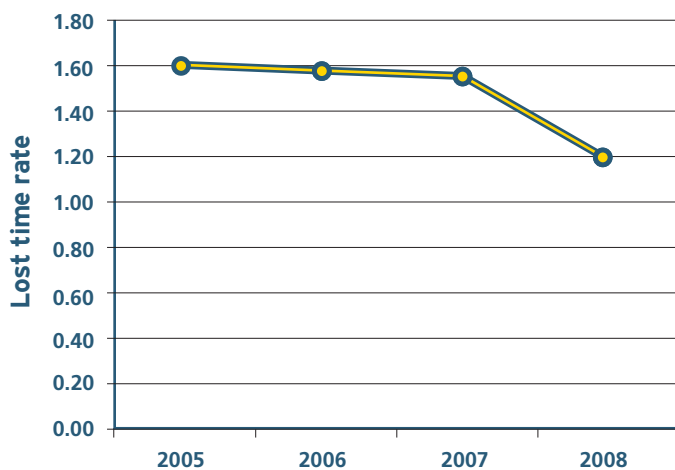
The Board requires that all businesses systematically manage their health, safety and environment hazards, set objectives, monitor progress by regular measurement, audit and review, and take additional action where necessary. Each Managing Director is responsible for the management of health, safety and environmental issues within their business and for providing adequate resources to satisfy the Board's requirements. Managers are required to enforce procedures, and to provide leadership and commitment to promote and embrace a positive health and safety culture. We emphasise the importance of individual responsibility for health and safety at all levels of the organisation. We expect employees to report potential hazards, to be involved in implementing solutions, and to adhere to rules and procedures.

We recognise that a key element in the continual improvement of health, safety, and environmental management is sharing best practice and lessons learnt from incidents across all of the Group companies. A common incident reporting and investigation procedure is in place, as well as an alert system that formally ensures key findings from incidents are quickly communicated to all operational sites and actions taken as appropriate. All accidents and near misses are investigated. An annual Group health, safety and environment conference is attended by representatives from all businesses, and a Health, Safety and Environment Technical Committee supports continual improvement through the development and promotion of good practice across the Group and provision of training and support.

We continue our successful implementation of formal management systems across the business and now have seven sites validated as compliant with the health and safety management system OHSAS18001. We require all newly-acquired businesses to achieve certification within two years of joining the Group and, with the exception of these businesses, we expect all other Group companies to have achieved certification by the end of 2009.

Whilst we are pleased to report that there were no serious safety incidents in the year, our safety programmes have been heavily influenced by the incident which occurred at Simmel Difesa in October 2007, which led to the death of one of our employees. Following the incident, a formal structured investigation and root cause analysis was undertaken using an established process. This generated a series of actions which were disseminated across the Group. We are determined to do all we can to minimise the likelihood of similar incidents in the future.

Following three years of static lost time performance, added focus on the management of health and safety resulted in a real improvement in performance during the year, with our lost time incident rate (calculated using the US OSHA rules) reducing from 1.56 to 1.20 incidents per 100 employees, as set out below:



This performance improvement has been achieved by implementation of several structured and formal processes including:

- cultural development
- product safety management
- introduction of formal "safety case" processes
- enhanced training
- manufacturing process refinement
- extended audit programmes; and
- product safety reviews.

Six of our sites reported no lost work days in the year, which is an excellent achievement.

A focus on "near misses" during the year resulted in 1,332 near misses being formally reported and acted upon. Employees are encouraged to report issues, however small, which then go through a rigorous corrective action process.

In recognition of the need to drive further improvements in the management of health and safety within the Group, we embarked upon a project to develop and establish a common safety culture across the Group's businesses. The project undertook audits and employee culture surveys at most sites in Europe and the US, and from the themes which emerged, a number of common approaches have been defined including leadership behaviour, training and competence, maintenance management and the implementation of safety case methodology. The project also included a review of the Group's health, safety and environment management system, which has been updated and re-published as a result.

Cultural development is an ongoing activity and further actions will emerge.

Newly-acquired businesses are rapidly introduced to the Group's safety philosophy, with detailed regulatory compliance audits and programme gap analysis. Risk registers are compiled and businesses are required to reduce their major health and safety risks to as low as reasonably practicable.

In the US, all businesses participated in a process safety management workshop, with external speakers, to ensure that a common level of knowledge and awareness was in place and best practice networks established.

The Group has committed to substantial investments in facilities that will, in addition to improving productivity, improve the safety of the workforce by reducing the levels of risk.

The Group has also established a relationship with Cranfield University, both for the supply of employee training programmes and for the development of simulation modelling to evaluate blast and thermal effects from the ignition of pyrotechnic materials.

Environment

The Board believes that environmental protection will help to secure the long term future of our businesses. The Group's Health, Safety and Environment Policy states that we will control pollution, minimise the quantity of material burnt at each site, consume resources efficiently, and use materials that minimise the environmental impact of our operations where practicable.

We now have ten sites certified to the environmental management system ISO14001. As with OHSAS18001, we require all newly-acquired businesses to achieve ISO14001 certification within two years of joining the Group. All other businesses are expected to achieve certification by the end of 2009.

Our ISO14001 programme requires that all sites have their own goals and objectives which are very much focused on local aspects and impacts. However, we continue to monitor key environmental data from a Group perspective, specifically energy consumption to allow us to derive CO₂ emissions and waste.

Corporate Responsibility Report

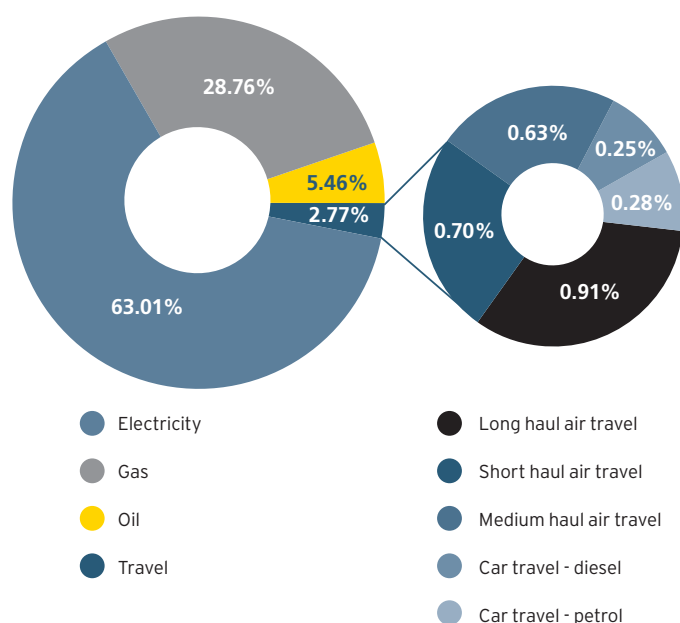
CONTINUED

We are continually improving our waste management and percentage of waste recycled. Our total waste volumes are dominated by a caustic etching process at Alloy Surfaces, which prepares metal products for coating. The waste is sold to a third party who is able to use it as feedstock for waste water treatment. This has eliminated the discharge of 6,177 tonnes of process water to local sewer systems, significantly reducing the need for the third parties to purchase neutralisation materials.

Our total non-recycled waste in the year, excluding that generated by businesses acquired during the year, was as follows:

Non-hazardous	1,027 tonnes
Hazardous	1,425 tonnes
Total	2,452 tonnes

In order to better understand our CO₂ sources, the Group monitored car and air travel throughout the year to gauge the size of this impact against the more easily accessible utilities data. The year of data collection revealed that only 2.77% of our total CO₂ emissions were generated by travel. As this data capture was difficult and time-consuming, we propose not to collect this data in the coming year but may return and check it again at some stage in the future. Our major source of CO₂ is indirect emission from electrical power generation. All Group businesses now have goals to reduce their future consumption. A breakdown of CO₂ emissions is set out below:



Our total emissions, excluding those of businesses acquired during the year, in CO₂ equivalents were as follows:

Source	2008 (tonnes CO ₂)	2007 (tonnes CO ₂)
Electricity	27,131	21,556
Gas	12,384	11,931
Oil	2,351	2,878
Total	41,866	36,365

Our total CO₂ emissions increased by 15% in a year in which the Group's revenue increased by 39%. Whilst this reduction in intensity is pleasing, we will increase our efforts to address energy conservation and thus indirect emissions in the future.

This year we are monitoring water consumption. Dependant upon what we find we may establish future targets and improvement programmes.

During the year we acquired Scot, Inc., which is based in Downers Grove, Illinois, USA. We were aware, prior to acquiring the business, that the Downers Grove area has "superfund" status under the US contaminated land (CERCLA) regime, and this was reflected in the price agreed for the business. There is a £5.0 million provision in respect of the pre-acquisition environmental liabilities associated with the site, which the Board considers to be adequate (see Note 25 of the financial statements). We are now working with external consultants to ensure that the legal obligations of the business in relation to this matter are fully satisfied.

Employees

The Board recognises the valuable contribution that the Group's employees continue to make to its success, and aims to provide a working environment that reflects and rewards this. The Group now has over 3,000 employees in seven countries.

The Group pursues a policy of employee communication through meetings (including team briefings and works councils) and in-house magazines by which employees are made aware of the progress of the Group and the companies in which they work. A Group magazine, The Chemring Eye, was introduced during the year, which is distributed to all our employees on a quarterly basis and has been well-received to date.

We continue to address training and development requirements for employees at all levels within the organisation. We are in the process of implementing a tailored management development programme for senior managers in the Group, which will be delivered by Henley Management College. This will subsequently be rolled-out to the next tier of management. Succession planning, human resource requirements and the future organisational structure of the Group as it continues to grow are reviewed on a regular basis by the Board.

The Board obtained shareholder approval for the establishment of a savings-related share option scheme at the last Annual General Meeting. The Chemring Group 2008 UK Sharesave Plan was launched for UK employees in July 2008, and The Chemring 2008 US Stock Purchase Plan was launched for US employees in August 2008. The Board is keen to encourage eligible employees to join the schemes in order that they can share in the future success of the Group. Provided that there is sufficient interest from employees, we also intend to introduce similar schemes in the other countries in which we operate.

The Group employs disabled persons wherever circumstances permit, and full and fair consideration is given to applications for employment by disabled persons having regard to their particular aptitudes and disabilities. Disabled persons in employment receive equal treatment to that afforded to other employees, in line with the Group's philosophy of equal opportunities for all employees, irrespective of race, nationality, gender, disability or age. The Group is committed to meeting, at a minimum, the labour rights and legislation requirements in each country in which it operates, and in practice, often exceeds these. These policies are introduced at newly-acquired businesses at the earliest opportunity after they join the Group. During the year, Martin Electronics received an award from its local governor, by which it was recognised as one of Florida's top employers of persons with development disabilities.

Community

The Board recognises that each of the Group's businesses has an important role to play in its local community.

The Board operates a charitable policy, which confirms its commitment to support selected charitable causes with a focus on the military and armed services, and those linked to the local communities in which the Group's businesses operate. At a Group level, charitable donations are considered on a monthly basis by the Executive Committee, and each business has its own locally held charity budget. Examples of support provided during the year include:

- Donations to a range of charities including "Help for Heroes", the Falklands Veterans' Association, Wiltshire Air Ambulance, the Salvation Army, various local hospitals and hospices, and ongoing support for the Mary Rose Appeal.
- Sole sponsorship of the 7 Air Assault Battalion Royal Electrical and Mechanical Engineers (REME) Royal Navy Field Gun Crew. The Group is proud to be associated with the 7 Air Assault Battalion, who provide support to the vehicles, weapons and aircraft of 16 Air Assault Brigade. The soldiers support aircraft in various areas of conflict around the world.
- Sponsorship of a UK employee in his efforts to compete in his chosen sport of archery at the 2012 Olympics.

In addition to making cash donations, the Group also encourages and supports employees who undertake voluntary work in the local community, where appropriate. During the year, our employees donated their time and services on a wide range of projects, several of which had an educational bias.

The Group is involved with a number of educational initiatives, notably including the sponsorship of various local schools. Each year, Kilgore awards a scholarship to a student graduating from its local high school to enable the student to pursue a college education. Certain businesses are assisting their employees who did not graduate from senior school to return to academic studies in order to supplement their vocational training. The Group has a partnership agreement with Cranfield University, under which the Group has committed to the provision of significant funding for students' research activities over the next five years. The Group has also instigated a programme which aims to attract new graduates to pursue a career in the Group, and we are now offering gap year placements in the UK.

With regards to the impact of our manufacturing activities on the local community, at locations where our operations may inconvenience neighbours through product proofing, we liaise with local residents to minimise any impact. We are also cognisant of the potential impact of our operations on the local environment, and we are addressing this through our environmental strategy.

Directors and Professional Advisers



Kenneth C Scobie~+

Non-Executive Chairman

Joined the Group as Non-Executive Chairman in June 1997. Former Chairman of Allied Leisure plc. Chairman, Chief Executive and Non-Executive Director of a wide range of industrial companies since 1972.

Aged 70.



Dr David J Price

CHIEF EXECUTIVE

Executive Director

Joined the Group in April 2005 as Chief Executive. Formerly Managing Director, Naval Marine at Rolls-Royce plc. Previous appointments in the aerospace sector include Managing Director of Thomson (UK) Holdings Ltd and Chief Executive of Thomson-Thorn Missile Electronics Ltd (both now part of the Thales Group). Fellow of the Institute of Electrical Engineers and the Institute of Marine Engineering, Science & Technology. Member of the Defence Industries Council.

Aged 53.



Paul A Rayner FCA

FINANCE DIRECTOR

Executive Director

Joined the Group in June 1994 and acted as Finance Director to several Group companies before being appointed to the Board in August 1999. Formerly a Senior Audit Manager with Deloitte LLP.

Aged 47.



David R Evans

Non-Executive Director

Joined the Group in 1987 as Managing Director of the Countermeasures business and appointed to the Board in 1988. He took up his current position as a Non-Executive Director in April 2005, after stepping down as Chief Executive, a position he had held since January 1999. Managing Director of the Marconi torpedo business prior to joining the Group. Currently a Non-Executive Director of Avon Rubber plc. Previously a Non-Executive Director of Whatman PLC.

Aged 62.

Professional advisers**Auditors**

Deloitte LLP, Southampton

Solicitors

Ashurst, London
Seyfarth Shaw, Washington

Bankers

Bank of Scotland, London

Stockbrokers

Investec Henderson
Crosthwaite, London

Headquarters and registered office

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**The Rt Hon
Lord Freeman***



Ian F R Much*~+



**Air Marshal
Sir Peter Norriss KBE
CB AFC MA FRAeS*~+**



Sarah Ellard FCIS

Non-Executive Director

Joined the Group as a Non-Executive Director in May 2006. Chairman of the Audit Committee. Currently a consultant (formerly Partner) to PricewaterhouseCoopers and Chairman of Thales UK plc. He is also on the main Board of Thales S.A., France. Chairman of Cambridge Enterprise – the University Technology Transfer Office. Partner with Lehman Brothers Investment Bankers between 1969 and 1985. Member of Parliament from 1983 to 1997. Made a Privy Councillor in 1993. Minister from 1985 to 1997.

Aged 66.

Non-Executive Director

Joined the Group as a Non-Executive Director in December 2004. Chairman of the Remuneration Committee. Previous appointments include Chief Executive of De La Rue plc and T&N plc, and Non-Executive Director of Admiral plc, Camelot plc and Manchester United plc. Currently a Non-Executive Director of Senior plc and Simplyhealth Group Ltd.

Aged 64.

Non-Executive Director

Joined the Group as a Non-Executive Director in May 2004. Currently a Non-Executive Director of Turbomeca UK Limited, Senior Military Adviser of Selex Systems Integration Limited and consultant within the aerospace and defence sector. Formerly Deputy Chief of Defence Procurement (Operations) and Controller Aircraft. Past President of the Royal Aeronautical Society and Chairman of Turbomeca UK Limited.

Aged 64.

Company Secretary

Directors' Report

The directors present their annual report, together with the audited financial statements of the Group and the Company, for the year ended 31 October 2008.

Principal activities

The principal activities of the Group are the design, manufacture and sale of energetic material products and countermeasures.

Business review

The Statement by the Chairman, the Review by the Chief Executive and the Review by the Finance Director on pages 2 to 17, together with the Business Review and the Corporate Responsibility Report on pages 18 to 31, provide a review of the Group's business development, performance and position during and at the end of the financial year; its strategy and likely future development; key performance indicators; and a description of the principal risks and uncertainties facing the business. Further information regarding financial risk management policies and financial instruments is given in Note 24 of the financial statements. Details of significant events since the balance sheet date are contained in Note 39 of the financial statements.

Results and dividends

The profit attributable to the Group's shareholders for the year was £41.2 million (2007: £32.1 million). The directors recommend a final dividend of 25p per ordinary share, which together with the interim dividend of 10p per ordinary share paid in August 2008 gives a total for the year of 35p (2007: 25p). The final dividend is subject to approval by shareholders at the Annual General Meeting on 25 March 2009, and accordingly has not been included as a liability in these financial statements.

Directors and their interests

The present directors are shown on pages 32 and 33.

Dr D J Price, Mr P A Rayner, Mr D R Evans and Mr K C Scobie will be retiring by rotation at the forthcoming Annual General Meeting and will be offering themselves for re-election. Details of the service contracts between the Company and Dr Price, Mr Rayner and Mr Scobie are set out in the Directors' Remuneration Report on page 43. Mr Evans does not have a service contract with the Company.

None of the directors had a beneficial interest in any contract of significance to which the Group was a party during the year ended 31 October 2008.

Information required as to directors' shareholdings is set out in the Directors' Remuneration Report.

Substantial shareholdings

At 20 January 2009 the following substantial holdings in the ordinary share capital of the Company had been notified to the Company in accordance with Chapter 5 of the Disclosure and Transparency Rules of the Financial Services Authority:

Name	% Interest
Standard Life Investments Ltd	6.44
Old Mutual Asset Managers	5.13
JP Morgan Chase & Co.	4.94
AXA S.A and its group of companies	4.84
Legal and General Group PLC	3.97

Employees

Details of the Group's employment policies are set out in the Corporate Responsibility Report on page 30.

Charitable and political donations

Charitable donations amounting to £29,306 (2007: £9,875) were made during the year. No political donations were made during the year (2007: £nil).

Policy on payment of suppliers

It is the policy of the Group that each of the Group companies should agree appropriate terms and conditions for its transactions with suppliers. These will range from standard written terms to individually negotiated contracts. Creditor days of the Group as at 31 October 2008 amounted to 60 days (2007: 62 days).

The Chemring Group Performance Share Plan (the "PSP")

The following conditional awards were made under the PSP during the year:

Date of award	Total number of shares awarded	Number of participants receiving awards
23 Jan 2008	98,771	24

The Chemring 1998 Executive Share Option Scheme (the "1998 ESOS")

No options were granted during the year. Options over 127,798 ordinary shares were exercised during the year. Additional information is set out in Note 32.

The Chemring Group 2008 UK Sharesave Plan (the "UK Sharesave Plan")

On 1 August 2008 options were granted over 51,416 ordinary shares. During the year options on 241 shares lapsed. No options were exercised during the year. Additional information is set out in Note 32.

The Chemring Group 2008 US Stock Purchase Plan (the "US Stock Purchase Plan")

On 16 September 2008 options were granted over 6,953 ordinary shares. No options were exercised during the year. Additional information is set out in Note 32.

The Chemring Group PLC Share Based Incentive Scheme (the "ESOP")

No options were granted during the year and there were no options outstanding under the ESOP at 31 October 2008.

Approach to share ownership

The Group actively encourages its employees to share in the future success of the Group. The UK Sharesave Plan and the US Stock Purchase Plan were both launched during the year, following approval at the Annual General Meeting held on 20 March 2008. The Board is currently considering the establishment of similar schemes for employees in Group companies outside of the UK and the US.

Share capital and shareholder rights**General**

The Company's share capital consists of ordinary shares of 5p each and preference shares of £1 each, which are fully paid up and quoted on the main market of the London Stock Exchange. Full details of the movements in the authorised and issued share capital of the Company during the financial year are provided in Note 27 of the financial statements.

All holders of ordinary shares are entitled to attend, speak and vote at any general meeting of the Company and to appoint a proxy or proxies to exercise these rights. At a general meeting, every shareholder present in person, by proxy or (in the case of a corporate member) by corporate representative has one vote on a show of hands, and on a poll has one vote for every share held.

To decide who can attend or vote at a general meeting, the notice of meeting can give a time, which must not be more than 48 hours before the meeting, by which shareholders must have entered on the register in order to have the right to attend or vote at the meeting.

If a shareholder has been properly served with notice under section 793 of the Companies Act 2006 requiring information about interests in shares, and has failed to supply such information within 14 days after the service of the notice, then the shareholder is not entitled to attend and vote at a shareholder meeting.

There are no restrictions on the transfer of ordinary shares in the capital of the Company other than certain restrictions which may from time to time be imposed by law, for example insider trading law. In accordance with the Listing Rules of the Financial Services Authority, certain employees are required to seek the approval of the Company to deal in its shares.

The cumulative preference shares carry an entitlement to a dividend at the rate of 7p per share per annum, payable in equal instalments on 30 April and 31 October each year. Holders of the preference shares have the right on winding-up to receive, in priority to any other classes of shares, the sum of £1 per share together with any arrears of dividends.

The Company is not aware of any agreements between shareholders that may result in restrictions on the transfer of securities and/or voting rights.

The Company's Articles of Association may only be amended by special resolution at a general meeting of shareholders.

Directors' Report

CONTINUED

Issue of shares

Under the provisions of section 80 of the Companies Act 1985 ("the Act") the Board is prevented from exercising its powers under the Articles of Association ("the Articles") to allot shares without an authority in terms of the Act contained either in the Articles or in a resolution of the shareholders in general meeting. The authority, when given, can last for a maximum period of five years, but the Board proposes that renewal should be sought at each Annual General Meeting. Such proposal is set out as resolution 9 in the Notice of the Annual General Meeting.

Section 89 of the Act requires that an allotment of shares for cash may not be made unless the shares are first offered to existing shareholders on a pre-emptive basis in accordance with the terms of the Act. In accordance with general practice, to ensure that small issues of shares can be made without the necessity of convening a general meeting, the Board proposes that advantage be taken of the provisions of section 95 of the Act to not apply the Act's pre-emptive requirements. Accordingly, a special resolution (set out as resolution 10 in the Notice of Annual General Meeting) will be proposed which, if passed, will have the effect of granting the directors the power to allot not more than 5% of the present issued ordinary share capital free of the requirements of section 89 of the Act. No issue of these shares will be made which would effectively alter the control of the Company without prior approval of the shareholders in general meeting.

Purchase of own shares

During the year the Company purchased 160,000 (2007: 150,000) of its ordinary shares. At 31 October 2008, the Company held a total of 310,000 ordinary shares in treasury (representing 0.9% of the ordinary shares in issue on 1 November 2008). All purchases of ordinary shares were by means of market purchases through the London Stock Exchange. Further details can be found in Note 30 of the financial statements.

A special resolution (set out as resolution 11 in the Notice of Annual General Meeting) will be proposed at the forthcoming Annual General Meeting, to renew the Company's authority to purchase its own shares in the market up to a limit of 10% of its issued ordinary share capital. The maximum and minimum prices are stated in the resolution. The directors believe that it is advantageous for the Company to have this flexibility to make market purchases of its own shares. The directors of the Company will consider holding repurchased shares pursuant to the authority conferred by this resolution as treasury shares. This would give the Company the ability to re-issue treasury shares quickly and cost effectively and would provide the Company with additional flexibility in the management of its capital base. Any issues of treasury shares for the purposes of the Company's employee share schemes will be made within the 10% anti-dilution limit set by the Association of British Insurers. The directors will only exercise this authority if they are satisfied that a purchase would result in an increase in expected earnings per share and would be in the interests of shareholders generally.

Statement of Directors' Responsibilities

The directors are responsible for preparing the annual report, the Directors' Remuneration Report and the financial statements. Company law requires the directors to prepare financial statements for each financial year. The directors are required by the IAS Regulations to prepare the Group accounts under International Financial Reporting Standards (IFRSs) as adopted by the European Union. The Group financial statements are also required by law to be properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. International Accounting Standard 1 requires that financial statements present fairly for each financial year the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's "Framework for the Preparation and Presentation of Financial Statements". In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable International Financial Reporting Standards. Directors are also required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in International Financial Reporting Standards is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance;
- for the Company financial statements, state whether applicable UK accounting standards have been followed; and
- prepare the accounts on a going concern basis unless, having assessed the ability of the Company to continue as a going concern, management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a directors' report, which comply with the requirements of the Companies Act 1985.

The directors are responsible for the maintenance and integrity of the Company website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements differs from legislation in other jurisdictions.

The directors confirm that suitable accounting policies, consistently applied and supported by reasonable and prudent judgments and estimates, have been used in the preparation of the financial statements, and that applicable accounting standards have been followed.

Directors' Responsibility Statement

We confirm to the best of our knowledge that:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position, and profit and loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Statement by the Chairman, the Review by the Chief Executive, the Review by the Finance Director, the Business Review and the Corporate Responsibility Statement, which are cross-referred from the Directors' Report, include a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties they face.

Provision of information to auditors

Each of the directors at the date of approval of this report confirms that:

- so far as the director is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- the director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s234ZA of the Companies Act 1985.

Close company provisions

As far as the directors are aware, the close company provisions of the Taxes Acts do not apply to the Group nor has there been any change in that respect since 31 October 2008.

Auditors

On 1 December 2008, Deloitte & Touche LLP changed its name to Deloitte LLP. A resolution to re-appoint Deloitte LLP as auditors will be proposed at the Annual General Meeting.

Annual General Meeting

The resolutions to be proposed at the Annual General Meeting to be held on 25 March 2009, together with explanatory notes, appear in the separate Notice of Annual General Meeting sent to all shareholders.

Approved by the Board of Directors on 20 January 2009

Signed on behalf of the Board

S L Ellard

COMPANY SECRETARY

Directors' Remuneration Report

This report sets out the information required by the Directors' Remuneration Report Regulations 2002 ("the Regulations"). The Report has been prepared in accordance with Schedule 7A to the Companies Act 1985, meets the relevant requirements of the Listing Rules of the Financial Services Authority, and describes how the Board has applied the principles relating to directors' remuneration in the Combined Code. As required by the Regulations, the Directors' Remuneration Report will be submitted to shareholders for approval at the Annual General Meeting on 25 March 2009.

UNAUDITED INFORMATION

Remuneration Committee

During the year under review the Remuneration Committee comprised:

Mr I F R Much (Committee Chairman)
Air Marshal Sir Peter Norriss
The Rt Hon Lord Freeman
Mr K C Scobie

The Committee's principal responsibilities are:

- determining, agreeing with the Board and reviewing from time to time the overall policy for the remuneration of the Chairman, the executive directors, the Company Secretary and certain other senior executives in the Group, and their individual remuneration packages and any changes thereto;
- approving the terms and conditions of employment, and any changes thereto, of the executive directors;
- approving any compensation payments for executive directors;
- approving the design of, and determining targets for, any performance-related pay schemes operated by the Group;
- reviewing the design of all share incentive plans for approval by the Board and the Company's shareholders; and
- overseeing any major changes in employee benefits structures across the Group.

None of the Committee members has any personal financial interest in the matters reserved for the Committee (other than the Chairman in respect of his own remuneration; accordingly, he is not present during any discussions relating to this matter), nor do they have any conflicts of interest arising from cross-directorships, and they are not involved in the day to day running of the Group's business. Therefore, they are regarded by the Board as independent.

The Committee met six times during the year. The Chief Executive attends meetings by invitation but is not present during any discussions relating to his own remuneration.

The terms of reference of the Committee are available on the Company's website or on request from the Company Secretary.

Advisers

During the year the Committee received advice on remuneration matters from Hewitt New Bridge Street.

The Committee also consults internally with the Chief Executive and the Company Secretary.

Remuneration policy for executive directors

The Committee's policy is to provide executive remuneration packages which are competitive, but not excessive, by reference to market rates across comparator companies, reflect the performance of the business against financial objectives, and which take into account the individual contribution and performance of each executive director. Remuneration packages comprise the following elements:

- (i) basic salary and benefits, including pensions;
- (ii) annual bonuses linked to the Group's financial performance; and
- (iii) awards of share-based incentives linked to the long term growth of the Group.

The Committee aims to align the interests of executive directors with those of shareholders, by ensuring that a significant proportion of remuneration is performance-related. This is achieved through the performance-related elements of annual bonuses and share-based incentives.

In January 2008, the Committee decided that it needed to undertake a full review of the total remuneration packages which applied to the executive directors and senior managers, against the background of the substantial growth achieved by the Group in terms of revenue, profits and market capitalisation over the last few years and the enhanced complexity of the Group arising from this growth.

This review was carried out using a number of published reports prepared by third parties and an independent report which was commissioned from Hewitt New Bridge Street. The main findings of the report were that:

- directors' fixed pay levels were at or below lower quartile when compared with both sector companies and general companies of similar turnover and market capitalisation;
- the maximum annual bonus potential for directors of 60% of salary was significantly below the market norm; and
- the total value of the remuneration package of both of the executive directors was at or below the market lower quartile.

Following this review, the Committee decided to increase basic salaries from 1 April 2008 for Dr Price and Mr Rayner to £400,000 per annum and £250,000 per annum respectively to reflect their outstanding performance and to bring them closer to market norms. It also agreed to increase the maximum bonus potential for the executive directors to 100% of salary with effect from 1 November 2008.

The Committee believes that these changes achieve the correct balance between an appropriate level of basic pay and the opportunity to see increased levels of variable pay if the Group continues to be as successful as in the last three years. The Committee is comfortable that the resulting packages are appropriate, given the strong recent growth of the Company, and necessary to ensure the retention of key executives whose recent performance has proved their significant value to the business and shareholders.

Basic salaries and benefits

The executive directors' basic salaries are reviewed annually by the Committee, and adjustments made, if appropriate, taking into account individual performance and comparable salary levels in manufacturing companies of a similar size and in other companies within the aerospace and defence sector. The Committee refers to published salary surveys and data provided by its remuneration advisers, Hewitt New Bridge Street, and also reviews the remuneration information presented in the annual reports of companies in the reference group.

The main taxable benefits for executive directors are company cars, fuel for private motoring and private medical insurance.

Annual bonuses

During the year under review, the Company operated an annual performance-related bonus plan for the executive directors, with key characteristics as follows:

- a maximum bonus potential for the executive directors of 60% of basic salary, with an on-target bonus of 30% of basic salary;
- three quarters of the bonus potential linked to two separate financial performance conditions, namely earnings per share and cash flow (with equal weighting). The conditions, which are set by the Committee, take into account a number of factors including budget, market expectations, long term growth prospects and the previous year's out-turn. No bonus is payable for achievement of less than 90% of target, with bonuses being earned thereafter on a straight-line basis up to the maximum for 110% or better achievement of target;
- one quarter of the bonus potential may be achieved in connection with the satisfaction of personal objective criteria set at the beginning of the financial year. These comprise a mixture of short term and longer term objectives linked to the delivery of the Company's strategic plan. No part of this element of bonus is payable unless threshold performance of both the financial conditions described above is achieved;
- one quarter of any bonus payable is deferred as a conditional award of the Company's shares, with vesting subject to continued employment (save in good leaver scenarios) three years from the award of bonus; and
- the payment of any bonus remains ultimately at the discretion of the Committee.

Bonuses are non-pensionable.

The table below summarises the bonuses earned by the executive directors, as a percentage of basic salary, in respect of the current and last years:

	Earnings per share target %		Cash flow target%		Achievement of personal objectives %		Total %	
	2008	2007	2008	2007	2008	2007	2008	2007
D J Price	19.1	19.0	22.5	15.1	10.5	12.0	52.1	46.1
P A Rayner	19.1	19.0	22.5	15.1	12.7	10.5	54.3	44.6

Directors' Remuneration Report

CONTINUED

As noted above, the review undertaken by the Committee in January 2008 identified that a maximum annual bonus potential of 60% of salary for executive directors is below market norms. The median maximum bonus in both comparator groups and the FTSE 250 as a whole is 100% of salary. It has therefore been agreed that, with effect from 1 November 2008, the maximum bonus potential for the executive directors will increase to 100% of annual salary, with appropriate targets to ensure that the upper quartile of payments is only achieved in exceptional years. All other aspects of the bonus scheme will remain unchanged (namely 25% deferred in shares and bonus determined by a mixture of EPS, cash flow and personal targets).

In relation to this increase in bonus potential, shareholders can take comfort from the Committee's track record of setting highly challenging bonus targets in recent years, as evidenced by the fact that the executive directors have not received maximum bonuses in any of the last four years despite outstanding levels of EPS growth and returns to shareholders (see chart below).

Year	2005	2006	2007	2008
Growth in underlying EPS ¹	52%	53%	56%	43%
Return to shareholders in year	70%	145%	41%	-23%

Executive	D J Price	P A Rayner	D J Price	P A Rayner	D J Price	P A Rayner	D J Price	P A Rayner
Maximum bonus potential (% of salary)	45%		60%		60%		60%	
Bonus paid (% of salary)	37.3% ²	37.3%	58.5%	58.5%	46.1%	44.6%	52.1%	54.3%

¹Source: Statutory accounts for the years ended 31 October 2005, 2006, 2007 and 2008

²Pro-rated to reflect mid-year joining

Long term incentive schemes

Performance share plan

The Company operates the Chemring Group Performance Share Plan for the executive directors and other key members of the senior management team who influence the performance and prospects of the Group. The key features of the plan are as follows:

- conditional awards can be made of the Company's shares worth no more than 100% of basic salary each year;
- awards will vest three years after grant subject to the extent to which a demanding performance condition has been achieved over a single three year performance period (with no ability to re-test the performance condition). The performance condition is based on the growth of the Company's earnings per share in excess of RPI over three consecutive financial years. The Committee considers an earnings per share condition to most closely align the interests of participants with those of the Company's shareholders;
- the following vesting schedule applies in respect of awards made prior to 23 January 2007:

Total earnings per share growth per annum (not compounded) over three financial years	Percentage of the total number of shares under an award that vest
Less than RPI + 5%	Nil
RPI + 5%	33%
RPI + 15% or more	100%
Between RPI + 5% and RPI + 15%	Between 33%-100% on a straight-line basis

- the following vesting schedule applies in respect of awards made on 24 January 2007:

Total earnings per share growth per annum (not compounded) over three financial years	Percentage of the total number of shares under an award that vest
Less than RPI + 7.5%	Nil
RPI + 7.5%	33%
RPI + 20% or more	100%
Between RPI + 7.5% and RPI + 20%	Between 33%-100% on a straight-line basis

- the following vesting schedule applies in respect of awards made on or after 23 January 2008. The Committee has determined that this highly challenging performance condition remains appropriate for any awards which may be made during the current financial year:

Total earnings per share growth per annum (not compounded) over three financial years	Percentage of the total number of shares under an award that vest
Less than RPI + 10%	Nil
RPI + 10%	25%
RPI + 30% or more	100%
Between RPI + 10% and RPI + 30%	Between 25%-100% on a straight-line basis

- earnings per share is calculated on a fully diluted and normalised basis, as specified by the Committee prior to grant; and
- market purchase shares or new issue shares (including treasury shares) may be used to satisfy awards. To the extent that new issue shares or treasury shares are used, these will count towards the usual share usage dilution limits (10% in ten years for all schemes and 5% in ten years for discretionary (executive) schemes).

Participation in the plan is extended at the discretion of the Committee to the executive directors and senior management of the Group, both in the UK and overseas. The following awards were made under the plan during the year:

Date of award	Total number of shares awarded	Number of participants receiving awards
23 Jan 2008	98,771	24

Details of the awards made to executive directors during the year are set out on page 45. The Committee has verified that the current annual awards to the executive directors of performance shares worth 100% of salary are around market compared to the Company's two comparator groups and the FTSE 250 as a whole. The current arrangements for the level of awards to the executive directors under the plan will therefore remain unchanged for the foreseeable future.

The executive directors are expected to build-up, over a five year period following appointment, and maintain a shareholding in the Company equivalent to one year's basic salary. Other participants in the plan are expected to retain a shareholding equivalent to 25% of their basic salary following vesting of the awards.

During the year, the Company purchased 160,000 (2007: 150,000) treasury shares at a cost of £2.9 million for use in the plan.

Other schemes

The Company introduced all-employee savings-related share schemes in the UK (The Chemring Group 2008 Sharesave Plan) and the US (The Chemring Group 2008 US Stock Purchase Plan) during the year. There are no performance criteria for these arrangements and options are issued to all participants in accordance with UK HM Revenue and Customs and US Internal Revenue Service regulations.

Between 1998 and 2005 the Company operated the Chemring 1998 Executive Share Option Scheme. Following the introduction of the Chemring Group Performance Share Plan, no further grants have been made under the option scheme, save in exceptional circumstances such as on recruitment, and the conditions applying to any such grants have accorded with current corporate governance best practice. The scheme ceased to operate for any new grants on 4 March 2008.

The Company previously operated a long term incentive scheme known as the Chemring Group PLC Share Based Incentive Scheme. This scheme is not being utilised at present.

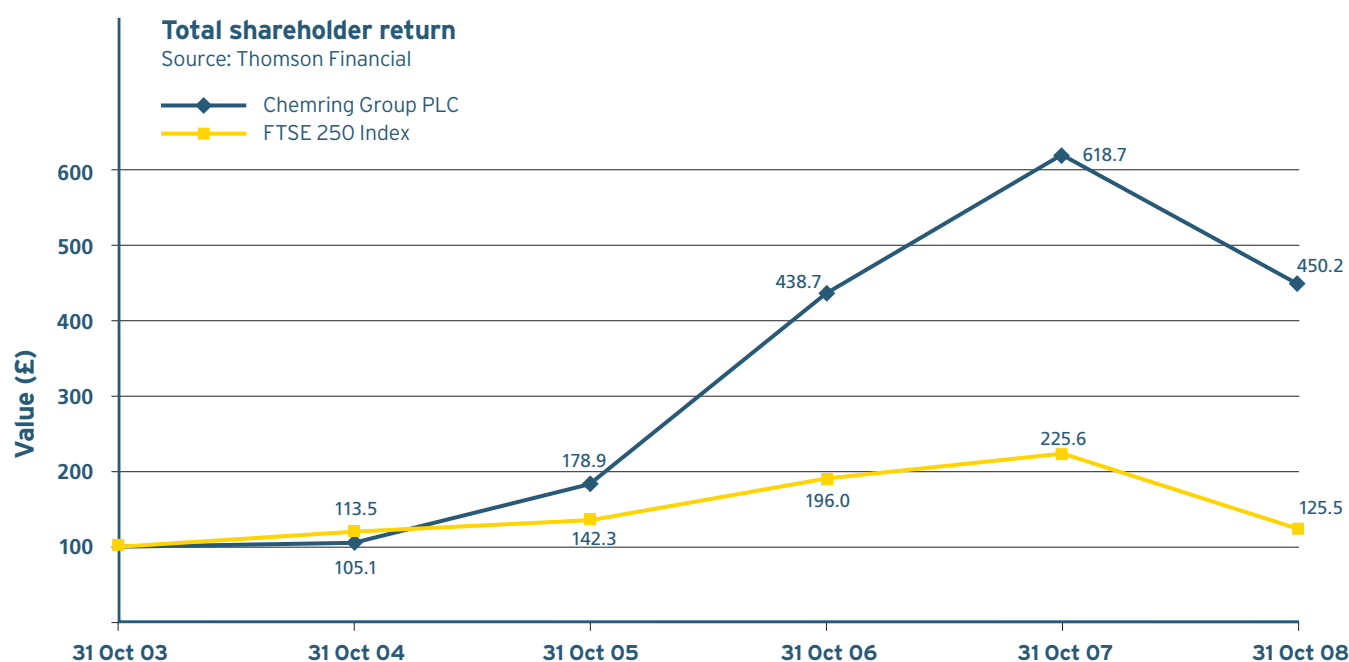
The Company complies with the dilution guidelines contained within "Executive Remuneration - ABI Guidelines on Policies and Practices". At 31 October 2008, awards outstanding and issued under all share schemes during the previous ten years amounted to 2.87% of the ordinary share capital of the Company. At 31 October 2008, awards outstanding and issued under executive share schemes during the previous ten years amounted to 2.71% of the ordinary share capital of the Company.

Directors' Remuneration Report

CONTINUED

Performance graph

The following graph shows a comparison of the Company's total shareholder return (TSR) over the last five financial years against a "broad equity market index", as required by the Regulations. The FTSE 250 Index has been selected by the Committee for this comparison because it provides the most appropriate measure of performance of listed companies of a similar size to the Company.



This graph shows the value, by 31 October 2008, of £100 invested in Chemring Group PLC on 31 October 2003 compared with the value of £100 invested in the FTSE 250 Index. The other points plotted are the values at intervening financial year ends.

Pensions

Dr Price is a member of the Chemring Group Staff Pension Scheme ("the Staff Scheme"). This is an approved final salary scheme, which is contracted out of the State Second Pension, and which provides, at retirement, a pension of up to two-thirds of salary, subject to Inland Revenue limits. The Staff Scheme also provides life assurance cover, dependants' pensions and lump sum payments on death-in-service. Members of the Staff Scheme are required to make monthly contributions to the scheme at the rate of 8% of pensionable salary.

Dr Price's pension under the Staff Scheme accrues at 1/80th of final pensionable salary for each year of membership, and he also accrues a cash lump sum at 3/80ths of final pensionable salary for each year of membership. On death-in-service, Dr Price's dependants would receive a lump sum payment of two times basic salary and, in addition, a 50% spouses' pension would be payable. Dr Price is subject to an earnings cap (equivalent to the cap applied by HM Revenue and Customs prior to April 2006) in respect of his membership of the Staff Scheme.

Mr Rayner is a member of the Chemring Group Executive Pension Scheme ("the Executive Scheme"). The Executive Scheme is also an approved final salary scheme but is not contracted out of the State Second Pension. Members of the Executive Scheme are required to make monthly contributions to the scheme at the rate of 8% of pensionable salary. Mr Rayner's benefits under the Executive Scheme accrue in an identical manner to that in which Dr Price accrues benefits under the Staff Scheme, as set out above, save that a two-thirds' spouses pension is payable in respect of service accrued to 31 January 2004, reducing to 50% for service accrued thereafter. Mr Rayner is also subject to an earnings cap.

Although the current pension arrangements for the executive directors (1/80ths accrual rate only as far as the notional earnings cap) are well below market norms, the Committee determined, following its January 2008 review, that it would not change either the accrual rate or the notional earnings cap.

Both Dr Price and Mr Rayner have a normal retirement age of 65.

Service contracts

Dr Price has a rolling service contract dated 4 April 2005. This provides for termination by either party on twelve months' notice. The Company may however terminate without notice, and make a payment in lieu of notice equal to the sum of the salary due for the unexpired notice period plus the fair value of any contractual benefits. Any such sum may be paid in instalments, and in these circumstances there is a requirement to mitigate loss.

Mr Rayner has a rolling service contract dated 27 August 1999. This provides for termination by either party on twelve months' notice. The Company may however terminate without notice and make a payment in lieu of notice equal to the sum of twelve months' salary plus the value of any contractual benefits. There are no other provisions relating to compensation on early termination.

It is the Committee's general policy that all new executive directors appointed in the future will have service contracts with the Company which are terminable on a maximum of twelve months' notice. The service contracts will contain provisions permitting the Company to make any termination payments by instalments, and will require directors to mitigate their loss in such circumstances.

Policy on outside appointments

With the specific approval of the Board in each case, executive directors may accept external appointments as non-executive directors of other companies, provided that they do not detract from their responsibilities to the Group, and may retain any related fees paid to them. Neither of the executive directors currently hold any such external appointments.

Non-executive directors

Mr Scobie has a service contract with the Company which will expire at the conclusion of the Company's Annual General Meeting in March 2010, unless terminated earlier on twelve months' notice by either party. His appointment may be extended by one further year by mutual agreement of both parties. His remuneration under the contract, part of which is paid to his company for consultancy services, is £125,000 per annum. He is required to devote such time to his role as is reasonably necessary for the proper performance of his duties.

Mr Evans, The Rt Hon Lord Freeman, Mr Much and Air Marshal Sir Peter Norriss have letters of appointment covering, amongst other items, their terms of appointment and expected time commitment. These letters of appointment provide for three year appointments, unless terminated earlier by and at the discretion of either party upon three months' written notice. Mr Much and Air Marshal Sir Peter Norriss are currently serving their second three year terms as non-executive directors, which will expire on 30 April 2010 and 30 November 2010 respectively. It is anticipated that, subject to satisfactory performance, The Rt Hon Lord Freeman will also be invited to serve a second three year term on expiry of his current appointment on 25 May 2009. Mr Evans' current appointment as a non-executive director expires on 30 March 2009; in view of his continuing contribution to the Board, it has been agreed that, subject to re-election by the shareholders at the forthcoming Annual General Meeting, his appointment will be extended for an additional three year term.

The basic fee payable to each of the four non-executive directors is £40,000 per annum. The Rt Hon Lord Freeman and Mr Much each receive an additional fee of £6,000 per annum, in respect of their Chairmanship of the Audit Committee and Remuneration Committee respectively.

Fees for the non-executive directors are determined annually by the Board, having regard to the practice of other companies and the particular demands of the Group. The Company provides private medical insurance for Mr Scobie, Mr Evans and Air Marshal Sir Peter Norriss, and their respective spouses.

The non-executive directors do not participate in the Company's pension, bonus or share-based incentive schemes. However, Mr Evans does receive a pension from the Chemring Group Executive Pension Scheme, which he accrued during his former employment with the Company. In addition, a long term incentive scheme, known as The Chemring Group Phantom Share Option Scheme, was established in 1997 to secure the appointment of Mr Scobie as Chairman at a difficult time when the Group was undergoing a fundamental reorganisation. Mr Scobie, who was the only participant in the scheme, acquired a contractual entitlement on his appointment in 1997 to the grant of phantom options over 141,025 ordinary shares in the Company at a notional exercise price of 78p per share. Mr Scobie exercised his rights under this scheme on 31 October 2007 and received a cash payment from the Company in November 2007 of £3,008,063 (gross), being equivalent to the difference between the market value of the ordinary shares on the exercise date (2,211p) less the total exercise price. This scheme has now terminated.

Directors' Remuneration Report

CONTINUED

AUDITED INFORMATION

Directors' emoluments

The emoluments of all the directors who served during the year are shown below:

	Salaries and fees		Bonuses (cash and deferred shares)		Taxable benefits		2008 £000	Total 2007 £000
	2008 £000	2007 £000	2008 £000	2007 £000	2008 £000	2007 £000		
Executives								
D J Price	379	329	208	161	31	31	618	521
P A Rayner	238	208	136	98	19	19	393	325
Non-executives								
D R Evans	38	34	-	-	1	1	39	35
R N Freeman	43	38	-	-	-	-	43	38
I F R Much	43	38	-	-	-	-	43	38
P C Norriss	38	34	-	-	1	1	39	35
K C Scobie	123	102	-	-	3	2	126	104
Total remuneration	902	783	344	259	55	54	1,301	1,096

Amounts shown above in the salaries and fees column relate to basic salary in the case of executive directors and fees in the case of non-executive directors.

Mr Scobie's remuneration includes payments to his company, K C Scobie Limited, in respect of his consultancy services. In addition to the remuneration shown above, Mr Scobie received a cash payment of £3,008,063 (gross) in November 2007, following the exercise of his phantom options under the long term incentive scheme established on his appointment, further details of which are given on page 43.

Directors' share interests

The interests of the directors in the ordinary shares of the Company at 1 November 2007 and 31 October 2008 are shown below. All are beneficial holdings.

	2008 Number	2007 Number
D R Evans	15,000	50,348
R N Freeman	350	350
I F R Much	3,000	3,000
P C Norriss	5,400	4,600
D J Price	97,698	72,900
P A Rayner	30,500	21,100
K C Scobie	216,173	195,964

The directors' share interests at 31 October 2008 include shares held by the directors' adult children, as required by the Companies Act 2006.

During November 2008, Mr Scobie purchased an additional 4,000 ordinary shares. No other movements have taken place between 31 October 2008 and 20 January 2009.

In addition to the interests detailed above, by the virtue of section 324 of the Companies Act 1985, the executive directors are technically deemed to be interested in all of the shares held by the Trustee of the Chemring Group PLC Share Based Incentive Scheme. 31,198 ordinary shares were held by the Trustee at 31 October 2008.

Performance share plan

Details of awards made to the executive directors under the Chemring Group Performance Share Plan are shown below.

	Number of shares under award				At 31 Oct 2008	Date of vesting	Share price on date of award (p)
	At 1 Nov 2007	Awarded during the year	Lapsed during the year	Vested during the year			
D J Price	22,321	-	-	-	22,321	23 Mar 2009	1,136
	17,543	-	-	-	17,543	24 Jan 2010	1,730
	-	18,004	-	-	18,004	23 Jan 2011	1,895
	39,864	18,004	-	-	57,868		
P A Rayner	14,285	-	-	-	14,285	23 Mar 2009	1,136
	11,111	-	-	-	11,111	24 Jan 2010	1,730
	-	11,316	-	-	11,316	23 Jan 2011	1,895
	25,396	11,316	-	-	36,712		

Awards were granted during the year on 23 January 2008. 25% of the shares under award will vest if earnings per share growth is RPI+10% p.a. over the three year performance period, rising on a straight-line basis to full vesting for growth of at least RPI+30% p.a.

Share options

The holdings by the executive directors of share options granted under the Chemring 1998 Executive Share Option Scheme at 1 November 2007 and 31 October 2008 are shown below.

	Number of share options				At 31 Oct 2008	Exercise price (p)	Market price at date of exercise (p)	Aggregate gain on exercise (£)	Date from which exercisable	Expiry date
	At 1 Nov 2007	Granted during the year	Lapsed during the year	Exercised during the year						
D J Price	52,798	-	-	46,463	-	473.5	2,377	884,423	7 Apr 2008	6 Apr 2015
				6,335	-	473.5	2,295	115,392	7 Apr 2008	6 Apr 2015
P A Rayner	25,000	-	-	25,000	-	436.5	2,382	486,375	8 Jul 2007	7 Jul 2014

The holdings by the executive directors of share options granted under the Chemring Group 2008 UK Sharesave Plan at 1 November 2007 and 31 October 2008 are shown below.

	Number of share options				At 31 Oct 2008	Exercise price (p)	Market price at date of exercise (p)	Date from which exercisable	Expiry date
	At 1 Nov 2007	Granted during the year	Lapsed during the year	Exercised during the year					
D J Price	-	503	-	-	503	1,868	-	1 Aug 2011	31 Jul 2018
P A Rayner	-	871	-	-	871	1,868	-	1 Aug 2013	31 Jul 2018

Directors' Remuneration Report

CONTINUED

Deferred shares

Details of awards of deferred shares made to the executive directors under the annual performance-related bonus plan are set out below.

	Number of deferred shares under award				At 31 Oct 2008	Date of vesting	Share price on date of award (p)
	At 1 Nov 2007	Awarded during the year	Lapsed during the year	Vested during the year			
D J Price	2,566	-	-	-	2,566	16 Jan 2010	1,710
	-	1,944	-	-	1,944	10 Jan 2011	1,944
	2,566	1,944	-	-	4,510		
P A Rayner	1,625	-	-	-	1,625	16 Jan 2010	1,710
	-	1,261	-	-	1,261	10 Jan 2011	1,944
	1,625	1,261	-	-	2,886		

Awards will vest subject only to the continued employment of the executive directors.

The market price of the ordinary shares at 31 October 2008 was 1,590p. During the year, the ordinary shares traded within the range 1,570p to 2,545p.

Pensions

The following table sets out the pension benefits accrued by the executive directors during the year.

	Total benefit accrued at 31 Oct 07		Transfer value of accrued benefit at 31 Oct 07 (£)	Increase in accrued benefit during year before inflation		Total benefit accrued at 31 Oct 08		Transfer value of accrued benefit at 31 Oct 08 (£)	Increase in accrued benefit during year after inflation		Transfer value of increase in accrued benefit after inflation (less members' contributions) (£)	Increase in transfer value during year (less members' contributions) (£)
	Pension (£ p.a.)	Cash (£)		Pension (£ p.a.)	Cash (£)	Pension (£ p.a.)	Cash (£)		Pension (£ p.a.)	Cash (£)		
D J Price	3,525	10,575	40,592	1,620	4,860	5,145	15,435	60,693	1,472	4,415	8,143	10,835
P A Rayner	18,917	56,752	228,417	2,275	6,825	21,192	63,577	254,281	1,478	4,434	3,920	16,648

- i) Transfer values represent liabilities of the applicable scheme, and do not represent sums paid to the individuals.
 ii) Transfer values have been calculated on the basis of actuarial advice in accordance with actuarial professional guidance.

Approval of the Directors' Remuneration Report

The Directors' Remuneration Report was approved by the Board on 20 January 2009.

Signed on behalf of the Board

I F R Much

CHAIRMAN OF THE REMUNERATION COMMITTEE

Statement on Corporate Governance

This statement sets out how the Company has applied the main and supporting principles of good governance set out in Section 1 of the Combined Code on Corporate Governance issued in 2006 by the Financial Reporting Council ("the Combined Code"), and whether or not the Company has complied throughout its accounting period with the provisions of Section 1 of the Combined Code.

The Board

The Board currently comprises the Chairman, the Chief Executive, the Finance Director and four non-executive directors. The Board considers that three of the current non-executive directors, The Rt Hon Lord Freeman, Mr Much and Air Marshal Sir Peter Norriss, are independent in character and judgment, and meet the criteria for independence set out in the Combined Code. The directors' biographical details are set out on pages 32 and 33.

The Board, which meets at least ten times a year, approves the Group's long term goals and strategies and provides overall financial and organisational control. The Board has a formal schedule of matters specifically reserved to it for consideration and approval, including: approval of the Group's corporate plan; approval of the annual operating budgets; acquisitions, disposals and major capital expenditure; financing and treasury; pensions; ethical policies; health and safety strategy; reviewing the Group's systems of financial control and risk management; approving appointments to the Board and approving policies relating to directors' remuneration; and maintaining an effective dialogue with shareholders. All directors take decisions objectively in the interests of the Company.

The Board delegates certain responsibilities to the Executive Committee, including: implementation of the Group's strategies and policies as determined by the Board; monitoring of operational and financial results against budget; allocation of resources across the Group within the overall plan approved by the Board; capital expenditure within limits imposed by the Board; and developing and implementing risk management systems. Further details of the Executive Committee are set out in the section of this report covering Board Committees.

Procedures are in place covering the content, presentation and timely delivery of papers to the Board for each Board meeting, to ensure that directors have sufficient information to make expedient and considered decisions in fulfilment of their fiduciary duties. Where directors have concerns which cannot be resolved about the running of the Company or a proposed action, such concerns are recorded in the Board minutes.

Each director has full access to the advice and services of the Company Secretary who, under the direction of the Chairman, is responsible for maintaining good information flows within the Board and its committees, assisting with induction and keeping the directors informed about changes to their duties and responsibilities, and advising the Board on all governance matters. The appointment and removal of the Company Secretary is a matter for the Board as a whole.

All directors are entitled to take independent professional advice in furtherance of their duties at the Company's expense, if the need should arise.

An internal induction programme on the Group's operations and its strategic and business plans is provided for newly-appointed directors. The Company Secretary also provides detailed information on directors' legal duties and responsibilities on appointment, and updates the Board on a regular basis with regards to regulatory changes affecting the directors and the Group's operations generally. Directors are continually updated on the Group's businesses and the matters affecting the market in which they operate. The Company meets the cost of appropriate external training for directors, the requirement for which is kept under review by the Chairman.

The Company separates the roles of Chairman and Chief Executive in accordance with the recommendations of the Combined Code. The division of responsibilities between the Chairman and the Chief Executive, and their respective job descriptions, are set out in writing and agreed by the Board.

In addition to chairing the Board, the Chairman is responsible for: ensuring that the Board is kept properly informed and is consulted on all decisions reserved to it; promoting constructive relations between the executive and non-executive directors; ensuring that the development needs of directors are identified and the performance of the Board evaluated on a regular basis; and ensuring effective communication with shareholders and acting as a conduit to ensure that the views of shareholders are communicated to the Board. The Chairman has no significant business commitments other than his chairmanship of the Company.

The non-executive directors perform an essential role in safeguarding shareholders' interests. They actively participate in the development of strategic objectives and monitor the performance of executive management in achieving these objectives. The non-executive directors also review financial performance, and consider the integrity of the financial information produced by the Group and whether the financial controls and risk management systems are robust and defensible. They meet periodically with the management of the Group's operating companies. In addition to participating in Board meetings, the three independent non-executive directors are the members of the standing committees set up to deal with audit and the remuneration of executive directors and senior management. The Board considers that the current balance of executive and non-executive influence which exists is appropriate for the Company, taking into account its size and status.

The Board has not appointed a senior independent director, as it does not consider this to be appropriate at the present time in view of the size of the Board.

During the financial year, the Chairman met regularly with the non-executive directors without the executives present.

Statement on Corporate Governance

CONTINUED

Mr Evans, The Rt Hon Lord Freeman, Mr Much and Air Marshal Sir Peter Norriss all have letters of appointment covering, amongst other items, their terms of appointment and expected time commitment. These letters of appointment provide for a three year appointment, unless terminated earlier by and at the discretion of either party upon three months' written notice. The non-executive directors' letters of appointment are available for inspection on request to the Company Secretary.

In accordance with the Combined Code and the Company's Articles of Association, all directors submit themselves for re-election every three years. The Chairman will now offer himself for re-election annually, having reached the age of 70 and having served for more than nine years as a non-executive director.

The papers accompanying the Notice of Annual General Meeting include a statement from the Chairman confirming that the performance of each non-executive director seeking re-election at the meeting continues to be effective and that each such director continues to demonstrate commitment to their role.

A full evaluation of the performance of the Board and its committees was undertaken during the year. The process adopted involved each of the directors considering a structured questionnaire, the responses to which were discussed at a full Board meeting. In addition, the Chairman and the non-executive directors considered the individual performance of the Chief Executive and the Finance Director as part of the annual remuneration review. Similarly, the performance of the Chairman was considered by the non-executive directors during the annual review of his remuneration, and the Chairman and the Chief Executive reviewed the performance of the non-executive directors. No significant issues were identified but minor areas for improvement are being addressed.

The Company maintains directors and officers liability insurance in respect of legal action against its directors.

Meetings attendance

The following table shows the attendance of directors, who served during the year, at meetings of the Board, the Audit Committee, the Nomination Committee and the Remuneration Committee:

	Board (11 meetings)	Audit Committee (4 meetings)	Nomination Committee (0 meetings)	Remuneration Committee (6 meetings)
K C Scobie	11(11)	-	-	6(6)
D R Evans	11(11)	-	-	-
The Rt Hon Lord Freeman	11(11)	4(4)	-	6(6)
I F R Much	10(11)	4(4)	-	6(6)
Air Marshal Sir Peter Norriss	11(11)	4(4)	-	6(6)
D J Price	11(11)	-	-	-
P A Rayner	11(11)	-	-	-

The maximum number of meetings which each director could have attended is shown in brackets.

Board Committees

The terms of reference of the Audit Committee, the Nomination Committee and the Remuneration Committee are posted on the Company's website and are available on request from the Company Secretary.

Audit Committee

The Rt Hon Lord Freeman, Mr Much and Air Marshal Sir Peter Norriss all served as members of the Audit Committee during the year. The Rt Hon Lord Freeman is Chairman of the Committee. The Committee met four times during the year and operates within formal written terms of reference. As referred to above, the terms of reference are available on the Company's website. Meetings of the Committee are attended, at the invitation of the Committee, by the external auditors, the Chairman, the Finance Director and representatives from the Group finance and internal audit function. The Committee meets with the auditors on a regular basis without executive directors present. The Company Secretary acts as secretary to the Committee and minutes of meetings are circulated to all Board members.

The Committee is authorised to seek any information it requires from any employee of the Company in order to perform its duties, and to obtain any outside legal or other professional advice it requires at the Company's expense.

The Committee monitors the integrity of the Group's financial statements and the effectiveness of the external audit process. It is responsible for ensuring that an appropriate relationship between the Group and the external auditors is maintained, including reviewing non-audit services and fees. The Committee keeps under review the effectiveness of the Group's internal controls and financial risk management systems, and on an annual basis, considers the effectiveness of the Group's internal audit function. The Committee reviews annually its terms of reference and its effectiveness, and recommends to the Board any changes required as the result of such review.

During the year, the Committee, operating under its terms of reference, discharged its responsibilities by:

- reviewing the Group's draft 2007 financial statements and 2008 interim results statement prior to Board approval and reviewing the external auditors' detailed reports thereon;
- reviewing the appropriateness of the Group's accounting policies, and reviewing various accounting matters raised by management and the external auditors in the context of financial disclosures;
- considering and approving changes to the Group's accounting policy manual;
- reviewing the potential impact in the Group's financial statements of certain matters such as impairments of fixed asset values and International Financial Reporting Standards;
- reviewing the external auditors' plan for the 2007 and 2008 financial statements and the 2008 interim report, including key risks on the accounts, confirmation of auditor independence and the proposed audit fee, and approving the terms of engagement for the audit;
- considering the Group's transfer pricing policy and certain other tax-related matters;
- receiving reports from the Risk Committee and reviewing the Group's risk register;
- approving a revised whistleblowing policy and procedures for employees; and
- reviewing the work undertaken by the Group's internal audit function.

The Company appointed an Internal Auditor in 2007. The initial internal audit programme focused on a review of financial controls across the Group. These activities have now been widened to include an audit of certain non-financial controls and procedures. The Committee reviews the internal audit plan and receives regular reports from the Internal Auditor.

The Board has accepted the Committee's recommendation that Deloitte LLP be proposed for re-appointment as auditors at the forthcoming Annual General Meeting.

The Committee keeps under review the level of non-audit services which are provided by the external auditors, to ensure that this does not impair their independence and objectivity. The Committee, in conjunction with the Finance Director, also ensures that the Group maintains a sufficient choice of appropriately qualified audit firms. During the year, work on corporate finance matters was sourced from the external auditors only where there was no direct conflict with their role as external auditors and where there were clear efficiencies and value added benefits for the Company. The Committee has now adopted a policy which states that the external auditors should no longer be appointed to provide services in relation to corporate finance matters, unless the Committee agrees that their appointment would be in the best interests of the Company's shareholders in particular circumstances. Details of the amounts paid to the external auditors during the year for audit and other services are set out in the notes to the financial statements on page 66.

Nomination Committee

Mr Scobie, Mr Much and Air Marshal Sir Peter Norriss all served on the Nomination Committee during the year. Mr Scobie is Chairman of the Committee but, in accordance with the Committee's terms of reference, is not permitted to chair meetings when the Committee is dealing with the appointment of his successor. As referred to above, the Committee's terms of reference are available on the Company's website.

With regards to the recruitment and appointment of new directors to the Board, the Committee considers the specific knowledge and expertise which would be of benefit to the Group's current operations and future strategy, and provides a brief to external search agents based upon its conclusions. The search agents put forward a short list of candidates for the Committee to interview before making its recommendations to the Board. The Board interviews preferred candidates prior to making any formal offers of appointment.

Remuneration Committee

The Rt Hon Lord Freeman, Mr Much, Air Marshal Sir Peter Norriss and Mr Scobie all served on the Remuneration Committee during the year. Mr Much is Chairman of the Committee. The Committee met six times during the year. Further details on the Committee and the Company's policy on directors' remuneration are included within the Directors' Remuneration Report.

Executive Committee

The Chief Executive, Dr Price, chairs the Executive Committee, which meets monthly. The other members are the Finance Director, the Company Secretary, the Business Development Director, the Group Director of Safety, the Managing Director of the European Energetics Division and the President of the Group's US operations. The Executive Committee is responsible for the executive day-to-day running of the Company, submission to the Board of strategic plans and budgets for the Group's operations, and monitoring the day-to-day performance of the Group as a whole.

Relations with shareholders

The Company maintains an active dialogue with institutional shareholders through regular briefing meetings and formal presentations following the release of interim and annual results. Meetings are usually attended by the Chairman, the Chief Executive and the Finance Director. However, the non-executive directors are offered the opportunity to meet with major shareholders and attend meetings if so requested by major shareholders. No such requests were received during the year. Communication with private investors is achieved largely through the medium of the interim report and the financial statements.

Statement on Corporate Governance

CONTINUED

The Company's website (www.chemring.co.uk) provides financial and business information on the Group.

The directors are provided with reports and other written briefings from the Company's principal shareholders and analysts, and are regularly informed by the Company Secretary about changes to significant shareholdings.

It is the Company's policy that all directors should attend and make themselves available to take questions from shareholders or address any concerns at the Annual General Meeting. At other times of the year, the directors can be contacted via the Company's head office.

All substantial issues, including the adoption of the annual report and financial statements, are proposed on separate resolutions at the Annual General Meeting. The number of proxy votes received for and against each resolution, together with the number of abstentions, are indicated after votes have been dealt with on a show of hands. The Notice of the Annual General Meeting is sent to shareholders at least twenty working days before the meeting.

Financial reporting

The Statement of Directors' Responsibilities in respect of the financial statements and accounting records maintained by the Company is set out on page 36.

Internal control and risk management

The Board has continued to review the effectiveness of the Group's systems of internal control, including financial, operational and compliance controls, and risk management systems.

The Board acknowledges its responsibility for the Group's systems of internal control and attaches considerable importance to these systems, which are designed to meet the Group's particular needs and identify those risks to which it is exposed. However, the systems can only provide reasonable, not absolute, assurance against material misstatement, loss or mismanagement of the Group's assets.

In carrying out its review of the effectiveness of the Group's systems of internal control in compliance with provision C2.1 of the Combined Code, the Board has taken into consideration the following key features of the Group's risk management systems and control procedures which operated during the year:

- The Board assesses the key risks associated with achievement of the Group's business objectives as part of the annual strategic planning process. Out of this process, each business establishes a five year plan and annual budget, which are subject to approval by the Board. The performance of each business against budget and prior years is reviewed on a monthly basis at both operational level and by the Board. Achievement of strategic business objectives and the associated risks are monitored by the Board on an ongoing basis.
- All businesses hold monthly operating meetings, which are attended by at least one main Board director, either in person or, in the case of the overseas companies, by video conference. In the case of the US businesses, formal Board meetings are held quarterly and these are attended by main Board directors and external non-executive directors appointed in the US. The US non-executive directors are available to provide guidance and monitor governance in the US businesses throughout the year. External non-executive directors have also been appointed to the Board of the Group's Italian subsidiary, Simmel Difesa S.p.A.
- Each business is required to comply with the Group's accounting policy manual, which sets out formal procedures for incurring certain types of expenditure and making contractual commitments. Compliance with the accounting policy manual is audited by the Internal Auditor, who reports regularly to the Audit Committee on his findings.
- The Board retains primary responsibility for acquisitions and disposals, and financing arrangements for the Group. Treasury management, IT strategy, insurance and significant legal matters are dealt with centrally from the Group head office, and the Board receives regular reports on each of these items. Reviews of the Group's pensions, insurance and risk management arrangements are carried out by external advisors on a regular basis.
- The Group Director of Safety, supported by two divisional Health and Safety Management Committees, co-ordinates and controls the activities of each business in relation to health and safety and environmental matters, which are a key focus for the Board in view of the nature of the Group's operations. The Chief Executive is the Board member nominated with specific responsibility for health and safety. The Chief Executive meets formally with health and safety professionals from each business on an annual basis.
- The Group committed to adherence with the European Aerospace and Defence Association's Common Industry Standards on Anti-Corruption in the year, and is now reviewing all its business policies and procedures to ensure compliance.

The Group's Risk Management Committee meets on a quarterly basis. The Chief Executive, the Finance Director, the Company Secretary, the Business Development Director, the Director of Safety, the Managing Director of the Energetics Division and the President of the Group's US operations serve on the Committee. The Committee reviews the key risks associated with the achievement of the annual budget and the five year plan for each business, and the risk control procedures implemented. It also considers the top five health and safety risks which have been identified at each site and agrees the action plan to address these. The Risk Management Committee reports biannually to the Audit Committee and the Board on the top ten risks from a Group perspective, and monitors the actions being taken to mitigate these.

The Board confirms that it has reviewed the effectiveness of the Group's systems of internal control and risk management which were in place during the financial year ended 31 October 2008, and it confirms that systems of internal control and risk management compliant with the Combined Code and the Turnbull Guidance were in place throughout the year and have remained in place up to the date of approval of these financial statements. Notwithstanding this, the Board will continue to take steps to embed internal control and risk management further into the operations of the Group and to deal with any areas of improvement which come to the attention of management and the Board.

Compliance with the provisions of the Combined Code

Throughout the year ended 31 October 2008, the Company has been in compliance with the code provisions set out in Section 1 of the Combined Code on Corporate Governance issued by the Financial Reporting Council in 2006, with the exception that the Board has not nominated a non-executive director as the senior independent director (provision A.3.3), as it does not consider this to be appropriate at the present time in view of the size of the Board. This requirement will be kept under review.

Procedures to deal with directors' conflicts of interest

With effect from 1 October 2008, all directors have a duty under the Companies Act 2006 (the '2006 Act') to avoid a situation in which he or she has or can have a direct or indirect interest that conflicts or possibly may conflict with the interests of the Company. The Company has procedures in place to deal with situations where directors may have conflicts of interest. The Company will be seeking shareholder approval at the forthcoming Annual General Meeting to amend its Articles of Association to include updated provisions for dealing with directors' conflicts of interest in accordance with the 2006 Act. In accordance with these amended provisions, the members of the Board will endeavour to:

- consider each conflict situation separately on its particular facts;
- consider the conflict situation in conjunction with the rest of their duties under the 2006 Act;
- keep records and Board minutes as to authorisations granted by directors and the scope of any approvals given; and
- regularly review conflict authorisation.

Going concern

The directors have acknowledged the latest guidance on going concern. They have made appropriate enquiries and taken into account factors such as:

- the strong order book of £409 million as at the year end;
- the Group's operating cash flow of £83.7 million during the year;
- the strong balance sheet at the year end of £230.6 million; and
- the Group's available banking facilities, which amount to £107.1 million with maturities through to March 2012 (see Note 21).

The Group's banking covenants have all been met with a comfortable margin during the past year and the expectation is that this will continue. Details of how the Group manages its liquidity risk can be found in Note 24 of the financial statements.

Whilst the current volatility in financial markets has created general uncertainty in respect of the current economic outlook, the long term nature of the Group's business, taken together with the Group's forward order book, provide a satisfactory level of confidence to the Board in respect of trading in the year ahead.

The directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Approved by the Board of Directors on 20 January 2009

S L Ellard
COMPANY SECRETARY

Independent Auditors' Report to the Members of Chemring Group PLC

FOR THE YEAR ENDED 31 OCTOBER 2008

We have audited the Group financial statements of Chemring Group PLC for the year ended 31 October 2008 which comprise the Consolidated Income Statement, the Consolidated Statement of Recognised Income and Expense, the Consolidated Balance Sheet, the Consolidated Cash Flow Statement, the Notes to the Cash Flow Statement and the related Notes 1 to 39. These Group financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

We have reported separately on the individual company financial statements of Chemring Group PLC for the year ended 31 October 2008.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an Auditors' Report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report, the Directors' Remuneration Report and the Group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities in the Directors' Report.

Our responsibility is to audit the Group financial statements and the part of the Directors' Remuneration Report described as having been audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the Group financial statements give a true and fair view, whether the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation and whether the part of the Directors' Remuneration Report described as having been audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the Group financial statements. The information given in the Directors' Report includes that specific information presented in the Statement by the Chairman, the Review by the Chief Executive and the Review by the Finance Director that is cross referred from the review of the year and results section of the Directors' Report.

In addition, we report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We review whether the Statement on Corporate Governance reflects the Company's compliance with the nine provisions of the 2006 Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statement on internal control covers all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the annual report as described in the contents section including the unaudited part of the Directors' Remuneration Report and consider whether it is consistent with the audited Group financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Group financial statements. Our responsibilities do not extend to any further information outside the annual report.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Group financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the Group financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Group financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Group financial statements and the part of the Directors' Remuneration Report to be audited.

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 October 2008 and of its profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation;
- the part of the Directors' Remuneration Report described as having been audited has been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the Group financial statements.

Deloitte LLP
Chartered Accountants and Registered Auditors
Southampton, United Kingdom
20 January 2009

Consolidated Income Statement

FOR THE YEAR ENDED 31 OCTOBER 2008

	Note	2008 £m	2007 £m
Continuing operations			
Revenue			
- continuing		334.6	254.7
- acquired		19.6	–
Total revenue	4	354.2	254.7
Operating profit			
- continuing		65.2	57.8
- acquired		3.2	–
Total operating profit	5,6	68.4	57.8
Operating profit is analysed as:			
Underlying operating profit*		84.9	61.2
Goodwill adjustment arising from recognition of tax losses		(1.8)	–
Intangible amortisation arising from business combinations		(6.0)	(3.4)
Loss on fair value movements on derivatives		(8.7)	–
		68.4	57.8
Share of post-tax results of associate		0.1	0.1
Finance income	8	1.8	0.6
Finance expense	9	(12.6)	(8.7)
Profit before tax for the year from continuing operations		57.7	49.8
Profit before tax is analysed as:			
Underlying profit before tax*		74.2	53.2
Goodwill adjustment arising from recognition of tax losses		(1.8)	–
Intangible amortisation arising from business combinations		(6.0)	(3.4)
Loss on fair value movements on derivatives		(8.7)	–
		57.7	49.8
Tax	10	(16.5)	(15.9)
Profit after tax for the year from continuing operations		41.2	33.9
Discontinued operations			
Loss after tax from discontinued operations	34	–	(1.9)
Profit after tax for the year	28	41.2	32.0
Attributable to: Equity holders of the parent		41.2	32.1
Minority interest		–	(0.1)
Earnings per ordinary share			
From continuing operations:	12		
Underlying*		160p	112p
Basic		123p	105p
Diluted		123p	104p
From continuing and discontinued operations:	12		
Basic		123p	99p
Diluted		123p	98p

*Before goodwill adjustment arising from recognition of tax losses, intangible amortisation arising from business combinations and loss on fair value movements on derivatives

Consolidated Statement of Recognised Income and Expense

FOR THE YEAR ENDED 31 OCTOBER 2008

	Note	2008 £m	2007 £m
Profit after tax for the year		41.2	32.0
Other recognised income and expense			
(Losses)/gains on derivatives		(3.8)	0.2
Movement on deferred tax relating to cash flow hedges		0.8	(0.1)
Exchange differences on translation of foreign operations		24.8	(7.0)
Actuarial (losses)/gains on defined benefit pension schemes	35	(0.1)	4.4
Movement on deferred tax relating to pension schemes		–	(1.5)
Current tax on items taken directly to equity		(0.6)	2.0
Deferred tax on items taken directly to equity		(4.2)	1.1
Total recognised income and expense for the year	29	58.1	31.1
Attributable to:			
Equity holders of the parent		58.1	31.2
Minority interest		–	(0.1)

Consolidated Balance Sheet

AS AT 31 OCTOBER 2008

	Note	£m	2008 £m	£m	2007 £m
Non-current assets					
Goodwill	13	128.8		94.8	
Other intangible assets	14	85.0		37.1	
Property, plant and equipment	15	110.4		69.8	
Interest in associate	17	1.0		1.0	
Deferred tax	26	9.7		9.1	
			334.9		211.8
Current assets					
Inventories	18	89.1		51.2	
Trade and other receivables	19	87.8		61.9	
Cash and cash equivalents	20,24	69.6		38.7	
Derivative financial instruments	24	–		0.9	
			246.5		152.7
Total assets			581.4		364.5
Current liabilities					
Bank loans and overdrafts	21	(19.7)		(22.5)	
Obligations under finance leases	22	(0.7)		(0.7)	
Trade and other payables	23	(108.5)		(71.4)	
Provisions	25	(1.5)		(0.4)	
Current tax liabilities		(6.3)		(3.3)	
Derivative financial instruments	24	(8.1)		–	
			(144.8)		(98.3)
Non-current liabilities					
Bank loans	21	(163.6)		(113.5)	
Obligations under finance leases	22	(2.2)		(1.5)	
Trade and other payables	23	(1.8)		(0.4)	
Long term provisions	25	(4.4)		(1.3)	
Deferred tax	26	(17.3)		(12.1)	
Preference shares	27	(0.1)		(0.1)	
Retirement benefit obligations	35	(13.6)		(13.3)	
Derivative financial instruments	24	(3.0)		–	
			(206.0)		(142.2)
Total liabilities			(350.8)		(240.5)
Net assets			230.6		124.0
Equity					
Share capital	27		1.8		1.6
Share premium account	28		119.8		60.5
Special capital reserve	28		12.9		12.9
Hedging reserve	28		(2.6)		0.4
Revaluation reserve	28		1.5		1.6
Retained earnings	28		102.9		49.8
			236.3		126.8
Own shares	30		(5.7)		(2.8)
Equity attributable to equity holders of the parent			230.6		124.0
Total equity			230.6		124.0

These financial statements were approved by the Board of Directors on 20 January 2009.

Signed on behalf of the Board

D J Price

P A Rayner

Consolidated Cash Flow Statement

FOR THE YEAR ENDED 31 OCTOBER 2008

	Note	2008 £m	2007 £m
Cash flows from operating activities			
Cash generated from operations	A	83.7	60.6
Tax paid		(13.4)	(12.0)
Net cash inflow from operating activities		70.3	48.6
Cash flows from investing activities			
Dividends received from associate		0.1	0.1
Purchases of property, plant and equipment		(31.0)	(14.6)
Purchases of intangible assets		(3.2)	(1.4)
Proceeds on disposal of subsidiary undertaking/division		–	3.2
Proceeds on disposal of property, plant and equipment		–	0.2
Acquisition of subsidiary undertakings (net of cash acquired)	33	(68.2)	(46.9)
Net cash outflow from investing activities		(102.3)	(59.4)
Cash flows from financing activities			
Dividends paid		(9.3)	(6.0)
Interest paid		(8.2)	(7.4)
Proceeds on issue of shares		58.6	0.1
New borrowings		72.7	50.7
Repayments of borrowings		(36.4)	(6.4)
Proceeds from/(repayments of) obligations under finance leases		0.4	(0.7)
Purchase of own shares		(2.9)	(2.8)
Net cash inflow from financing activities		74.9	27.5
Increase in cash and cash equivalents during the year		42.9	16.7
Cash and cash equivalents at start of the year		25.4	9.0
Effect of foreign exchange rate changes		1.3	(0.3)
Cash and cash equivalents at end of the year		69.6	25.4

Notes to the Consolidated Cash Flow Statement

FOR THE YEAR ENDED 31 OCTOBER 2008

A. Cash generated from operations	2008 £m	2007 £m			
Operating profit from continuing operations	65.2	57.8			
Operating profit from acquired operations	3.2	–			
Loss on discontinued operations	–	(1.9)			
Adjustment for:					
Depreciation of property, plant and equipment	9.7	6.8			
Amortisation of intangible assets arising from business combinations	6.0	3.4			
Amortisation of other intangibles	0.7	0.6			
Loss on fair value movements on derivatives	8.7	–			
Goodwill adjustment arising from recognition of tax losses	1.8	–			
Share-based payment expense	1.7	2.4			
Negative goodwill included in operating profit	–	(0.4)			
Difference between pension contributions paid and amount recognised in Income Statement	0.1	(0.6)			
Decrease in provisions	(2.2)	(0.5)			
Operating cash flows before movements in working capital	94.9	67.6			
Increase in inventories	(18.8)	(4.6)			
Increase in trade and other receivables	(14.1)	(9.0)			
Increase in trade and other payables	21.7	6.6			
Cash generated from operations	83.7	60.6			
Reconciliation of net cash flow to movement in net debt					
Increase in cash and cash equivalents during the year	42.9	16.7			
Cash inflow from increase in debt and lease financing	(36.7)	(43.6)			
Change in net debt resulting from cash flows	6.2	(26.9)			
New finance leases	0.8	(2.1)			
Translation difference relating to loans	(23.6)	0.4			
Amortisation of debt finance costs	(0.5)	(0.4)			
Movement in net debt in the year	(17.1)	(29.0)			
Net debt at start of the year	(99.6)	(70.6)			
Net debt at end of the year	(116.7)	(99.6)			
Analysis of net debt					
	As at 1 Nov 2007 £m	Cash flow £m	Non-cash changes £m	Exchange movement £m	As at 31 Oct 2008 £m
Cash at bank and in hand	38.7	29.6	–	1.3	69.6
Overdrafts	(13.3)	13.3	–	–	–
	25.4	42.9	–	1.3	69.6
Debt due within one year	(9.2)	10.4	(18.0)	(2.9)	(19.7)
Debt due after one year	(113.5)	(46.8)	18.0	(21.3)	(163.6)
Finance leases	(2.2)	(0.3)	0.3	(0.7)	(2.9)
Preference shares	(0.1)	–	–	–	(0.1)
	(99.6)	6.2	0.3	(23.6)	(116.7)

Notes to the Group Financial Statements

1. General information

Chemring Group PLC is a company incorporated in England and Wales under registration number 86662. The address of the registered office is Chemring House, 1500 Parkway, Whiteley, Fareham, Hampshire PO15 7AF. The nature of the Group's operations and its principal activities are set out in Note 5 and in the Directors' Report on pages 34 to 37. These financial statements are the consolidated financial statements of Chemring Group PLC and its subsidiaries ("the Group").

These financial statements are presented in pounds sterling. Foreign operations are included in accordance with the policy set out in Note 3 of the financial statements.

2. Adoption of new and revised standards

In the year under review two Interpretations issued by the International Financial Reporting Interpretations Committee were effective. These were IFRIC11 *IFRS2 Group and Treasury Share Transactions* and IFRIC14/IAS19 *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*. The adoption of these Interpretations has not led to any changes in the Group's accounting policies.

At the date of authorisation of these financial statements the following Standards and Interpretations, which have not been applied in these financial statements, were in issue but not yet effective:

- IFRS1 (amended)/IAS27 (amended) *Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate*
- IFRS2 (amended) *Share-based Payment - Vesting Conditions and Cancellations*
- IFRS3 (revised 2008) *Business Combinations*
- IFRS8 *Operating Segments* (effective from 1 January 2009)
- IAS1 (revised 2007) *Presentation of Financial Statements* (effective 1 January 2009)
- IAS23 *Borrowing Costs* (effective 1 January 2009)
- IAS27 (revised 2008) *Consolidated and Separate Financial Statements*
- IAS32 (amended)/IAS1 (amended) *Puttable Financial Instruments and Obligations Arising on Liquidation*
- IFRIC12 *Service Concession Arrangements*
- IFRIC15 *Agreements for the Construction of Real Estate*
- IFRIC16 *Hedges of a Net Investment in a Foreign Operation*

The directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material impact on the financial statements of the Group.

3. Accounting policies

Basis of preparation

These financial statements have been prepared in accordance with IFRS adopted for use in the European Union. These will be those IAS, IFRS and related Interpretations (Standing Interpretations Committee (SIC)/International Financial Reporting Interpretations Committee (IFRIC) interpretations), subsequent amendments to those standards and related interpretations, future standards and related interpretations issued or adopted by the International Accounting Standards Board (IASB) that have been endorsed by the European Commission (collectively referred to as IFRS). These are subject to ongoing review and endorsement by the European Commission or possible amendment by interpretive guidance from the IASB and the IFRIC and are therefore still subject to change.

Basis of accounting

The financial statements have been prepared in accordance with IFRS adopted by the European Union and therefore the Group financial statements comply with Article 4 of the EU IAS Regulation. The particular accounting policies adopted have been applied consistently throughout the current and previous year and are described below.

Accounting convention

The financial statements are prepared under the historical cost convention, except for the revaluation of certain properties and financial instruments.

Basis of consolidation

The Group financial statements consolidate those of the Company and all of its subsidiaries. A subsidiary undertaking is an entity over which the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The results of subsidiaries acquired are consolidated from the date on which control passes to the Group and the results of disposed subsidiaries are consolidated up to the date on which control passes from the Group.

All companies within the Group make up their financial statements to the same date. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

3. Accounting policies continued

Operating profit

Operating profit is stated before the share of results of associates and before finance expense. Operating profit excludes the results of discontinued operations.

Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for deliveries made, work completed or services rendered during the year, net of discounts, VAT and other revenue related taxes. Revenue is recognised when title passes, or when the right to consideration, in exchange for performance, has been completed. For bill and hold arrangements revenue is recognised when the risks and rewards are transferred to the customer, typically on formal acceptance. An appropriate proportion of total long term contract value, based on the fair value of work performed, is included in revenue and an appropriate level of profit is taken based on the percentage completion method when the final outcome can be reliably assessed. Provision is made in full for foreseeable losses as soon as they are identified.

Investment income

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

Acquisitions

On acquisition of a subsidiary, the cost is measured as the fair value of the consideration given plus any directly attributable costs. The assets, liabilities and contingent liabilities of a subsidiary that meet the IFRS3 *Business Combinations* recognition criteria are measured at the fair value at the date of acquisition. Where cost exceeds fair value of the net assets acquired the difference is recorded as goodwill.

Where the fair value of the net assets exceeds the cost, the difference is recorded directly in the income statement. The accounting policies of subsidiaries are changed where necessary to be consistent with those of the Group.

Intangible assets

Goodwill

The purchased goodwill of the Group is regarded as having an indefinite useful economic life and, in accordance with IAS36 *Impairment of Assets*, is not amortised but is subject to annual tests for impairment. In reviewing the carrying value of goodwill of the various businesses the Board has considered the separate plans and cash flows of these businesses consistent with the requirements of IAS36 and is satisfied that these demonstrate that no impairment has occurred in respect of continuing operations. Goodwill arising on acquisition before the date of transition to IFRS has been retained at the previous UK GAAP amounts subject to being tested for impairment at that date. On disposal of a subsidiary, associate or jointly controlled entity, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

For acquisitions after 1 November 2004 the Group recognises separately from goodwill intangible assets that are separable or arise from contractual or other legal rights and whose fair value can be measured reliably. These intangible assets are amortised on a straight-line basis over their useful economic lives, averaging ten years.

Other intangibles

Research and development expenditure

Expenditure on research activities is recognised as an expense in the period in which it is incurred. Development expenditure, where it meets certain criteria given below, is capitalised on a straight-line basis over typically three years from the date commercial production commences. Development costs not meeting the criteria for capitalisation are expensed as incurred.

An intangible development asset is recognised only if all of the following conditions are met:

- the development costs are separately identifiable;
- the development costs can be measured reliably;
- management are satisfied as to the ultimate technical and commercial viability of the project; and
- it is probable that the asset will generate future economic benefits.

Patents and trademarks

Patents and trademarks are measured initially at purchase cost and are amortised on a straight-line basis over their estimated useful lives.

Notes to the Group Financial Statements

3. Accounting policies continued

Property, plant and equipment

Other than revalued land and buildings, property, plant and equipment are held at cost less accumulated depreciation and any recognised impairment loss. No depreciation is provided on freehold land. On other assets depreciation is provided at rates calculated to write down their cost or valuation to their estimated residual values by equal instalments over their estimated useful economic lives, which are considered to be:

Freehold buildings	- up to 50 years
Leasehold buildings	- the period of the lease
Plant and equipment	- 10 years

Impairment of non-current assets

Assets that have indefinite lives are tested for impairment annually. Assets that are subject to depreciation or amortisation are reviewed for impairment whenever changes in circumstances indicate that the carrying value may not be recoverable. To the extent that the carrying value exceeds the recoverable amount an impairment loss is recorded for the difference as an expense in the income statement. The recoverable amount used for impairment testing is the higher of the value in use and its fair value less costs of disposal. For the purpose of impairment testing assets are grouped at the lowest levels for which there are separately identifiable cash flows.

Inventories

Inventories are recorded at the lower of cost and net realisable value. Cost represents materials, direct labour, other direct costs and related production overheads and is determined using the first-in first-out (FIFO) method. Net realisable value is based on estimated selling price, less further costs expected to be incurred to completion and disposal.

Provision is made for slow moving, obsolete and defective items where appropriate.

Tax

The tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the Income Statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items of income that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable taxable profits will be available in the future against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the Income Statement, except where it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Special capital reserve

The special capital reserve was created as part of a capital reduction scheme involving the cancellation of the share premium account which was approved by the Court in 1986 and is in accordance with the requirements of the Companies Act 1985.

3. Accounting policies continued

Foreign currencies

The individual financial statements of each Group company are presented in the currency of the primary economic environment in which it operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each Group company are expressed in pounds sterling, which is the functional currency of the Company, and the presentation currency for the consolidated financial statements.

In preparing the financial statements of the individual companies, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are re-translated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not re-translated.

Exchange differences arising on the settlement of monetary items, and on the re-translation of monetary items, are included in the profit or loss for the period.

In order to hedge its exposure to certain foreign exchange risks, the Group enters into forward contracts and forward currency structures which are accounted for as derivative financial instruments (see below for details of the Group's accounting policies in respect of such derivative financial instruments).

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period.

Financial instruments

Financial assets and liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

Financial assets

Trade receivables

Trade receivables do not carry any interest and are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits, and other short term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

Financial liabilities and equity instruments

Financial liabilities

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

Bank borrowings

Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs. Finance charges including premiums payable on settlement or redemption, and direct issue costs are accounted for on an accruals basis to the Income Statement using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

Trade payables

Trade payables are not interest bearing and are stated at their nominal value.

Notes to the Group Financial Statements

3. Accounting policies continued

Derivative financial instruments

The Group's activities expose it primarily to the financial risks of interest rate and foreign currency transactions, and it uses derivative financial instruments to hedge its exposure to these transactional risks. The Group uses interest rate swap contracts, foreign exchange forward contracts and other forward currency structures to reduce these exposures and does not use derivative financial instruments for speculative purposes.

Derivative financial instruments are recognised at fair value at the date the derivative contract is entered into and are revalued at fair value at each balance sheet date. The method by which any gain or loss is recognised depends on whether the instrument is designated a hedging instrument or not. To be designated as a hedging instrument the instrument must be documented as such at inception and must be assessed at inception and on an ongoing basis to be highly effective in offsetting changes in fair values or cash flows of hedged items.

Hedge accounting principles are used for foreign currency forward contracts (net investment hedge) and interest rate swaps (cash flow hedge) where movements in fair value are held in equity until such time as the underlying amounts of the contract mature. At maturity or disposal of the net investment the amounts held in equity will be recycled to the Income Statement. Changes in fair value of any ineffective portion of net investment hedges and interest rate swaps are recognised in the Income Statement immediately. The fair values of derivative financial instruments are calculated by independent third party valuers.

Where derivatives do not meet the criteria for hedge accounting the changes in fair value are immediately recognised in the Income Statement.

Embedded derivatives that are not closely related to the host contract are treated as separate derivatives, with unrealised gains and losses reported in the Income Statement.

Retirement benefit costs

Payments to defined contribution retirement benefit schemes are charged as an expense as they fall due. For defined benefit schemes, the cost of providing benefits is determined using the projected unit credit method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised outside of the profit or loss and presented in the Statement of Recognised Income and Expense (SORIE).

Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the benefits become vested.

The retirement benefit obligation recognised in the Balance Sheet represents the present value of the defined benefit obligation as adjusted for unrecognised past service cost, and as reduced by the fair value of scheme assets. Any asset resulting from this calculation is limited to past service cost, plus the present value of available refunds and reductions in future contributions to the scheme.

Leased assets

Where the Group enters into a lease which entails taking substantially all the risks and rewards of ownership of an asset, the lease is treated as a finance lease. The asset is recorded in the Balance Sheet as property, plant and equipment and is depreciated over the shorter of the estimated useful economic life and the lease term. Future instalments under such leases, net of finance charges, are included in creditors. The finance element of the instalments is charged to the Income Statement at a constant rate of charge on the remaining balance of the obligation.

All other leases are operating leases and the rental charges are taken to the Income Statement on a straight-line basis over the life of the lease.

Share-based compensation

The Group operates equity settled and cash settled share-based compensation schemes.

For grants made under the Group's share-based compensation schemes, the fair value is calculated at the grant date with changes in the fair value recognised in the Income Statement on a straight-line basis over the vesting period, based on the Group's estimate of the shares that will eventually vest. The valuation of the options utilises a methodology based on the Black-Scholes model.

For equity settled share-based grants, the total amount recognised is based on the fair value of the equity instrument measured at the date the award is made. At each balance sheet date the impact of any revision to vesting estimates is recognised in the income statement over the vesting period. Proceeds received, net of any directly attributable transaction costs, are credited to share capital and share premium.

3. Accounting policies continued

For cash settled share-based grants, the total amount recognised is based on the fair value of the liability incurred. The fair value of the liability is re-measured at each balance sheet date with changes in the fair value recognised in the Income Statement for the period.

Post balance sheet events

Following IAS10 *Events after the Balance Sheet Date*, the Group continues to disclose events that it considers material and non-disclosure of which can influence the economic decisions of users of the financial statements.

Critical accounting judgements and key sources of estimation uncertainty

When applying the Group's accounting policies, management must make assumptions and estimates concerning the future that affect the carrying amounts of assets and liabilities at the balance sheet date and the amounts of revenue and expenses recognised during the accounting period. Such assumptions and estimates are based upon factors such as historical experience, the observance of trends in the industries in which the Group operates, and information available from the Group's customers and other outside sources.

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year include:

Goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the entity to determine such assets, to estimate the future cash flows expected to arise from the cash-generating unit and to determine a suitable discount rate in order to calculate present value.

Intangible assets acquired in business combinations

Under IFRS3 *Business Combinations*, it is necessary to separately identify and value any acquired intangible assets. In order to ascertain the values of the separate assets it is necessary for management to estimate the future cash flows attributable to the asset and estimate their useful economic lives.

Pensions

The liability recognised in relation to retirement benefit obligations is dependent on a number of assumptions, including discount rate, mortality rate, salary increases and inflation. Any change in these assumptions would change the amount recognised (see Note 35).

4. Revenue

All of the Group's revenue is derived from the sale of goods. The following table provides an analysis of the Group's revenue by destination.

Revenue by destination	Continuing operations 2008 £m	Acquisitions 2008 £m	Total 2008 £m	Total 2007 £m
UK	85.8	0.6	86.4	60.7
USA	130.7	11.4	142.1	109.4
Europe	63.1	3.4	66.5	37.5
Middle and Far East	39.3	2.7	42.0	34.9
Australia	10.8	1.4	12.2	8.4
Rest of the world	4.9	0.1	5.0	3.8
	334.6	19.6	354.2	254.7

In addition to the revenues shown above there was finance income of £1.8 million (2007: £0.6 million) from continuing operations. There was no discontinued revenue in 2008 (2007: £3.8 million). Full disclosure is given in Note 34. Total revenue including finance income was £356.0 million (2007: £255.3 million).

Notes to the Group Financial Statements

5. Business and geographical segments

For management purposes the Group has two operating divisions - Energetics and Countermeasures. These divisions are the basis on which it reports its primary segment information.

Principal activities are as follows:

Energetics: Pyrotechnics, battlefield simulation products, flares, cartridge/propellant actuated devices, explosive ordnance disposal equipment, propellants, munitions

Countermeasures: Expendable countermeasures

A segmental analysis of revenue and operating profit is set out below:

Business segments

	2008 £m	2007 £m
Revenue		
Energetics	196.7	128.2
Countermeasures	157.5	126.5
Total revenue from third parties	354.2	254.7
Analysis of operating profit	2008 £m	2007 £m
Energetics	45.7	27.9
Countermeasures	45.5	38.6
Charge for share-based payments	(1.7)	(2.4)
Unallocated head office costs	(4.6)	(2.9)
Total underlying operating profit*	84.9	61.2
Goodwill adjustment arising from recognition of tax losses	(1.8)	–
Intangible amortisation arising from business combinations	(6.0)	(3.4)
Loss on fair value movements on derivatives	(8.7)	–
Total operating profit	68.4	57.8

Included within the charge for share-based payments are net costs of £1.7 million (2007: £1.4 million) for equity settled share-based payments.

	2008 £m	2007 £m
Balance Sheet		
Assets		
Energetics	403.5	240.9
Countermeasures	137.2	100.0
Interest in associate	1.0	1.0
Unallocated assets	39.7	22.6
Consolidated total assets	581.4	364.5
Liabilities		
Energetics	(239.0)	(165.5)
Countermeasures	(66.0)	(61.5)
Unallocated liabilities	(45.8)	(13.5)
Consolidated total liabilities	(350.8)	(240.5)
Group net assets	230.6	124.0

*Before goodwill adjustment arising from recognition of tax losses, intangible amortisation arising from business combinations and loss on fair value movements on derivatives

5. Business and geographical segments continued

Other information	2008 £m	2007 £m
Capital additions - continuing		
Energetics	21.5	7.8
Countermeasures	12.7	8.2
Depreciation and amortisation - continuing		
Energetics	10.2	6.2
Countermeasures	6.2	4.6

Geographical segments

The Group's Energetics division operates in the UK, EU countries, Australia and the US. The Group's operations in the Countermeasures division are located in the UK, Australia and the US.

The following is an analysis of the carrying amount of net segment assets and additions to property, plant and equipment and intangible assets, analysed by the geographical area in which the assets are located. Net segment assets include continuing operations with associates and unallocated segment assets and liabilities (shown within the UK).

	2008 £m	Carrying amount of net segment assets 2007 £m	2008 £m	Additions to property, plant and equipment and intangible assets 2007 £m
UK	108.9	26.3	11.4	6.4
USA	72.8	55.4	11.3	8.3
Rest of the world	48.9	42.3	11.5	1.3
	230.6	124.0	34.2	16.0

6. Operating profit

The following table shows a reconciliation of cost by function:

	2008 £m	2007 £m
Total revenue	354.2	254.7
Cost of sales	(227.1)	(162.4)
Distribution costs	(10.3)	(3.8)
Administrative expenses*	(31.9)	(27.3)
Goodwill adjustment arising from recognition of tax losses	(1.8)	—
Intangible amortisation arising from business combinations	(6.0)	(3.4)
Loss on fair value movements on derivatives	(8.7)	—
Total administrative expenses	(48.4)	(30.7)
Total operating profit	68.4	57.8

*Before goodwill adjustment arising from recognition of tax losses, intangible amortisation arising from business combinations and loss on fair value movements on derivatives

Operating profit is stated after charging:

	2008 £m	2007 £m
Research and development costs	9.3	6.7
Depreciation		
- property, plant and equipment	9.1	6.4
- leased assets	0.6	0.4
Amortisation		
- development costs	0.7	0.6
- arising from business combinations	6.0	3.4
Operating lease rentals - plant and machinery	0.7	0.7
- other	1.1	1.1
Foreign exchange losses	9.3	0.7
Staff costs (see Note 7)	84.8	67.2
Cost of inventories recognised as an expense	140.2	87.4
Auditors' remuneration for audit services (see over)	0.4	0.3

Notes to the Group Financial Statements

6. Operating profit continued

A more detailed analysis of auditors' remuneration on a worldwide basis is provided below:

	2008 £m	2007 £m
Audit fees	0.2	0.2
Auditing accounts of subsidiary companies	0.2	0.1
	0.4	0.3
Other services:		
Tax services - compliance	0.1	0.1
Tax services - advisory	0.3	0.2
Corporate finance services	0.4	0.5
	1.2	1.1

Corporate finance services above relate to fees for acquisitions and disposals. Included in the Group audit fees is £0.1 million (2007: £0.1 million) paid in respect of the parent company.

A description of the work of the Audit Committee is set out in the Statement on Corporate Governance on pages 48 and 49 and includes an explanation of how auditor objectivity and independence is safeguarded when non-audit services are provided by the auditors.

During the year the Group incurred professional fees with other accountancy firms for the provision of corporate finance services of £0.1 million (2007: £0.2 million).

7. Staff costs

The average monthly number of employees within each category (including executive directors) was:

	2008 Number	2007 Number
Production	2,529	2,019
Administrative, sales and marketing	541	573
	3,070	2,592

The costs incurred in respect of these employees were:

	2008 £m	2007 £m
Wages and salaries	69.0	54.7
Social security costs	11.6	8.9
Other pension costs	4.2	3.6
	84.8	67.2

8. Finance income

	2008 £m	2007 £m
Interest income	1.8	0.6

9. Finance expense

	2008 £m	2007 £m
Bank overdraft and loan interest	0.2	2.2
US loan notes interest	5.1	—
Medium term loan interest	6.0	5.4
Finance lease interest	0.1	0.1
Amortisation of debt finance costs	0.5	0.4
Interest cost of retirement benefit obligations (see Note 35)	0.7	0.6
	12.6	8.7

10. Tax

	2008 £m	2007 £m
Current tax charge	(15.2)	(14.9)
Deferred tax charge	(1.3)	(1.0)
Total current year tax charge	(16.5)	(15.9)

Income tax in the UK is calculated at 28.83% (2007: 30%) of the estimated assessable profit for the year. Tax for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions.

The total charge for the year can be reconciled to the Income Statement as follows:

	2008 £m	2007 £m
Profit before tax from continuing operations	57.7	49.8
Tax at the UK corporation tax rate of 28.83% (2007: 30%)	(16.6)	(14.9)
Income/(expenses) not allowable/(deductible) for tax purposes net of tax credits	1.4	(0.1)
Utilisation of tax losses	1.1	0.3
Other	0.6	1.6
Prior year adjustments	0.4	(0.1)
Overseas profits taxed at rates different to the standard rate	(3.4)	(2.7)
Total current year tax charge	(16.5)	(15.9)

In addition to the income tax expense charged to the Income Statement, a tax debit of £4.8 million (2007: tax credit £1.5 million) has been recognised in equity in the year and is included in the Statement of Recognised Income and Expense.

Tax on discontinued operations is shown in Note 34.

11. Dividends

	2008 £m	2007 £m
Dividends on ordinary shares of 5p each		
Final dividend for the year ended 31 October 2007 17.8p (2006: 11.2p)	5.8	3.6
Interim dividend for the year ended 31 October 2008 10.0p (2007: 7.2p)	3.5	2.4
Total dividends	9.3	6.0

The proposed final dividend in respect of the year ended 31 October 2008 of 25p per share will, if approved, absorb approximately £8.8 million of shareholders' funds. The dividend is subject to approval by shareholders at the Annual General Meeting and accordingly has not been included as a liability in these financial statements.

Notes to the Group Financial Statements

12. Earnings per share

Earnings per share are based on the average number of shares in issue of 33,339,754 (2007: 32,470,410) and profit on ordinary activities after tax and minority interests of £41.2 million (2007: £33.9 million). Diluted earnings per share has been calculated using a diluted average number of shares in issue of 33,514,169 (2007: 32,678,486) and profit on ordinary activities after tax and minority interests of £41.2 million (2007: £34.0 million).

The earnings and shares used in the calculations are as follows:

From continuing operations

	2008			2007		
	Earnings £m	Ordinary shares Number 000s	EPS Pence	Earnings £m	Ordinary shares Number 000s	EPS Pence
Basic	41.2	33,340	123	33.9	32,470	105
Additional shares issuable other than at fair value in respect of options outstanding	–	174	–	0.1	208	(1)
Diluted	41.2	33,514	123	34.0	32,678	104

Reconciliation from basic earnings per share to underlying earnings per share

Underlying basic earnings has been defined as earnings before intangible amortisation arising from business combinations, goodwill adjustment arising from recognition of tax losses and loss on fair value movements on derivatives. The directors consider this measure of earnings allows a more meaningful comparison of earnings trends.

	2008			2007		
	Earnings £m	Ordinary shares Number 000s	EPS Pence	Earnings £m	Ordinary shares Number 000s	EPS Pence
Basic	41.2	33,340	123	33.9	32,470	105
Intangible amortisation arising from business combinations, goodwill adjustment and loss on fair value movements on derivatives (after tax)	12.3	–	37	2.3	–	7
Underlying	53.5	33,340	160	36.2	32,470	112

From continuing and discontinued operations

	2008			2007		
	Earnings £m	Ordinary shares Number 000s	EPS Pence	Earnings £m	Ordinary shares Number 000s	EPS Pence
Basic	41.2	33,340	123	32.1	32,470	99
Additional shares issuable other than at fair value in respect of options outstanding	–	174	–	–	208	(1)
Diluted	41.2	33,514	123	32.1	32,678	98

13. Goodwill

£m

Cost

At 1 November 2006	59.7
Recognised on acquisition of subsidiary undertakings	35.6
De-recognised on disposal of subsidiary undertakings	(0.1)
Foreign exchange adjustments	(0.4)

At 1 November 2007	94.8
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Recognised on acquisition of subsidiary undertakings	24.1
Recognition of tax assets in respect of losses	(1.8)
Foreign exchange adjustments	11.7

At 31 October 2008	128.8
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Accumulated impairment losses

At 1 November 2006, 1 November 2007 and 31 October 2008	–
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Carrying amount

At 31 October 2008	128.8
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At 31 October 2007	94.8
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Goodwill acquired in a business combination is allocated at acquisition to the cash generating units ("CGU") that are expected to benefit from that business combination. The carrying amount of goodwill has been allocated as follows:

Energetics

£m

Simmel Difesa S.p.A.	34.1
Pirotécnia Oroquieta S.L.	0.2
Goodwill arising from fair value adjustments on prior year acquisitions *	1.3

At 31 October 2007	35.6
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Richmond Electronics & Engineering Limited	7.1
Titan Dynamics Systems, Inc.	1.0
Scot, Inc.	10.4
Martin Electronics, Inc.	4.2
Goodwill arising from fair value adjustments on prior year acquisitions *	1.4

At 31 October 2008	24.1
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The Group tests goodwill annually for impairment or more frequently if there are indications that goodwill might be impaired.

The recoverable amounts of the CGU are determined from value in use calculations. The key assumptions for the value in use calculations are those regarding the discount rates, the growth rates and expected changes to selling prices and direct costs during the period for which management have detailed plans. Management estimates discount rates using pre-tax rates that reflect current market assessments of the time value of money and the risks specific to the CGU being measured (the weighted average cost of capital "WACC"). The discount rate used is 10.0% (2007: 10.0%). The growth rates are based on a prudent view of industry growth forecasts adjusted for a premium associated with the high technological nature of the businesses. A growth assumption of 2.5% (2007: 2.5%) has been used. Changes in selling price and direct costs are based on past practices and expectations of future changes in the market. The Group prepares cash flow forecasts derived from the most recent financial budgets approved by management for the next five years and extrapolates cash flows after that period based on growth as described above.

Following a detailed review, no impairment losses for continuing operations have been recognised in the year and no prior impairment losses reversed.

*In accordance with IFRS3 fair value adjustments have been made within twelve months of the acquisition dates which has resulted in additional goodwill being recognised in the year (Simmel Difesa S.p.A. and Technical Ordnance, Inc. - £1.4 million).

Notes to the Group Financial Statements

14. Other intangible assets

	Acquired intangibles £m	Other* £m	Total £m
Cost			
At 1 November 2006	24.6	2.7	27.3
Additions	–	1.4	1.4
Recognised on acquisition of subsidiary undertakings	15.5	0.7	16.2
De-recognised on disposal of subsidiary undertakings	(0.1)	–	(0.1)
Foreign exchange adjustments	(1.3)	(0.1)	(1.4)
At 1 November 2007	38.7	4.7	43.4
Additions	–	3.2	3.2
Recognised on acquisition of subsidiary undertakings**	37.6	0.3	37.9
Foreign exchange adjustments	14.2	0.8	15.0
At 31 October 2008	90.5	9.0	99.5
Amortisation			
At 1 November 2006	0.8	1.6	2.4
Charge for the year	2.9	1.1	4.0
Foreign exchange adjustments	–	(0.1)	(0.1)
At 1 November 2007	3.7	2.6	6.3
Charge for the year	6.0	0.7	6.7
Foreign exchange adjustments	1.0	0.5	1.5
At 31 October 2008	10.7	3.8	14.5
Carrying amount			
At 31 October 2008	79.8	5.2	85.0
At 31 October 2007	35.0	2.1	37.1

All of these assets are recognised at fair value to acquire and are amortised over their estimated useful lives. Fair values for acquired intangible assets are assessed by reference to future estimated cash flows discounted at an appropriate rate to present value, or by reference to the amount that would have been paid in an arm's length transaction between two knowledgeable and willing parties.

*Other intangibles comprise development costs, patents and licences.

**See Note 33.

15. Property, plant and equipment

	Land and buildings £m	Plant and equipment £m	Total £m
Cost or valuation			
At 1 November 2006	28.0	51.7	79.7
Additions	4.1	10.5	14.6
Acquired on acquisition of subsidiary undertakings	5.1	2.0	7.1
Disposals	—	(0.5)	(0.5)
Foreign exchange adjustments	—	(2.7)	(2.7)
At 1 November 2007	37.2	61.0	98.2
Additions	11.6	19.4	31.0
Acquired on acquisition of subsidiary undertakings	5.9	2.1	8.0
Disposals	—	(2.7)	(2.7)
Foreign exchange adjustments	5.6	13.2	18.8
At 31 October 2008	60.3	93.0	153.3
Accumulated depreciation			
At 1 November 2006	3.2	18.8	22.0
Charge for the year	1.2	5.6	6.8
Disposals	—	(0.3)	(0.3)
Foreign exchange adjustments	—	(0.1)	(0.1)
At 1 November 2007	4.4	24.0	28.4
Charge for the year	1.8	7.9	9.7
Disposals	—	(2.6)	(2.6)
Foreign exchange adjustments	1.0	6.4	7.4
At 31 October 2008	7.2	35.7	42.9
Carrying amount			
At 31 October 2008	53.1	57.3	110.4
At 31 October 2007	32.8	37.0	69.8

The carrying amount of the Group's plant and equipment includes an amount of £2.4 million (2007: £2.5 million) in respect of assets held under finance leases.

Land and buildings were revalued at 30 September 1997 by Chestertons Chartered Surveyors, independent valuers not connected with the Group, on the basis of depreciated replacement cost for the two pyrotechnic sites, and on open market for the remainder.

	2008 £m	2007 £m
30 September 1997 depreciated replacement cost	5.8	5.8
Freehold at cost	54.5	31.4
	60.3	37.2

If stated under historical cost principles the comparable amounts for the total of land and buildings would be:

	2008 £m	2007 £m
Cost	58.3	35.2
Accumulated depreciation	(7.3)	(4.7)
Historical cost value	51.0	30.5

All other tangible fixed assets are stated at historical cost.

At 31 October 2008 the Group had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £1.1 million (2007: £1.0 million).

Notes to the Group Financial Statements

16. Subsidiary undertakings

All subsidiary undertakings have been included in the consolidation. The undertakings held at 31 October 2008 which, in the opinion of the directors, principally affected the results for the year or the net assets of the Group are shown below.

Subsidiary undertaking	Country of incorporation (or registration) and operation	% of issued ordinary share capital controlled by Chemring Group PLC	Activity
Chemring Countermeasures Ltd	England	100	Countermeasures
Chemring Defence UK Ltd	England	100	Energetics
Chemring Marine Ltd	England	100	Energetics
B.D.L. Systems Ltd	England	100	Energetics
Chemring EOD Ltd	England	100	Energetics
Richmond Electronics & Engineering Ltd	England	100	Energetics
Chemring Energetics UK Ltd	Scotland	100	Energetics
Chemring Defence Germany GmbH	Germany	100	Energetics
Alloy Surfaces Company, Inc.	USA	100	Countermeasures
Kilgore Flares Company LLC	USA	100	Countermeasures and energetics
Technical Ordnance, Inc.	USA	100	Energetics
Titan Dynamics Systems, Inc.	USA	100	Energetics
Scot, Inc.	USA	100	Energetics
Martin Electronics, Inc.	USA	100	Energetics
Chemring Australia Pty Ltd	Australia	100	Countermeasures and energetics
Pirotécnia Oroquieta S.L.	Spain	100	Energetics
Simmel Difesa S.p.A.	Italy	100	Energetics
Chemring Nobel AS	Norway	100	Energetics
Associated undertaking			
CIRRA S.A.	France	49	Countermeasures

17. Interest in associate

	2008 £m	2007 £m
Interest in associate (including goodwill of £0.5 million (2007: £0.5 million))	1.0	1.0
Amounts relating to associate:		
	2008 £m	2007 £m
Assets	0.9	0.6
Liabilities	(0.4)	(0.1)
Revenue	0.7	0.6
Profit after tax	0.1	0.1

Results of the associated undertaking relate to the Group's share of CIRRA S.A.

18. Inventories

	2008 £m	2007 £m
Raw materials	36.4	22.5
Work in progress	30.1	14.7
Finished goods	22.6	14.0
	89.1	51.2

There are no significant differences between the replacement costs and the fair values shown above.

19. Trade and other receivables

	2008 £m	2007 £m
Current		
Trade receivables	77.2	51.6
Allowance for doubtful debts	(1.2)	(0.1)
	76.0	51.5
Other debtors	8.1	8.6
Prepayments and accrued income	3.7	1.8
	87.8	61.9

All amounts shown above are due within one year.

The average credit period taken on sales of goods, adjusted for Group revenue had the acquisitions taken place on the first day of the financial year, is 77 days (2007: 69 days). No interest is charged on the receivables from the date of invoice to payment.

The Group's policy is to provide in full for debtors greater than 120 days beyond agreed terms, unless extenuating circumstances exist. The Group does not experience significant bad debt write-offs and hence no movement schedule for the allowance for doubtful debts has been provided due to its immaterial level, 1% of trade receivables (2007: nil). An ageing analysis has not been shown as all significant overdue receivables are covered by the allowance for doubtful debts provision above.

The directors consider that the carrying amount of trade and other receivables approximates to their fair values.

20. Cash and cash equivalents

Bank balances and cash comprise cash held by the Group and short term deposits with an original maturity of three months or less. The carrying amount of these assets approximates to their fair value.

£5.0 million of cash is held in escrow in relation to the Chemring Group Staff Pension Scheme (see Note 35).

21. Bank loans and overdrafts

	2008 £m	2007 £m
Bank loans and overdrafts	19.7	22.5
UK medium term loans	22.9	32.1
- sterling denominated	-	22.1
- US dollar denominated	45.0	52.6
- Euro denominated	3.2	3.1
- other denominated	3.1	3.6
Overseas medium term loans	12.5	-
US loan notes	76.9	-
	183.3	136.0
Borrowings falling due within:		
One year	19.7	22.5
One to two years	21.2	18.2
Two to five years	34.9	86.1
After five years	107.5	9.2
	183.3	136.0
Analysis of borrowings by currency:		
Sterling	45.1	54.1
US dollar	81.1	25.7
Euro	53.8	53.1
Other	3.3	3.1
Total	183.3	136.0

Notes to the Group Financial Statements

21. Bank loans and overdrafts continued

	2008 %	2007 %
The weighted average interest rates paid were as follows:		
Bank overdrafts	6.1	6.3
UK medium term loans		
- sterling denominated	6.7	6.7
- US dollar denominated	6.3	6.4
- Euro denominated	5.6	5.4
- other denominated	6.8	6.5
Overseas medium term loans		
- US dollar denominated	4.2	2.7
US loan notes		
- sterling denominated	6.8	–
- US dollar denominated	6.3	–

Bank loans and overdrafts held with Bank of Scotland are secured by a debenture over the assets of certain of the Group's subsidiaries and are also subject to cross guarantees between subsidiaries. Bank loans held with Citizens Bank of Pennsylvania (USA) are secured on the related assets purchased with these loans by Alloy Surfaces Company, Inc. The security over the US loan notes ranks pari passu with that held by Bank of Scotland.

As the loans are re-translated to the year end exchange rates, the directors do not believe the fair value of the Group's borrowings to be materially different to the book values.

There have been no breaches of the terms of the loan agreements or defaults during the current or previous year.

The Group has the following undrawn borrowing facilities in various currencies available in respect of which all conditions precedent had been met. These facilities are at floating interest rates.

	2008 £m	2007 £m
Undrawn borrowings		
Cash and gross facilities	140.6	73.7
Bonds and guarantees	(33.5)	(18.7)
Total undrawn borrowings	107.1	55.0

22. Obligations under finance leases

	2008 £m	Minimum lease payments 2007 £m	2008 £m	Present value of minimum lease payments 2007 £m
Amounts payable under finance leases:				
Within one year	0.8	0.8	0.7	0.7
In the second to fifth years	2.2	1.2	1.8	1.1
After five years	0.4	0.4	0.4	0.4
Less future finance charges	(0.5)	(0.2)	–	–
Present value of lease obligations	2.9	2.2	2.9	2.2
Less amounts due within twelve months shown under current liabilities			(0.7)	(0.7)
Amount due for settlement after twelve months			2.2	1.5

Finance lease obligations attract interest rates of between 2% and 3% above base rate. Lease obligations are denominated in sterling, US dollars, Euro and Australian dollars.

The fair value of the Group's leases approximates to their carrying amounts.

The Group's obligations under finance leases are secured by the lessors' title to the underlying leased assets (see Note 15).

23. Trade and other payables

	2008 £m	2007 £m
Current		
Trade creditors	58.6	34.4
Other creditors	9.6	17.7
Other tax and Social Security	3.2	3.4
Accruals and deferred income	37.1	15.9
	108.5	71.4
Non-current	1.8	0.4

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. The directors consider that the carrying amount of trade payables approximates to their fair value.

24. Financial instruments and risk management

The Group uses financial instruments to manage financial and commercial risk wherever it is appropriate to do so. The main risks addressed by the financial instruments of the Group are interest rate risk, foreign exchange risk and liquidity risk. The Group's policies in respect of the management of these risks, which remained unchanged throughout the year, were as follows:

Market risk

The Group's multi-national activities expose it to the financial risks of changes in foreign currency exchange rates and interest rates. The Group enters into a variety of derivative financial instruments to manage its exposure to interest rate and foreign currency risk, including:

- Forward foreign exchange contracts to hedge the exchange rate risk arising on translation of the Group's investments in overseas businesses which have currencies other than sterling as their functional currency.
- Interest rate swaps to mitigate the risk of rising interest rates.
- Forward currency structures to hedge the exchange risk arising on translation of the overseas business profits.

Foreign currency risk management

The Group undertakes certain transactions denominated in foreign currencies. Hence, exposures to exchange rate fluctuations arise. Foreign currency exchange risk can be subdivided into two components, transactional risk and translation risk:

Transactional risk: The Group policy is to hedge significant transactional currency exposures via the use of forward foreign exchange contracts. The measurement and control of this risk is closely monitored on a Group-wide basis.

Translation risk: The Group translates overseas results and net assets in accordance with the accounting policy in Note 3. The translation risk on net assets is mitigated by the transfer of currencies between Group companies and the appropriate use of foreign currency borrowings.

The carrying amounts of the Group's foreign currency denominated monetary assets and liabilities at the year end are as follows:

	US\$	Euro	NOK	2008 AU\$	US\$	Euro	NOK	2007 AU\$
Monetary assets (million)	83.9	55.0	32.6	5.3	62.6	32.3	33.1	3.7
Monetary liabilities (million)	168.2	105.0	45.6	1.1	81.4	101.3	35.0	0.6

Currency denominated net assets are partially hedged by currency borrowings. The borrowings detailed below were designated as hedging instruments in net investment hedges.

	US\$	Euro	NOK	2008 AU\$	US\$	Euro	NOK	2007 AU\$
Borrowings (million)	125.0	66.9	35.0	—	47.9	80.0	35.0	—

The Group uses foreign exchange contracts to hedge its currency risk, most with a maturity of less than one year from the year end. When necessary, forward exchange contracts are rolled over at maturity. The most significant exchange rate to manage as far as the Group is concerned is the sterling: US dollar exchange rate.

Notes to the Group Financial Statements

24. Financial instruments and risk management continued

The following table details the forward foreign currency contracts for sales of foreign currencies outstanding as at 31 October:

	2008	Average exchange rate 2007	2008 m	Expiring within one year 2007 m
US dollar	2.04	1.97	9.0	5.0
Euro	1.39	1.43	2.0	4.0

At the year end, there were two US dollar structures in place which were set up to protect the Income Statement from currency fluctuations during 2008 and through to October 2010, and provide an economic hedge.

The structures involve a cap and a collar, which lock in the exchange rates and give the Group the appropriate protection. However, these structures do not give linear relationships with the gain or loss from re-translation of future profits and hence hedge accounting has not been adopted.

At 31 October 2008, an £8.7 million loss is shown as an adjustment to underlying operating profit and represents the fair value of the structures. The significant change arises due to the sudden appreciation of the US dollar in the last month of the year. The appreciation of the dollar has locked the structures into a fixed rate of 1.855 on a currency amount of \$66 million in the year to October 2009 and \$36 million in the year to October 2010.

The principal amounts of the Group's Euro, NOK and US dollar bank loans and private placement have been accounted as net investment hedges on the European, Norwegian and US businesses. These hedges are effective throughout the year and the losses arising on translation have been offset against the gains on retranslation of the subsidiaries in reserves.

Interest on borrowings is denominated in currencies that match the cash flows generated by the underlying operations of the Group. This provides an economic hedge and no derivatives are entered into except for interest rate swaps to hedge the interest rate risks.

Foreign currency sensitivity analysis

The following table details the Group's sensitivity to a 10 cent movement in the relevant foreign currencies against sterling. 10 cent represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the year end for a 10 cent change in foreign currency rates. A negative number indicates a decrease in profit and equity where sterling weakens against the relevant currency.

	2008 £m	US dollar impact 2007 £m	2008 £m	Euro impact 2007 £m
Loss	(7.8)	(0.7)	(3.5)	(3.8)
Other equity	(7.8)	(0.7)	(3.5)	(3.8)

The Group's sensitivity to foreign currency has increased during the current year mainly due to the growth of the US and European subsidiaries. These potential losses arising on the year end foreign currency monetary assets and liabilities would be more than offset by future translation and transaction gains.

In the management's opinion the sensitivity analysis is unrepresentative of the inherent foreign exchange risk as the year end exposure does not reflect the exposure during the year.

Interest rate risk

The Group finances its operations through a mixture of retained profits, bank borrowings and leasing lines of credit. The UK borrowings are denominated in sterling, Euro, US dollar and Norwegian Kroner and are subject to floating rates of interest linked to the Bank of Scotland base rate. In order to protect against the risk of higher interest rates, the Group has entered into amortising interest rate swaps for the majority of its UK borrowings. The overseas borrowings are denominated in local currency and are predominantly subject to fixed rates of interest.

During the year the Group refinanced part of its Bank of Scotland borrowing facilities with a private placement of ten year fixed interest loan notes in the US. The new arrangement provides a natural hedge against the Group's investment structure in its US businesses. The US loan notes are repayable in full in 2017.

24. Financial instruments and risk management continued

Euro, NOK and sterling floating rate borrowings have interest rate swaps which mitigate the exposure arising on the floating rate debt and are all designated as cash flow hedges. The following table details the notional principal amounts and remaining terms of interest rate swap contracts outstanding at the reporting date.

	Fixed rate %	Period of swap contracts		Currency value m
		From	To	
Sterling bank loans	5.41	November 2007	October 2011	34.6
Euro bank loans	4.35	November 2007	April 2012	66.9
NOK bank loans	5.495	November 2007	April 2012	35.0

As the Group has predominantly fixed interest rate loans the Income Statement is not sensitive to a small change in interest rates. The swap instruments match the interest payment profiles of the medium term debt.

Liquidity risk

The table below details the maturity profiles of the Group's derivative financial instruments and loans at 31 October 2008.

	Derivative payables £m	Derivative receivables £m	Loans and overdrafts £m	2008 Total £m	Derivative payables £m	Derivative receivables £m	Loans and overdrafts £m	2007 Total £m
Falling due within:								
One year	47.7	(41.2)	19.7	26.2	4.5	(4.6)	22.5	22.4
One to two years	22.1	(19.4)	21.2	23.9	–	–	18.2	18.2
Two to five years	–	–	34.9	34.9	–	–	86.1	86.1
After five years	–	–	107.5	107.5	–	–	9.2	9.2
	69.8	(60.6)	183.3	192.5	4.5	(4.6)	136.0	135.9

The profile of the Group's financial assets and liabilities is as follows:

Financial assets

	2008 Total £m	2007 Total £m
Sterling	38.5	12.3
US dollar	14.6	23.5
Australian dollar	1.8	1.5
Euro	21.0	13.4
Other currencies	1.7	0.7
	77.6	51.4
Offset in the UK	(8.0)	(12.7)
Cash at bank and in hand	69.6	38.7

Financial assets held in the UK enjoy a right of interest offset against overdraft balances. Overseas financial assets have a weighted average interest rate of 2.0% (2007: 3.9%). The financial assets for both years are at floating rate.

Included within the above is £5.4 million of restricted cash, £5.0 million of which is the escrowed pension scheme sum referred to in Note 35.

Notes to the Group Financial Statements

24. Financial instruments and risk management continued

Financial liabilities

	Floating rate £m	Fixed rate £m	2008 Total £m	Floating rate £m	Fixed rate £m	2007 Total £m
Sterling	(3.1)	(53.1)	(56.2)	(27.9)	(41.2)	(69.1)
US dollar	(4.2)	(76.9)	(81.1)	(3.0)	(22.7)	(25.7)
Euro	(0.8)	(53.0)	(53.8)	(1.6)	(51.5)	(53.1)
Other currencies	–	(3.2)	(3.2)	–	(3.1)	(3.1)
	(8.1)	(186.2)	(194.3)	(32.5)	(118.5)	(151.0)
Offset in the UK			8.0			12.7
			(186.3)			(138.3)
Bank loans and overdrafts			(19.7)			(22.5)
Medium term loans UK			(71.1)			(109.9)
US loan notes			(89.4)			–
Medium term loans overseas			(3.1)			(3.6)
Obligations under finance leases			(2.9)			(2.2)
Preference shares			(0.1)			(0.1)
			(186.3)			(138.3)

A right of offset exists for currency amounts held within the UK by Bank of Scotland. These are used to offset the interest charged on the UK overdraft which bears interest at 1.25% above LIBOR. Cash at bank and in hand consists primarily of overseas funds which are used as short term intra-group financing as well as an internal exchange rate hedge.

The weighted average interest rate of fixed rate financial liabilities at 31 October 2008 was 6.2% (2007: 5.7%) and the weighted average period of funding was six years (2007: five years).

Derivative financial instruments

The Group has three amortising interest rate swaps, from floating to fixed rate; one that expires in 2011 at a rate of 5.41% (sterling), one that expires in 2012 at a rate of 4.35% (Euro) and one that expires in 2012 at a rate of 5.495% (NOK). The fair value of interest rate swaps recognised on the Balance Sheet at 31 October 2008 was £1.2 million liability (2007: £0.6 million asset). The Group also has four forward exchange contracts with a fair value of £1.2 million liability (2007: £0.3 million asset). The total of these financial instruments is £2.4 million liability (2007: £0.9 million asset) and is recorded in reserves.

The following table details the fair value of derivative financial instruments recognised in the Balance Sheet at 31 October:

	2008 Total £m	2007 Total £m
Interest rate swaps	(1.2)	0.6
Forward exchange contracts	(1.2)	0.3
Forward currency structure derivatives	(8.7)	–
	(11.1)	0.9

Analysed as:

	2008 Total £m	2007 Total £m
Included in (current liabilities)/assets	(8.1)	0.9
Included in non-current liabilities	(3.0)	–
	(11.1)	0.9

Hedge accounting has been applied on the forward exchange contracts and interest rate swaps. The values are recorded in reserves. The £8.7 million loss on currency structures is recorded in the Income Statement as part of the reconciliation to underlying operating profit.

24. Financial instruments and risk management continued**Credit risk**

The Group's principal financial assets are bank balances and cash, and trade and other receivables, which represent the Group's maximum exposure to credit risk in relation to financial assets. The Group does not have any significant credit risk exposure to any single counterparty. The credit risk on liquid funds and derivative financial instruments is limited because the counterparties are banks with high credit ratings assigned by international credit rating agencies.

The Group's credit risk is primarily attributable to its trade receivables. The amounts presented in the Balance Sheet are net of allowances for doubtful receivables, based on prior experience and an assessment of the current economic environment. Trade receivables consist of a relatively small number of customers spread across diverse geographical areas. Customers are mainly multi national organisations or government agencies with whom the Group has long-term business relationships. The majority of the Group's business is with the US Department of Defense and the UK Ministry of Defence and as such the credit risk on debtors is considered to be very low. Ongoing credit evaluation is performed on the financial condition of accounts receivable and when appropriate action is taken to minimise the credit risk to the Group.

The Group's price risk is principally in relation to the cost of raw materials and is not considered significant. Price risk is managed through negotiations with suppliers and where appropriate the agreement of fixed price supply contracts.

Capital management

The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Board monitors both the demographic spread of shareholders, as well as the return on capital, which the Group defines as total shareholders' equity, excluding non-redeemable preference shares and minority interests, and the level of dividends to ordinary shareholders.

From time to time the Group purchases its own shares on the market; the timing of these purchases depends on the market prices. Primarily the shares are intended to be used for issuing shares under the Group's share-based incentive schemes. Buy and sell decisions are made on a specific transaction basis by the Board. The Group does not have a defined share buy-back plan.

There were no changes in the Group's approach to capital management during the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

25. Provisions

	Environmental provisions £m	Warranty provisions £m	Other provisions £m	Total £m
At 1 November 2007	–	1.6	0.1	1.7
Arising on acquisition of subsidiary undertaking	4.1	–	–	4.1
Effect of foreign exchange movements	0.9	–	–	0.9
Utilised in the year	–	(0.8)	–	(0.8)
At 31 October 2008	5.0	0.8	0.1	5.9
Analysed as:				
			2008 £m	2007 £m
Included in current liabilities			1.5	0.4
Included in non-current liabilities			4.4	1.3
			5.9	1.7

The warranty provisions at 31 October 2008 are held by Simmel Difesa S.p.A. and represent management's best estimate of the Group's liability under six year warranties granted, based on past experience for defective products.

The environmental provisions at 31 October 2008 are held by Scot, Inc. and represent management's best estimate of the liability based on certain environmental liabilities pre-dating the acquisition (see Note 33).

Notes to the Group Financial Statements

26. Deferred tax

The following are the major deferred tax liabilities/(assets) recognised by the Group and movements thereon during the year.

	Accelerated tax depreciation £m	Retirement benefit obligations £m	Tax losses £m	Other £m	Total £m
At 1 November 2006	6.7	(4.7)	(1.2)	(0.9)	(0.1)
(Credit)/charge to income	(0.2)	0.1	0.5	0.7	1.1
Charge/(credit) to equity	–	1.5	–	(1.0)	0.5
Amounts arising on acquisition of subsidiary undertakings	0.3	(0.4)	–	2.2	2.1
Foreign exchange movements	(0.4)	–	–	(0.2)	(0.6)
At 1 November 2007	6.4	(3.5)	(0.7)	0.8	3.0
Charge/(credit) to income	3.1	(0.3)	(0.9)	(0.7)	1.2
Charge to equity	0.5	–	–	3.0	3.5
Amounts arising on acquisition of subsidiary undertakings	0.1	–	–	(0.5)	(0.4)
Foreign exchange movements	(0.7)	–	–	1.0	0.3
At 31 October 2008	9.4	(3.8)	(1.6)	3.6	7.6

Certain deferred tax assets and liabilities have been offset in accordance with the Group's accounting policy. Deferred tax balances after offset, for balance sheet purposes are analysed as follows:

	2008 £m	2007 £m
Deferred tax liabilities	17.3	12.1
Deferred tax assets	(9.7)	(9.1)
	7.6	3.0

At the Balance Sheet date the Group had unrecognised tax losses of £8.4 million (2007: £16.8 million) potentially available for offset against future profits in certain circumstances. No deferred tax asset has been recognised in respect of this amount because of the unpredictability of future qualifying profit streams. These losses can be carried forward indefinitely.

27. Share capital

	2008 £m	2007 £m
Authorised		
43,000,000 ordinary shares of 5p each	2.2	2.2
Issued and fully paid		
35,535,699 (2007: 32,691,127) ordinary shares of 5p each	1.8	1.6

On 2 November 2007, 50,107 ordinary shares were issued at a market value of £1.0 million to partially fund the acquisition of Richmond Electronics & Engineering Limited.

On 27 June 2008, 1,111,112 ordinary shares were issued by way of a placing for cash to retrospectively fund the acquisition of Scot, Inc. and on 1 August 2008, a further 1,555,555 ordinary shares were issued as a vendor placing to fund the acquisition of Martin Electronics, Inc. The total net proceeds, after issue costs of £2.0 million, were £58.0 million.

A further 127,798 (2007: 82,500) ordinary shares were issued for a cash consideration of £0.5 million under the Group's executive share schemes.

The Company's authorised share capital also includes 62,500 7% cumulative preference shares of £1 each, which are all issued and fully paid-up, and are classified for accounting purposes within non-current liabilities.

28. Reserves

	Share premium account £m	Special capital reserve £m	Hedging reserve £m	Revaluation reserve £m	Retained earnings £m	Total £m
At 1 November 2006	53.6	12.9	0.2	1.6	23.9	92.2
Ordinary shares issued	6.9	–	–	–	–	6.9
Profit after tax for the year	–	–	–	–	32.0	32.0
Minority interest	–	–	–	–	0.1	0.1
Dividends paid	–	–	–	–	(6.0)	(6.0)
Net cost of share-based payments	–	–	–	–	0.9	0.9
Actuarial gain net of tax	–	–	–	–	2.9	2.9
Increase in fair value of cash flow hedging derivatives	–	–	0.2	–	–	0.2
Foreign exchange translation losses	–	–	–	–	(7.0)	(7.0)
Tax credits on items taken direct to reserves	–	–	–	–	3.0	3.0
At 1 November 2007	60.5	12.9	0.4	1.6	49.8	125.2
Ordinary shares issued	59.3	–	–	–	–	59.3
Profit after tax for the year	–	–	–	–	41.2	41.2
Dividends paid	–	–	–	–	(9.3)	(9.3)
Net cost of share-based payments	–	–	–	–	1.2	1.2
Actuarial gain net of tax	–	–	–	–	(0.1)	(0.1)
Decrease in fair value of cash flow hedging derivatives	–	–	(3.0)	–	–	(3.0)
Foreign exchange translation gains	–	–	–	–	24.8	24.8
Transfers between reserves	–	–	–	(0.1)	0.1	–
Tax debits on items taken direct to reserves	–	–	–	–	(4.8)	(4.8)
At 31 October 2008	119.8	12.9	(2.6)	1.5	102.9	234.5

The share premium account, the special capital reserve and the revaluation reserve are not distributable.

Included within retained earnings are £1.1 million of retained profits (2007: £1.1 million) relating to the associated undertaking and £0.1 million (2007: £0.1 million) of the Company's own shares held by the Group's ESOP trustees.

29. Statement of changes in equity

	2008 £m	2007 £m
Total recognised income and expense for the year (see page 54)	58.1	31.1
Dividends	(9.3)	(6.0)
	48.8	25.1
Ordinary shares issued	0.2	–
Share premium arising	59.3	6.9
Net cost of share-based payments	1.2	0.9
Purchase of minority interest	–	(0.2)
Own shares	(2.9)	(2.8)
Net addition to shareholders' funds	106.6	29.9
Opening shareholders' funds	124.0	94.1
Closing shareholders' funds	230.6	124.0

Equity comprises share capital, share premium and retained earnings.

Notes to the Group Financial Statements

30. Own shares

	2008 £m	2007 £m
Balance at 1 November 2007	2.8	—
Acquired in the year	2.9	2.8
Balance at 31 October 2008	5.7	2.8

The own shares reserve represents the cost of shares in Chemring Group PLC purchased in the market and held by the Group to satisfy options under the Group's share-based incentive schemes (see Note 32). During the year 160,000 (2007: 150,000) ordinary shares were acquired. This represents 0.87% of the total issued and fully paid ordinary share capital.

31. Obligations under non-cancellable operating leases

	2008 £m	2007 £m
Minimum lease payments under operating leases recognised in the Income Statement in the year	1.3	1.8

At the Balance Sheet date the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2008 £m	2007 £m
Within one year	1.1	0.9
Two to five years	1.5	2.6
More than five years	—	—
	2.6	3.5

Operating lease payments represent rentals payable by the Group. Leases are negotiated for an average term of three years and rentals are fixed for the lease period with an option to extend for a further period at the then prevailing market rate.

32. Share-based payments

The Group operates share-based compensation arrangements to provide incentives to the Group's senior management and other eligible employees.

Details of the four schemes which operated during the year are as follows:

The Chemring Group Performance Share Plan (the "PSP")

Under the PSP, conditional awards of ordinary shares are made at nil cost. Awards vest on the third anniversary of the award date. The scheme commenced in March 2006.

	Number of conditional shares awarded	
	2008	2007
Outstanding at beginning of year	228,096	128,676
Awarded during the year	98,771	99,420
Lapsed during the year	(16,124)	—
Outstanding at end of year	310,743	228,096
Subject to vesting at end of year	—	—

The Group assumes that all the conditions of the PSP will be met.

As there is no option element the share price is discounted based on the following assumptions:

- Dividend growth at 5% per annum (2007: growth at 5% per annum);
- weighted average cost of capital 10%.

The weighted average fair value of awards made during the year was 1,813.8p (2007: 1,661.5p)

32. Share-based payments continued

Restricted share award

A one-time award of 125,000 restricted ordinary shares at nil cost was made to Dr David Price on 4 April 2005, shortly after he took up his appointment as Chief Executive. 50% of the award vested in March 2006 and 50% in March 2007. There were no awards made during the year ended 31 October 2008 (2007: No awards).

The Chemring 1998 Executive Share Option Scheme (the "1998 ESOS")

Under the 1998 ESOS options are granted at a price not less than the market value of the Group's ordinary shares on the date the options are granted.

	Number of share options	2008 Weighted average exercise price Pence	Number of share options	2007 Weighted average exercise price Pence
Outstanding at beginning of year	177,798	598.5	197,798	512.0
Granted during the year	—	—	—	—
Exercised during the year	(127,798)	451.8	(20,000)	384.5
Outstanding at end of year	50,000	973.0	177,798	598.5
Exercisable at end of year	—	—	75,000	436.5

Share options were exercised throughout the year and the average share price was 2,324.5p (2007: 1,856.3p). The options outstanding at the end of the year have an exercise price of 973.0p.

The compensation expense recognised in respect of share options is based on their fair value at the grant date calculated using the Black-Scholes option pricing model.

No options were granted during the year. The Group recognised total expenses of £1.7 million (2007: £1.4 million) in respect of share-based payment transactions during the year.

A £3.4 million (including employers' national insurance) final settlement of The Chemring Group Phantom Share Option Scheme was made in November 2007. Expenses of £nil (2007: £1.0 million) were recognised during the year relating to this scheme.

The Chemring Group 2008 UK Sharesave Plan (the "UK Sharesave Plan")

The UK Sharesave Plan was launched during the year and the first tranche of options was granted on 1 August 2008.

	Number of options granted	
	2008	2007
Outstanding at beginning of year	—	—
Granted during the year	51,416	—
Lapsed during the year	(241)	—
Outstanding at end of year	51,175	—
Subject to exercise at end of year	—	—

The Chemring Group 2008 US Stock Purchase Plan (the "US Stock Purchase Plan")

The US Stock Purchase Plan was also launched during the year and the first tranche of options was granted on 16 September 2008. This plan has been introduced to provide US employees with the opportunity to share in the future success of the Group and mirrors the UK Sharesave Plan subject to certain legal and tax differences due to the differing jurisdictions.

	Number of options granted	
	2008	2007
Outstanding at beginning of year	—	—
Granted during the year	6,953	—
Outstanding at end of year	6,953	—
Subject to exercise at end of year	—	—

Notes to the Group Financial Statements

33. Acquisitions

The following acquisitions were completed during the year ended 31 October 2008:

Name of business acquired	Activity	Date of acquisition	Proportion of shares acquired %	Cost of acquisition £m
Richmond Electronics & Engineering Ltd	Energetics	2 Nov 2007	100	12.5
Titan Dynamics Systems, Inc.	Energetics	17 Mar 2008	100	2.6
Scot, Inc.	Energetics	2 Jul 2008	100	20.8
Martin Electronics, Inc.	Energetics	1 Aug 2008	100	37.1
				73.0
Satisfied by:				£m
Cash				72.0
Share issue to the vendors of Richmond Electronics & Engineering Ltd				1.0
				73.0
Reconciliation to cash flow statement:				£m
Cash paid for acquisitions in the year*				(72.0)
Cash acquired				3.8
Net cash outflow				(68.2)

*Includes £36.7 million funded by way of a vendor placing of ordinary shares for the acquisition of Martin Electronics, Inc.

An analysis of the net assets acquired of Scot, Inc. is shown below:

	Book value £m	Fair value adjustments £m	Fair value £m
Intangible assets	–	10.1	10.1
Property, plant and equipment	1.2	–	1.2
Deferred tax	–	1.7	1.7
Inventories	2.2	(0.5)	1.7
Trade and other receivables	1.0	–	1.0
Bank and cash balances*	0.3	–	0.3
Trade and other payables	(1.3)	(0.2)	(1.5)
Provisions	(0.6)	(3.5)	(4.1)
Net assets acquired	2.8	7.6	10.4
Goodwill arising on acquisition of Scot, Inc.	–	10.4	10.4
Total	2.8	18.0	20.8
£m			
Consideration			
Cash			20.4
Costs			0.4
Total			20.8

*Includes £0.3 million of restricted cash

Other than the IFRS3 valuation of acquired intangibles, the main fair value adjustment was the increase of an environmental provision by £3.5 million for certain environmental liabilities pre-dating the acquisition.

33. Acquisitions continued

An analysis of the net assets acquired of Martin Electronics, Inc. is shown below:

	Book value £m	Fair value adjustments £m	Fair value £m
Intangible assets	–	21.3	21.3
Property, plant and equipment	1.0	4.2	5.2
Deferred tax	–	0.1	0.1
Inventories	5.1	(0.4)	4.7
Trade and other receivables	3.3	(0.2)	3.1
Bank and cash balances	0.8	–	0.8
Trade and other payables	(2.3)	–	(2.3)
Net assets acquired	7.9	25.0	32.9
Goodwill arising on acquisition of Martin Electronics, Inc.	–	4.2	4.2
Total	7.9	29.2	37.1

£m

Consideration

Cash	36.7
Costs	0.4
Total	37.1

Other than the IFRS3 valuation of acquired intangibles the other significant adjustment was the revaluation of the land and buildings. An external consultancy company was appointed and a fair value adjustment of £4.2 million was made.

An analysis of the net assets acquired of Richmond Electronics & Engineering Ltd and Titan Dynamics Systems, Inc. is shown below:

	Book value £m	Fair value adjustments £m	Fair value £m
Intangible assets	0.2	6.0	6.2
Property, plant and equipment	1.7	–	1.7
Bank and cash balances	2.7	–	2.7
Working capital	(0.1)	(0.4)	(0.5)
Deferred tax	(0.1)	(1.9)	(2.0)
Provisions falling due within one year	(0.1)	(1.0)	(1.1)
Net assets acquired	4.3	2.7	7.0
Goodwill	–	8.1	8.1
Total	4.3	10.8	15.1

£m

Consideration

Cash	13.5
Share issue	1.0
Costs	0.6
Total	15.1

Adjustments from book value to fair value arise principally from the application of Group accounting policies and the recognition of intangible assets under IFRS3 *Business Combinations and Fair Value Adjustments to Inventories, Receivables, Property, Plant and Equipment*. Intangible assets relate principally to customer relationships, order book and trademarks (see Note 14). Fair values relating to the acquisition of Titan Dynamics Systems, Inc., Scot, Inc. and Martin Electronics, Inc. are provisional and will be finalised within one year of the acquisition date.

Costs include those legal and accounting costs incurred in developing the acquisition contracts and performing due diligence activities.

Notes to the Group Financial Statements

33. Acquisitions continued

All intangible assets were recognised at their respective fair values. The residual excess of total cost over the fair value of net assets acquired is recognised as goodwill in the financial statements. Goodwill represents the value of synergies and assembled workforces acquired.

The acquisitions during the year contributed £19.6 million of revenue and £3.2 million to the Group's profit before tax for the period between the date of acquisition and the Balance Sheet date.

If the acquisitions had been completed on the first day of the financial year, Group revenues and profits before tax for continuing activities for the year would have been approximately £381.2 million and £78.4 million respectively. This information is not necessarily indicative of the results of operations that would have occurred had the operations been acquired at the start of the year, nor of the future results of the combined operations.

34. Discontinued operations

The results of the discontinued operations for the year, or to the date of disposal, which have been included in the Consolidated Income Statement, were as follows:

	2008 £m	2007 £m
Revenue	–	3.8
Expenses	–	(4.0)
Trading loss	–	(0.2)
Loss on disposal	–	(1.5)
Loss before tax	–	(1.7)
Tax	–	(0.2)
Loss after tax for the year	–	(1.9)
Cash flows from discontinued operations		
Net cash used on operating activities	–	(0.9)
Net cash used on investing activities	–	(0.1)
Total	–	(1.0)

35. Pensions

Within the UK the Group operates two defined benefit schemes, the Chemring Group Staff Pension Scheme (the "Staff Scheme") and the Chemring Group Executive Pension Scheme (the "Executive Scheme"), as detailed below. In Germany, Chemring Defence Germany GmbH operates a defined benefit scheme (the "Chemring Defence Germany Pension Scheme") and in Norway, Chemring Nobel AS operates a defined benefit scheme (the "Chemring Nobel Scheme"). The other UK and overseas arrangements are all defined contribution schemes.

The Staff Scheme and Executive Scheme are funded schemes and the assets of the schemes are held in separate trustee administered funds. Full actuarial valuations for the Staff Scheme and the Executive Scheme as at 6 April 2006 have been prepared and updated to 31 October 2008 by a qualified actuary, using the projected unit credit method.

The Staff Scheme triennial valuation at 6 April 2006 was signed off by the trustees and the Company on 18 February 2008. The ongoing contributions were reduced. However the Group agreed to provide a £6.0 million bank guarantee to the Staff Scheme, to be drawn upon in certain events of default by the Company. In addition £5.0 million was placed in an escrow account to provide additional security to the Trustees in the event of a default (see Note 20).

The Executive Scheme triennial valuation at the same date was signed off by the trustees and Company on 5 October 2007.

The Chemring Defence Germany Pension Scheme is an unfunded scheme. The actuarial liability has been calculated at 31 October 2008 by a qualified actuary using the projected unit credit method. The main assumptions used were a discount rate of 5.3%, inflation rate of 1.8% and rate of increase in deferred pensions of 0%. The net deficit of the Chemring Defence Germany Pension Scheme was £1.1 million at 31 October 2008 (2007: £0.8 million).

The Chemring Nobel Scheme is an unfunded scheme. The actuarial liability has been calculated at 31 October 2008 by a qualified actuary using the projected unit credit method. The main assumptions used were a discount rate of 4.5%, inflation rate of 2.75% and rate of increase in deferred pensions of 1.5%. The net deficit of the Chemring Nobel Scheme was £1.4 million at 31 October 2008 (2007: £1.4 million).

35. Pensions continued

The amount recognised in the Balance Sheet in respect of the Group's defined benefit schemes is as follows:

	2008 £m	2007 £m
Present value of funded obligations	(42.0)	(48.3)
Fair value of scheme assets	28.4	35.0
Net liability recognised in the Balance Sheet	(13.6)	(13.3)

Analysis of the net liabilities recognised are as follows:

	2008 £m	2007 £m	Change £m
Chemring Group Staff Pension Scheme	(9.7)	(9.5)	(0.2)
Chemring Group Executive Pension Scheme	(1.4)	(1.6)	0.2
Chemring Defence Germany Pension Scheme	(1.1)	(0.8)	(0.3)
Chemring Nobel AS Pension Scheme	(1.4)	(1.4)	–
Net liability recognised in the Balance Sheet	(13.6)	(13.3)	(0.3)

Amounts recognised in the Income Statement in respect of the defined benefit schemes are as follows:

	2008 £m	2007 £m
Amounts included within operating profit:		
Current service cost	(0.9)	(1.0)
Amounts included as other finance costs:		
Expected return on scheme assets	2.0	1.9
Discount on scheme liabilities	(2.7)	(2.5)
	(0.7)	(0.6)
Net charge	(1.6)	(1.6)

Amounts recognised in the Statement of Recognised Income and Expense (SORIE) are as follows:

(i) scheme assets at the Balance Sheet date;

(ii) present value of the scheme liabilities at the Balance Sheet date.

	2008 £m	2007 £m
Actual return less expected return on pension scheme assets (i)	(9.9)	0.3
Experience (losses)/gains arising on scheme liabilities (ii)	–	–
Changes in assumptions underlying the present value of the scheme liabilities (ii)	9.8	4.1
Actuarial (loss)/gain recognised in SORIE	(0.1)	4.4

Changes in the present value of the defined benefit obligation are as follows:

	2008 £m	2007 £m
Opening defined benefit obligations	(48.3)	(48.5)
Opening adjustment to Chemring Nobel defined benefit obligations	(0.7)	–
Arising from business combinations	–	(1.4)
Service cost	(0.9)	(1.0)
Interest cost	(2.7)	(2.5)
Contributions from scheme members	(0.6)	(0.5)
Actuarial gains and losses	9.8	4.1
Benefits paid	1.4	1.5
Closing defined benefit obligation	(42.0)	(48.3)

Notes to the Group Financial Statements

35. Pensions continued

Movements in the fair value of the scheme assets were as follows:

	2008 £m	2007 £m
Opening fair value of scheme assets	35.0	32.2
Opening adjustment of Chemring Nobel scheme assets	0.7	–
Expected return on scheme assets	2.0	1.9
Actuarial gains and losses	(9.9)	0.3
Contributions from scheme members	0.6	0.5
Contributions from sponsoring companies	1.4	1.6
Benefits paid	(1.4)	(1.5)
	28.4	35.0

The total scheme assets updated to 31 October along with the expected rates of return on assets were as follows:

	Long term rate of return expected	2008 £m	Long term rate of return expected	2007 £m
Equities	8.4%	19.9	6.8%	24.5
Bonds	4.9%	8.5	4.8%	10.5
Total fair value of assets		28.4		35.0

The expected rates of return are determined by reference to relevant published indices. The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the scheme's investment portfolio.

History of experience gains and losses:

	IFRS 2008 £m	IFRS 2007 £m	IFRS 2006 £m	IFRS 2005 £m	UK GAAP 2004 £m
Present value of funded obligations	(42.0)	(48.3)	(48.5)	(47.6)	(38.8)
Fair value of scheme assets	28.4	35.0	32.2	27.4	22.7
Deficit in the schemes	(13.6)	(13.3)	(16.3)	(20.2)	(16.1)
Experience gains/(losses) on scheme liabilities	–	–	5.5	(0.3)	(0.9)
Percentage of scheme liabilities	–	–	11.2%	0.7%	2.3%
Experience (losses)/gains on scheme assets	(9.9)	0.3	2.2	2.2	(0.4)
Percentage of scheme assets	(34.9)%	0.9%	6.9%	8.0%	1.6%

Analysis of movement in the deficit in the schemes during the year:

	2008 £m	2007 £m
Opening deficit in schemes	(13.3)	(16.3)
Arising from business combinations	–	(1.4)
Current service cost	(0.9)	(1.0)
Contributions	1.4	1.6
Other finance costs	(0.7)	(0.6)
Actuarial (loss)/gain	(0.1)	4.4
Closing deficit in the schemes	(13.6)	(13.3)

The principal assumptions used in the actuarial valuations were as follows:

	2008	2007
Discount rate	7.4%	5.8%
Rate of increase in salaries	4.95%	4.6%
Rate of increase in deferred pensions	3.4%	3.1%
Rate of increase in pensions in payment (where applicable)	3.4%	2.3%
Inflation assumption	3.45%	3.1%
Expected return on scheme assets	7.3%	6.2%

35. Pensions continued

In determining the pension liabilities the Group uses mortality assumptions which are based on published mortality tables. For both the Staff Scheme and the Executive Scheme the actuarial table currently used is PA92(YOB)MC+1.

The assumption considered to be the most significant is the discount rate adopted. If the discount rate in the schemes were to change by 0.1% then it is predicted that the deficit in the schemes would change by approximately £0.7 million.

The Group anticipates contributions to the defined benefit schemes for the year ending 31 October 2009 will be £1.7 million (2007: 1.7 million).

36. Self insurance

The Group is self insured through its captive insurance company CHG Insurance Limited, based in Guernsey. The Group has been self insured for the first £2.5 million of material damage and business interruption cover, subject to a maximum liability of £3.5 million in any one year since 31 October 2001. Insurance cover in respect of this risk at a level over that disclosed here is placed with external insurers.

37. Insurance claim

During the year the case against the Group's former insurance broker for alleged negligence in relation to an insurance claim was settled. At the beginning of the year, the balance of the claim that had not been recovered from the broker was £2.4 million. After incurring legal costs in the year of £0.6 million, releasing a specific provision of £0.4 million and a related tax reserve of £0.8 million, a net write-off of £0.6 million was charged to unallocated head office costs in Note 5 following settlement.

38. Related party transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

Trading transactions

There are no trading activities between the Group and its associate.

Remuneration of key management personnel

The remuneration of the executive directors, who are the key management personnel of the Group, is set out below in aggregate for each of the categories specified in IAS24 *Related Party Disclosures*. Further information on the remuneration of individual directors is provided in the audited part of the Directors' Remuneration Report on pages 44 to 46.

The directors of the Company had no material transactions with the Company during the year other than as a result of service agreements.

The remuneration of the executive directors is determined by the Remuneration Committee having regard to the performance of individuals and the market trends.

	2008 £m	2007 £m
Remuneration of the executive directors	0.9	0.8
Share-based payments	0.1	0.3
Total	1.0	1.1

39. Post balance sheet events**Acquisition of Non-Intrusive Inspection Technology, Inc. ("NIITEK")**

On 12 December 2008 the Group completed the purchase of the entire stock capital of NIITEK for an initial consideration of \$30 million. Further deferred contingent consideration of up to \$10 million is payable upon achievement of certain financial targets.

Full disclosure of the acquisition and the analysis of assets acquired will be included in the 2009 Interim Report.

Independent Auditors' Report on the Parent Company Financial Statements

FOR THE YEAR ENDED 31 OCTOBER 2008

Independent Auditors' Report to the Members of Chemring Group PLC

We have audited the parent company financial statements of Chemring Group PLC for the year ended 31 October 2008 which comprise the Balance Sheet, the Statement of Total Recognised Gains and Losses, the Reconciliation of Movements in Shareholders' Funds and the related Notes 1 to 12. These parent company financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the Group financial statements of Chemring Group PLC for the year ended 31 October 2008 and on the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report, the Directors' Remuneration Report and the parent company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities in the Directors' Report.

Our responsibility is to audit the parent company financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the parent company financial statements give a true and fair view and whether the parent company financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the Directors' Report is consistent with the parent company financial statements. The information given in the Directors' Report includes that specific information presented in the Statement by the Chairman, the Review by the Chief Executive and the Review by the Finance Director that is cross referred from the review of the year and results section of the Directors' Report.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the other information contained in the annual report as described in the contents section and consider whether it is consistent with the audited parent company financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent company financial statements. Our responsibilities do not extend to any further information outside the annual report.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the individual company financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the individual company financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the parent company financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the parent company financial statements.

Opinion

In our opinion:

- the parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31 October 2008;
- the parent company financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the parent company financial statements.

Deloitte LLP

Chartered Accountants and Registered Auditors

Southampton, United Kingdom

20 January 2009

Parent Company Balance Sheet (under UK GAAP)

AS AT 31 OCTOBER 2008

	Note	£m	2008 £m	£m	2007 £m
Fixed assets					
Tangible assets	2		0.5		0.5
Investments	3		114.0		109.7
			114.5		110.2
Current assets					
Debtors	5	237.4		123.1	
Creditors due within one year	6	(39.2)		(31.4)	
Net current assets			198.2		91.7
Total assets less current liabilities			312.7		201.9
Creditors due after more than one year	7		(163.6)		(109.9)
			149.1		92.0
Capital and reserves					
Called-up share capital	8		1.8		1.6
Reserves					
Share premium account	9	119.8		60.5	
Special capital reserve	9	12.9		12.9	
Hedge reserve	9	(1.7)		1.0	
Revenue reserves	9	22.0		18.8	
			153.0	93.2	
Own shares	10	(5.7)		(2.8)	
			147.3		90.4
Shareholders' funds			149.1		92.0

These financial statements were approved by the Board of Directors on 20 January 2009.

Signed on behalf of the Board

D J Price

P A Rayner

Registered number in England: 86662

Parent Company Statement of Total Recognised Gains and Losses

FOR THE YEAR ENDED 31 OCTOBER 2008

	Note	2008 £m	2007 £m
Profit for the financial year	9	11.5	25.2
Own shares	10	(2.9)	(2.8)
(Decrease)/increase in fair value of hedge reserve	9	(3.4)	0.8
Deferred tax on hedge reserve movement	11	0.7	–
Total recognised gains and losses for the year		5.9	23.2

Reconciliation of movements in shareholders' funds

	Note	2008 £m	2007 £m
Profit for the financial year		11.5	25.2
Dividends		(9.3)	(6.0)
Profit for the year		2.2	19.2
Other recognised (losses)/profits		(2.7)	0.8
Ordinary shares issued	8	0.2	–
Share premium arising	9	59.3	6.9
Share-based payments	9	1.0	0.9
Own shares	10	(2.9)	(2.8)
Net addition to shareholders' funds		57.1	25.0
Opening shareholders' funds		92.0	67.0
Closing shareholders' funds		149.1	92.0

Profit attributable to shareholders

In accordance with the concession granted under the Companies Act 1985, section 230(1), the profit and loss account of Chemring Group PLC has not been presented separately in these financial statements. There is no material difference between the results disclosed and the results on an unmodified historical cost basis.

Cash flow statement

In accordance with the exemption under FRS1 the Company's cash flow statement has not been presented separately in these financial statements.

Notes to the Parent Company Financial Statements

FOR THE YEAR ENDED 31 OCTOBER 2008

1. Chemring Group PLC accounting policies

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards. The particular accounting policies adopted have been applied consistently throughout the current and previous year and are described below.

Accounting convention

The financial statements are prepared under the historical cost convention, as modified by the revaluation of property, in accordance with the Companies Act 1985 and applicable accounting standards (UK GAAP).

Revenue recognition

Interest income is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to its net carrying amount.

Dividend income from investments is recognised when the shareholder's rights to receive payment have been established.

Tangible fixed assets

Other than revalued land and buildings, property, plant and equipment are held at cost less accumulated depreciation and any recognised impairment loss. No depreciation is provided on freehold land. On other assets depreciation is provided at rates calculated to write down their cost or valuation to their estimated residual values by equal instalments over their estimated economic useful lives, which are considered to be:

Freehold buildings	- up to 50 years
Leasehold buildings	- the period of the lease
Plant and equipment	- 10 years

Investment in Group undertakings

Investments are stated at cost less any provision for impairment in value.

Operating leases

Operating lease rental charges are taken to the profit and loss account on a straight-line basis over the life of the lease.

Provisions

A provision is recognised when the Company has a present legal or constructive obligation as a result of a past event and it is probable that settlement will be required of an amount that can be reliably estimated. Long term liabilities and provisions are discounted when the impact is material.

Current tax

Current tax, including UK corporation tax and foreign tax, is provided for at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted, or substantially enacted, by the balance sheet date.

Deferred tax

Deferred tax is provided in full at the anticipated tax rates on differences arising from the inclusion of items of income and expenditure in tax computations in periods different from those in which they are included in the financial statements. Deferred tax is not provided on timing differences arising from the revaluation of fixed assets where there is no commitment to sell the asset. Deferred tax assets and liabilities are not discounted.

Special capital reserve

The special capital reserve was created as part of a capital reduction scheme involving the cancellation of the share premium account which was approved by the Court in 1986 and is in accordance with the requirements of the Companies Act 1985.

Foreign currencies

The functional currency of the Company is sterling. Transactions in foreign currencies are translated into sterling at the rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the rates ruling at that date. These translation differences are dealt with in the profit and loss account.

Pensions

The Company operates defined benefit pension schemes. The defined benefit schemes are multi-employer schemes including employees of other Group companies. It is not considered possible to allocate scheme assets and liabilities between the various companies and accordingly schemes are accounted for as though they were defined contribution schemes. The amount charged to the profit and loss account is the contribution payable in the year. Differences between amounts payable and actually paid are shown as accruals or prepayments in the Balance Sheet.

Share-based compensation

For grants made under the Company's share-based remuneration schemes, amounts which reflect the fair value of options awarded at the time of grant are charged to the profit and loss account. The valuation of the options utilises a methodology based on the Black-Scholes model.

Notes to the Parent Company Financial Statements

FOR THE YEAR ENDED 31 OCTOBER 2008

2. Tangible assets

	Land and buildings £m	Plant and equipment £m	Total £m
Cost			
At 1 November 2007	0.2	0.8	1.0
Additions	–	0.1	0.1
At 31 October 2008	0.2	0.9	1.1
Depreciation			
At 1 November 2007	–	0.5	0.5
Charge for the year	–	0.1	0.1
At 31 October 2008	–	0.6	0.6
Net book value			
At 31 October 2008	0.2	0.3	0.5
At 31 October 2007	0.2	0.3	0.5

The Company had no capital commitments at 31 October 2008 (2007: nil).

Land and buildings represent leasehold improvements.

3. Investments

	Shares in subsidiary undertakings £m	Loans to subsidiary undertakings £m	Total £m
Cost			
At 1 November 2007	122.6	6.3	128.9
Acquisitions of subsidiary undertakings	2.4	–	2.4
Disposal*	(5.5)	–	(5.5)
Foreign exchange**	7.4	–	7.4
At 31 October 2008	126.9	6.3	133.2
Provision for impairment			
At 1 November 2007 and 31 October 2008	19.2	–	19.2
Net book value			
At 31 October 2008	107.7	6.3	114.0
At 31 October 2007	103.4	6.3	109.7

*Disposal of the business and assets of Leaffield Engineering Limited to Chemring Energetics UK Limited, a fellow subsidiary undertaking, and disposal of the residual McMurdo business.

**The Company has Euro-denominated borrowings which it has designated as a hedge of the net investment in its Italian subsidiary, Simmel Difesa S.p.A.

4. Investments in Group undertakings

Subsidiary undertaking	Country of incorporation (or registration) and operation	% of issued ordinary share capital controlled by Chemring Group PLC	Activity
Chemring Countermeasures Ltd	England	100	Countermeasures
Chemring Defence UK Ltd	England	100	Energetics
Chemring Marine Ltd	England	100	Energetics
B.D.L. Systems Ltd*	England	100	Energetics
Chemring EOD Ltd*	England	100	Energetics
Richmond Electronics & Engineering Ltd*	England	100	Energetics
Chemring Energetics UK Ltd	Scotland	100	Energetics
Chemring Defence Germany GmbH*	Germany	100	Energetics
Alloy Surfaces Company, Inc.*	USA	100	Countermeasures
Kilgore Flares Company LLC*	USA	100	Countermeasures and energetics
Technical Ordnance, Inc.*	USA	100	Energetics
Martin Electronics, Inc.*	USA	100	Energetics
Scot, Inc.*	USA	100	Energetics
Titan Dynamics Systems, Inc.*	USA	100	Energetics
Chemring Australia Pty Ltd*	Australia	100	Countermeasures and energetics
Pirot��nia Oroquieta S.L.*	Spain	100	Energetics
Simmel Difesa S.p.A.	Italy	100	Energetics
Chemring Nobel AS*	Norway	100	Energetics
Associated undertaking			
CIRRA S.A.	France	49	Countermeasures

*Investments held by a subsidiary company

The directors consider that the carrying value of the investments approximates to their fair value.

5. Debtors

	2008 ��m	2007 ��m
Amounts owed by subsidiary undertakings	231.5	118.5
Advance corporation tax recoverable	–	0.2
Corporation tax recoverable	2.2	2.1
Deferred tax asset (see Note 11)	1.5	1.3
Other debtors	1.6	0.2
Financial instruments	–	0.6
Prepayments and accrued income	0.6	0.2
	237.4	123.1

A financial instrument asset of nil (2007:   0.6 million) is recognised on the Balance Sheet in respect of the fair value of interest rate swaps (see Note 24 of the Group financial statements). The directors consider that the carrying value of the debtors approximates to their fair value. Only the amounts owed by subsidiary undertakings are due after more than one year.

6. Creditors due within one year

	2008 ��m	2007 ��m
Bank overdrafts	1.1	9.9
Bank loans	17.7	8.3
Trade creditors	1.1	1.6
Amounts owed to subsidiary undertakings	6.4	6.1
Other creditors	8.5	0.2
Other tax and Social Security	0.1	0.5
Accruals and deferred income	4.3	4.8
	39.2	31.4

Notes to the Parent Company Financial Statements

FOR THE YEAR ENDED 31 OCTOBER 2008

6. Creditors due within one year continued

A financial instrument liability of £8.1 million (2007: nil) is recognised in other creditors in respect of the fair value of derivative financial instruments (see Note 24 of the Group financial statements).

Bank loans and overdrafts held with Bank of Scotland are secured by a debenture over the assets of certain of the Group's subsidiaries and are also subject to cross guarantees between subsidiaries.

7. Creditors due after more than one year

	2008 £m	2007 £m
Derivative financial instruments (see Note 24 of the Group financial statements)	3.0	–
Medium term loan	71.1	109.8
US loan notes	89.4	–
Preference shares (62,500 shares of £1 each)	0.1	0.1
	163.6	109.9

The cumulative preference shares carry an entitlement to a dividend at the rate of 7p per share per annum, payable in equal instalments on 30 April and 31 October each year. Holders of the preference shares have the right on winding-up to receive, in priority to any other classes of shares, the sum of £1 per share together with any arrears of dividends.

	2008 £m	2007 £m
Borrowings falling due within:		
One year	18.8	18.2
One to two years	19.8	15.8
Two to five years	33.1	85.1
After five years	107.6	8.9
	179.3	128.0

8. Called-up share capital

	2008 £m	2007 £m
Authorised		
43,000,000 ordinary shares of 5p each	2.2	2.2
Issued, allotted and fully paid		
35,535,699 (2007: 32,691,127) ordinary shares of 5p each	1.8	1.6

The preference shares are presented as a liability (see Note 7) and accordingly are excluded from called-up share capital in the Balance Sheet.

Share options

The following options to subscribe for the Company's ordinary shares granted under the Group's share-based incentive schemes were outstanding at 31 October 2008:

The Chemring 1998 Executive Share Option Scheme

Date of grant	Number of ordinary shares under option	Exercise price per share £	Dates between which options may be exercised
1 Feb 2006	50,000	10.590	1 Feb 2009–31 Jan 2016

8. Called-up share capital continued**The Chemring Group Performance Share Plan**

Date of award	Number of ordinary shares under award	Vesting price per share £	Date when awards will vest
23 Mar 2006	115,170	nil	23 Mar 2009
27 Sep 2006	7,256	nil	27 Sep 2009
24 Jan 2007	92,755	nil	24 Jan 2010
23 Jan 2008	95,562	nil	23 Jan 2011

The Chemring Group 2008 UK Sharesave Plan

Date of grant	Number of ordinary shares under option	Exercise price per share £	Dates between which options may be exercised
1 Aug 2008	23,322	18.68	1 Aug 2011–31 Jan 2018
1 Aug 2008	27,853	18.68	1 Aug 2013–31 Jan 2018

The Chemring Group 2008 US Stock Purchase Plan

Date of grant	Number of ordinary shares under option	Exercise price per share £	Dates between which options may be exercised
16 Sep 2008	6,953	18.49	16 Sep 2010–15 Dec 2010

Full details of the schemes are disclosed in Note 32 of the Group financial statements.

9. Reserves

	Share premium account £m	Special capital reserve £m	Hedging reserve £m	Revenue reserves £m	Total £m
At 1 November 2007	60.5	12.9	1.0	18.8	93.2
Ordinary shares issued	59.3	–	–	–	59.3
Profit for the year	–	–	–	11.5	11.5
Decrease in fair value of hedging reserve	–	–	(3.4)	–	(3.4)
Dividends paid	–	–	–	(9.3)	(9.3)
Tax credits on items taken directly to reserves	–	–	0.7	–	0.7
Net cost of share-based payments	–	–	–	1.0	1.0
At 31 October 2008	119.8	12.9	(1.7)	22.0	153.0

The share premium account and special capital reserve are not distributable. The Company generated a profit for the financial year of £11.5 million (2007: £25.2 million). Dividends from subsidiary undertakings of £11.2 million (2007: £30.0 million) were received in the year.

10. Own shares

	2008 £m	2007 £m
Balance at 1 November 2007	2.8	–
Acquired in the year	2.9	2.8
Balance at 31 October 2008	5.7	2.8

The own shares reserve represents the cost of shares in Chemring Group PLC purchased in the market and held by the Group to satisfy options under the Group's share-based incentive schemes (see Note 32 of the Group financial statements). During the year 160,000 (2007: 150,000) ordinary shares were acquired. This represents 0.87% of the total issued and fully-paid ordinary share capital.

Notes to the Parent Company Financial Statements

FOR THE YEAR ENDED 31 OCTOBER 2008

11. Deferred tax

	2008 £m	2007 £m
Movements in deferred tax liabilities/(assets) are as follows:		
At 1 November 2007	(1.3)	(0.9)
Charge/(credit) to profit and loss account	0.5	(0.1)
Credit to Statement of Total Recognised Gains and Losses	(0.7)	(0.3)
At 31 October 2008	(1.5)	(1.3)
The amount provided represents:		
Other timing differences	(1.5)	(1.3)

12. Staff costs

	2008 number	2007 number
The average monthly number of employees (including executive directors) was:		
Total	25	21
	2008 £m	2007 £m
The costs incurred in respect of these employees were:		
Wages and salaries	2.4	1.9
Social security costs	0.3	0.2
Other pension costs	0.3	0.3
	3.0	2.4

Disclosure in respect of directors' emoluments can be found in the Directors' Remuneration Report on pages 44 to 46 of the Group's financial statements.

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