

Chemring|
Group|

**DELIVERING
GLOBAL
PROTECTION**

**CHEMRING GROUP PLC
ANNUAL REPORT
AND ACCOUNTS**

for the year ended 31 October 2013

CHEMRING GROUP A WORLD-LEADING DEFENCE COMPANY

Chemring is a global business that specialises in the manufacture of high technology products. We operate in four strategic product segments: Countermeasures, Sensors & Electronics, Pyrotechnics & Munitions, and Energetic Sub-Systems, and deliver high reliability solutions to protect people, platforms, missions and information against constantly changing threats. With production facilities in seven countries, we meet specific customer requirements in defence and security markets in more than sixty countries worldwide.

CHEMRING'S KEY STRENGTHS

Market leading positions in a number of core markets

- Chemring is a world leader in the countermeasure, IED detection and naval ammunition markets.

Excellent technology and broad product range

- Leading developer of portable EW and new IED detectors.
- Advanced flares for next generation aircraft including F-35 and Typhoon.

Significant new market opportunities

- International reach to growing non-NATO defence markets.
- Growing opportunities in security, cyber protection and non-defence markets.

Knowledgeable and talented employees

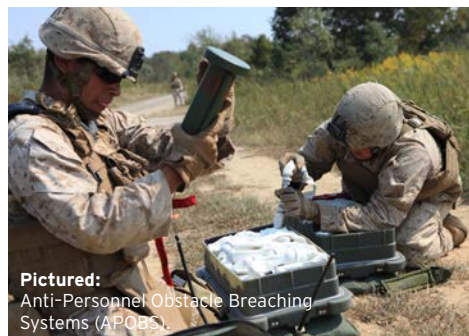
- Extensive pool of employees who continue to lead technology development in their fields.

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Chairman's statement

Find out Peter Hickson's view on Chemring's performance in 2013.



Pictured:
Anti-Personnel Obstacle Breaching Systems (APOBS).

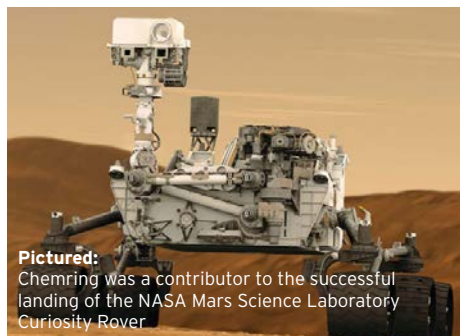
Segmental review

Review of the operational performance of the business.



CEO questions and answers

Mark Papworth's thoughts on his first year as Chief Executive Officer.



Pictured:
Chemring was a contributor to the successful landing of the NASA Mars Science Laboratory Curiosity Rover.

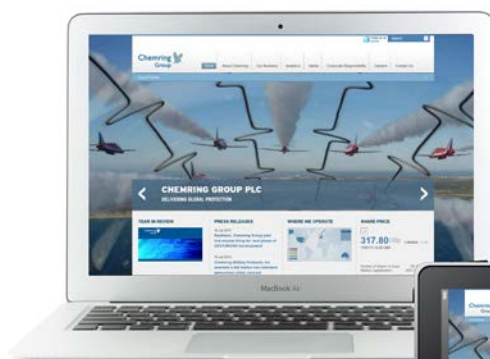
Strategy

Market environment, competitive dynamics and future prospects for each of Chemring's business segments.

Visit us online at

www.chemring.co.uk

Get investor information on the move with our iPad App.



Strategic report

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Chairman's statement



At the end of a year of significant change, Chemring is now a more resilient business, with a clear strategic direction. Much has been achieved by the new management team during the year, with the positive impact of the Performance Recovery Programme beginning to bear fruit. In addition, the Strategic Planning Process has provided a clear view of the market, competitive dynamics and prospects for each of the businesses, as well as identifying the core markets in which the Group will focus investment.

Defence markets have remained challenging, and operational issues in certain businesses further impacted the Group's financial performance. In addition, the US Government shutdown in the last month of the financial year meant that government inspectors were not present in a number of the Group's facilities, thus delaying product acceptance and shipment in October 2013.

Performance Recovery Programme

In January 2013, the new management team established a Performance Recovery Programme focused on delivering improvements in operational performance and providing increased resilience to challenging markets. This led to a reorganisation of the Group to ensure swift and effective response to attractive market opportunities. The cost of this reorganisation and restructuring will be approximately £15.0 million, which has predominantly arisen in the year ended 31 October 2013, and will deliver annual savings of approximately £10.0 million from 2014.

The Performance Recovery Programme had five initial areas of focus:

- Simplify the organisational structure.
- Integrate compatible business units and deliver untapped synergies.
- Implement a systematic programme of operational performance improvement.
- Refocus business development activity.
- Improve cash and cost management.

Chemring's previous organisational structure included significant divisional overhead, and this has been eliminated. Head office and divisional functions have been integrated into a single, tighter central management structure, resulting in a 46% reduction in head office and divisional headcount. The operating businesses have also been reorganised to provide a more effective reporting structure consisting of four strategic product segments: Countermeasures, Sensors & Electronics, Pyrotechnics & Munitions, and Energetic Sub-Systems.

Operational efficiency is improving, but it will take time to resolve all of the Group's operational issues. Clearer reporting lines and more rapid communication with the Group's senior management are delivering improved focus, accountability and responsiveness. Crucially, customers are also benefiting from this streamlined organisation through a more co-ordinated approach to the Group's markets, product portfolio, quality and technology development.

Strategic Planning Process

The Group has undertaken a comprehensive Strategic Planning Process to determine its business strategy. This has provided a clear view for each of Chemring's business units of their current market environment, competitive dynamics and future prospects. It has confirmed strong market-leading positions and the strength of the Group's technology in a number of areas, whilst highlighting new defence and adjacent non-defence opportunities. It has also identified a number of further operational initiatives which will enable the Group to manage the impact of current market challenges.

As a result of this process, a number of business units have been identified as not being part of Chemring's longer-term strategy. As a consequence, several divestment processes are now under way, the outcome of which should lead to a reduction in the Group's debt.

The first of these divestments was in December 2013, with a conditional agreement for the sale of Chemring Energetic Devices' build-to-print business located in Clear Lake, South Dakota to AMTEC Corporation for \$10.0 million (£6.1 million), payable in cash. Completion of the sale, which is conditional upon regulatory approvals and subject to a working capital adjustment, is expected within the next few weeks.

Trading

Chemring's improving operational performance has been adversely affected by the deteriorating external trading environment, largely as a result of budgetary pressures on global defence spending, which has manifested in delays in order placement in all our markets.

In particular, the US has seen a significant deterioration in defence spending due to the effects of sequestration, continuing resolution and budget reductions. This was heightened by the shutdown of the US Government in early October 2013, a key month in the Group's delivery schedule. The shutdown resulted in the temporary closure of the Defense Contract Management Agency (DCMA), the government agency with responsibility for inspecting and approving products for delivery to the US Department of Defense. This closure impacted deliveries to customers in the last weeks of the financial year but these delays are expected to be resolved in the first quarter of the current financial year.

Consequently, Group revenue for 2013 was £624.9 million, a decrease of 15.6%, generating an underlying operating profit of £72.1 million (2012: £88.3 million). Underlying profit before tax reduced by 25.2% to £52.4 million, resulting in underlying earnings per share of 21.6p (2012: 28.5p).

Order intake for the Group was £534.5 million, 14.5% below revenue. As a result, the closing order book was £675.5 million (2012: £760.9 million), a reduction of 11.2%. The closing order book is lower than the value of £702 million disclosed in the Group's trading update published on 25 November 2013, due to exchange rate fluctuations impacting the valuation of certain orders.

Board of directors

A number of changes were made to the Board of directors during the year. Mark Papworth joined as Chief Executive on 5 November 2012, followed by Steve Bowers as Finance Director on 7 January 2013.

Nigel Young, who was Interim Chief Financial Officer between August 2012 and January 2013, became a non-executive director and Chairman of the Audit Committee on 1 May 2013. Andy Hamment, who was previously Group Marketing Director of Ultra Electronics plc, joined the Board as a non-executive director on 1 July 2013. Two non-executive directors retired from the Board during the year: Peter Norriss, who had been a director since May 2004, stepped down at the Annual General Meeting in March 2013, and Roger Freeman, who had been a director since May 2006, retired from the Board on 31 December 2013. The Board is most grateful to both for their valuable contributions over many years.

These changes mean that Chemring has created a substantially new Board in the last two years. This fresh perspective will be important in meeting the challenges and opportunities facing the Group.

Dividends

The Board is recommending a final dividend for the year of 3.8p (2012: 4.2p). With the interim dividend of 3.4p (2012: 5.3p), paid in August 2013, this results in a total dividend in respect of 2013 of 7.2p (2012: 9.5p). This total dividend is in line with the Group's stated policy of maintaining a dividend that is covered three times by underlying earnings.

Chairman's statement

Outlook

Real progress has been made in transforming Chemring and the Performance Recovery Programme is eliminating a number of the issues that have dragged down recent performance. The benefits of the programme will come through in 2014 and the Group is better placed as a result.

While sequestration of the US defence budget has been avoided, the difficult market conditions that Chemring experienced in 2013 are expected to continue throughout 2014 and represent the most significant challenge that the Group currently faces. Growth in emerging markets is expected to be offset by defence spending constraints in the US, UK and Europe, and a recovery in the Group's traditional NATO markets is not expected in the medium term. The current strength of sterling against the US dollar, if sustained, will also impact earnings given the significance of the Group's US operations.

Chemring will continue to drive improvements in operational performance, and pursue the growth opportunities that exist, particularly within non-NATO markets where defence spending is expected to increase. It will also reshape and strengthen its portfolio of businesses through the disposal of non-core activities and technology investment in those businesses that can achieve sustainable growth and margin improvement. Meanwhile, the Board's expectations for the current financial year remain unchanged.

Peter Hickson

Chairman

23 January 2014

Underlying measures referred to in these financial statements are stated before costs relating to acquisitions and disposals, business restructuring and incident costs, profit on disposal of businesses, items deemed to be of an exceptional nature, impairment of goodwill and acquired intangibles, impairment of assets held for sale, amortisation of acquired intangibles and gains/losses on the movement in the fair value of derivative financial instruments. A reconciliation of underlying and total operating profit is set out in note 5 of the group financial statements.

Pictured right:
RESOLVE integrated tactical electronic warfare system.



MOVING INTO NEW TERRITORIES

CASE STUDY

HUSKY MOUNTED DETECTION SYSTEM (HMDS)

The Husky Mounted Detection System (HMDS) is a combat proven, high-performance ground penetrating radar (GPR) system, which operates on manned and unmanned blast-resistant vehicles that provide rapid ability to detect landmines and other explosive hazards, such as improvised explosive devices (IEDs), on main supply routes and open areas. Originally funded to satisfy an urgent operational requirement in Iraq and Afghanistan, the HMDS is now in use with the US, Canadian, Australian and Spanish militaries. The system's success has resulted in it being recognised as a critical requirement in the protection of troops, and there is significant interest in the system from other NATO countries.

There were over 250 HMDSs in use in Afghanistan, and in the US the system is now in the process of transitioning to become a baseline item in the US Department of Defense budget. In October 2013, Chemring Sensors & Electronic Systems was awarded a \$10.6 million contract by the US Army for the procurement of six HMDS test units, and a test support package. These systems will be used for advanced testing in preparation for a long-term procurement programme. This secures the position of the HMDS as an enduring capability for the US military over the next ten to fifteen years.



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Pictured left:
Husky HMDS checks a road for mines and IEDs in Afghanistan.

Chemring's business model

Chemring creates value by developing and manufacturing protection solutions for the defence and security markets based on threat detection, countermeasures and energetic material products.

Countermeasures

Chemring is well established as the world's leading manufacturer of expendable decoys to protect aircraft and ships from the growing threat of guided missiles. The Group's flares have been proven in peace-keeping operations in Iraq and Afghanistan, and the business continues to develop naval decoy technology in response to emerging anti-ship missile threats.

See page 10 for strategic focus
See page 18 and 19 for segmental review

Sensors & Electronics

Chemring's sensor and electronics products include the world's leading vehicle-mounted system for detecting IEDs, as well as core technologies for electronic warfare, and detecting, intercepting and jamming communications, including radio-controlled IEDs. The Group is exploiting its network protection capabilities to defend against the growing threat of cyber-attacks.

See page 10 for strategic focus
See page 20 and 21 for segmental review

Energetic Sub-Systems

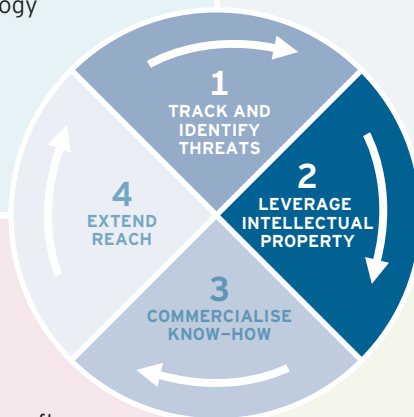
Chemring's energetic sub-systems are safety-critical components of missiles, aircraft and space launch systems. Operators and prime contractors depend on Chemring's very high reliability, single-use devices to perform key functions, including satellite deployment, aircrew egress and missile self-destruct.

See page 11 for strategic focus
See page 24 and 25 for segmental review

Pyrotechnics & Munitions

Chemring manufactures a range of pyrotechnic products which are used by militaries and security forces around the world for screening, signalling and illumination. In addition, the Group produces a specialist range of medium and large-calibre ammunition for tanks, armoured vehicles, infantrymen and naval platforms.

See page 11 for strategic focus
See page 22 and 23 for segmental review



Countermeasures



Sensors & Electronics



1 TRACK AND IDENTIFY THREATS

Chemring delivers protection solutions in a world facing rapidly-evolving threats from both organised militaries and the growing base of insurgents. Tracking and identifying threats and understanding their implications are critical precursors to detecting and countering these threats. The Group has strong, long-standing customer relationships around the world, which provide insight into a unique mix of military doctrines and security challenges faced by NATO, non-NATO and other security forces. The “home” markets in the US, UK, Europe and Australia provide a base of sophisticated and influential users, whilst a network of relationships in the Middle East, Asia Pacific and South America provide insight into specific security challenges, ranging from the Olympic Games to protecting offshore assets from pirates or insurgents. Chemring monitors the evolving pattern of threats, and this provides the base for exploring technology options to address these threats.

2 LEVERAGE INTELLECTUAL PROPERTY

Chemring has a strong portfolio of technology which it draws upon to develop solutions for customers. The Group strategically invests “seedcorn” capital to investigate technical alternatives and to secure critical intellectual property underpinning potential solutions. Where promising technologies are found outside the Group, a flexible approach is adopted to securing this for the targeted application – for example, by securing licences, funding joint development, or in some cases, outright acquisition of a company to secure both the technology and the underlying ability to develop it. Having secured the critical intellectual property, the Group takes a pragmatic approach to product design and development. In the case of specialist military products such as IED detectors, countermeasures or missile components, where the user’s specialist operational, qualification and test requirements place a disproportionate cost on development programmes, customer funding, support and qualification is sought to develop specific solutions. For example, our countermeasures products require significant investment in flight qualification, and the business work closely with a lead customer in the US or Europe to prove the product. Where military qualification costs are less prohibitive and their applications are wider than a single customer’s unique requirements, the Group invests its own development funding to secure a more versatile solution which can be sold more widely – for example, funding network protection offerings to ensure the Group can fully exploit the commercial market for these solutions.

Pictured left:
F15 dispensing flares.

Pictured far left:
HMDS is currently operational in Afghanistan.

3 COMMERCIALISE KNOW-HOW

Chemring is a manufacturing business, and we maintain a high margin portfolio by producing and selling proprietary products. This means that the Group optimises its manufacturing capability to protect our technology, product and process-related intellectual property. Energetic material products, including countermeasures, energetic sub-systems, pyrotechnics and munitions, all involve the blending, forming and packing of energetic materials. Rigour in these processes is critical to ensure product quality and performance, and the Group uses its world-leading capabilities in this field to perform the majority of this in-house at its large and well-equipped sites. For less critical production processes, such as metal part manufacture, component production may be outsourced. For sensors and electronics products, the critical processes are associated with assembly, test and software – the Group ensures that its production and delivery capabilities in these processes meet our production needs. In some cases, the Group exploits its knowledge by undertaking contract research and development for clients, where this provides an opportunity to extend the knowledge base, understand new opportunities and operational scenarios, or build new customer relationships.

4 EXTEND REACH

Chemring sells to over sixty countries globally through an established network of sales partners. These partners have strong in-country relationships with national procurement offices, and these channels are used in promoting Chemring’s full range of products, technologies, capabilities and solutions. These partners are critical to the launch of the Group’s new products into their markets, and also provide local intelligence and product support.

Defence is a sensitive capability for all countries, and many aim to develop a local industrial base to support their national security. This is particularly true in consumables such as countermeasures, where the ability of a supply chain to support military operations is key – the Group’s US and UK-based flare manufacturing capabilities were critical to support operations in Iraq and Afghanistan, and many nations are seeking to be self-sufficient in their own supply chain. The Group will work with nations who wish to develop indigenous capability, and will support product development and manufacturing facilities. For example, Chemring Australia has established a development programme in Australia, in collaboration with Chemring Technology Solutions, to develop a next-generation enhancement to man-portable electronic warfare equipment. Similarly, Mecar has signed an agreement to transfer technology for tank ammunition manufacture to a partner in Brazil, to enable it to meet national requirements locally – in this case, Mecar will control proprietary technologies through the long-term supply of critical components to its partner.

Strategy

The Group's vision is to be:

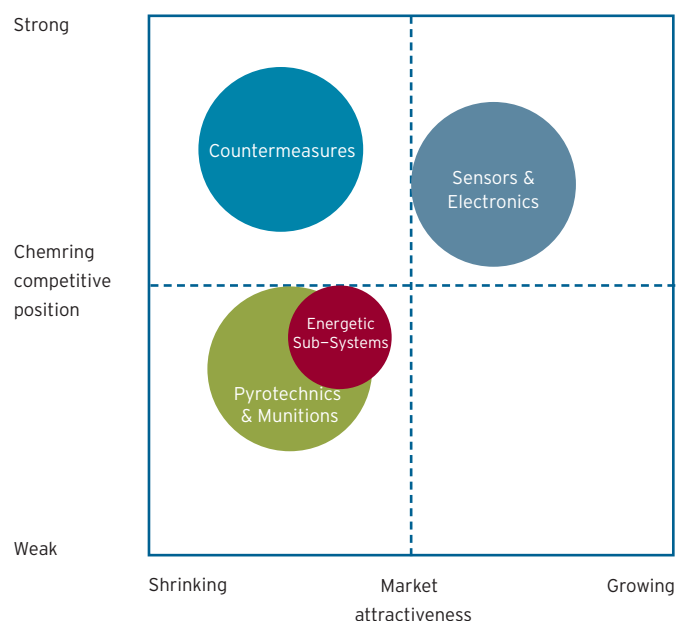
The leading developer and manufacturer of advanced detection and countermeasure technologies to defeat threats from radio frequency and network-based electronic warfare, IEDs, chemical and biological agents, and guided missiles.

The Group's strategy is to reposition itself for growth through the innovation and exploitation of intellectual property. This will focus on Chemring's core competencies, directing investment into those lines of business which have technologies, products and market positioning that provide the greatest opportunity to achieve sustainable high margins and revenue growth.

Historically, Chemring has adopted a strategy and structure focused on being able to respond quickly to urgent requirements in rapidly changing operational scenarios. This approach supported a regional divisional structure, and strong local investment in facilities, equipment and research and development. As current NATO operations draw to a close, Chemring has refocused its strategy on highly-targeted investment across the portfolio, delivering structural efficiencies and improving operational performance.

Targeted investment

The first element of Chemring's strategy is to manage the Group businesses as a portfolio, based on a rational and objective analysis of their markets, and their competitive position within those markets. The summary of this analysis is shown below with clear priorities for each segment.



Maintain world leadership in countermeasures market

Chemring has a clear lead in expendable decoys, as a result of its customer relationships and manufacturing facilities in its core markets of the US, UK and Australia, combined with advanced technologies in flare, radio frequency and special material decoys. In the face of reduced short-term demand, the Group is integrating Alloy Surfaces and Kilgore Flares to form Chemring Countermeasures USA, in order to reduce costs and raise efficiency levels.

The three strategic priorities for the Countermeasures segment are:

- Complete the integration of Chemring Countermeasures USA. The integration of Alloy Surfaces and Kilgore Flares has already reduced the overhead base and enabled sharing of operational best practice to position Chemring Countermeasures USA for profitable growth as new platforms enter service.
- Maintain a technological lead in core markets. Customers in these markets are the most advanced in the world, and the Group will promote targeted customer-funded development projects to maintain national capabilities to support future military operations.
- Optimise the Group's manufacturing base and routes to market. Current manufacturing capacity is scaled to meet surge levels of demand. This capacity and its utilisation will be optimised to ensure a flexible, efficient and safe manufacturing base to meet customer requirements.

Build a world-leading technology base in Sensors & Electronics

Chemring has world-leading technologies in chemical, biological and IED threat detection, electronic warfare and cyber protection. The Group will invest to extend this portfolio of Sensors & Electronics technology. The key priorities are:

- Ensure critical wins in the US defence market. The US market is the world's largest and the Group will continue to invest to secure its position and win key programmes.
- Build a world-leading technology base across the Group's transatlantic footprint. Chemring's technical centres in the US and UK are well-recognised nationally but do not fully exploit the scale and synergies of its international operations. Chemring will build on existing customer relationships to anticipate user needs and capitalise on its global capability, growing the Group's technology base through targeted investment.
- Leverage Chemring's proven skills and reputation to expand into adjacent areas, for example cyber protection.
- Incubate technologies for non-defence markets.
- Complete the integration of Chemring Detection Systems and NIITEK in the US into a single organisation, Chemring Sensors & Electronic Systems, to leverage technology capabilities, co-ordinate customer interactions and maximise supply chain efficiencies.

Optimise operational performance of Pyrotechnics & Munitions

Military pyrotechnics and ammunition are used in both training and active operations. The global market for these products has been heavily impacted by the decline in NATO operations in Afghanistan, leaving many forces' stockpiles full and a target for short-term cuts. The Group's strategic priorities for this segment are:

- Establish operational excellence in pyrotechnics. Chemring's pyrotechnic portfolio includes many products which are infrequently produced, which causes complexity and impacts margins. The Group will rationalise this product range and continue to improve production efficiency.
- Maintain the leading position in large and medium-calibre ammunition niches. Chemring has a strong position in naval and light armoured vehicle ammunition, and will maintain the technologies and relationships which underpin this. The Group will also manage workload across its sites to reduce manufacturing bottlenecks and maximise capacity utilisation.

Focus on performance improvement and near-term market opportunities in Energetic Sub-Systems

Chemring's Energetic Sub-Systems segment is complex, with a wide variety of products produced infrequently in batch production runs. The market is stable, with significant qualification costs and other barriers to entry, and the segment therefore has the potential to improve margins. However, recent operational challenges have impacted performance. The key priorities for Energetic Sub-Systems are:

- Complete the integration of Hi-Shear with Chemring Energetic Devices, in order to exploit Hi-Shear's strong market position on key programmes such as the PAC-3 missile and the NASA Standard Initiator, whilst eliminating manufacturing bottlenecks by distributing work between sites. The integration will also deliver benefits from sharing best practices, systems and marketing resources.
- Explore non-defence opportunities in civil aerospace, space and other markets.

Deliver structural efficiencies

In 2013, a review of the Group's divisional structure was completed. This highlighted that the organisational structure was more focussed on local agility than efficiency, and also risked creating some confusion in the market-place, as similar business units in the US and Europe sought export opportunities outside their home markets. As a result, the Group's operational structure has been reconfigured along product and technology lines to eliminate regional divisional entities, and the integration of several key business units has been completed.

Improve operational performance

The restructuring has reduced the Group's overheads, and has facilitated both national and transatlantic synergies. However, several businesses have a poor track record of delivery on time or to cost and quality. This has driven a highly-focused thrust on manufacturing and operational performance improvement throughout the Group, but with specific focus on certain businesses. Actions include improvements to financial systems, changing operational management, redistribution of work between sites and elimination of manufacturing bottlenecks. This will continue within the segments, where grouping similar businesses together will better enable sharing of best practices, co-ordinated marketing strategies and establishment of centres-of-excellence.

Global growth opportunities

AREAS OF OPERATION AND POTENTIAL GROWTH

"With a footprint in the USA, Europe and Australia, Chemring is established in the world's largest defence markets – the Group is well positioned to move into fast-growing markets in the Middle East, Asia Pacific and South America."

NORTH AMERICA

Market overview

- Declining budget but reduced uncertainties following recent Bipartisan Budget Act
- Maintenance of key programmes including Joint Strike Fighter ("JSF")
- Transition from urgent operational requirements to core Programs of Record

Chemring's position

- Strong position on HMDS as it transitions to become a Program of Record
- Well positioned to capitalise on pre-emptive countermeasure technology and growth in JSF fleet
- Further opportunities in Sensors & Electronics

Regional defence spend*

\$664bn

SOUTH AMERICA

Market overview

- Growing regional defence and security spend
- Brazil is economically and strategically dominant in the region

Chemring's position

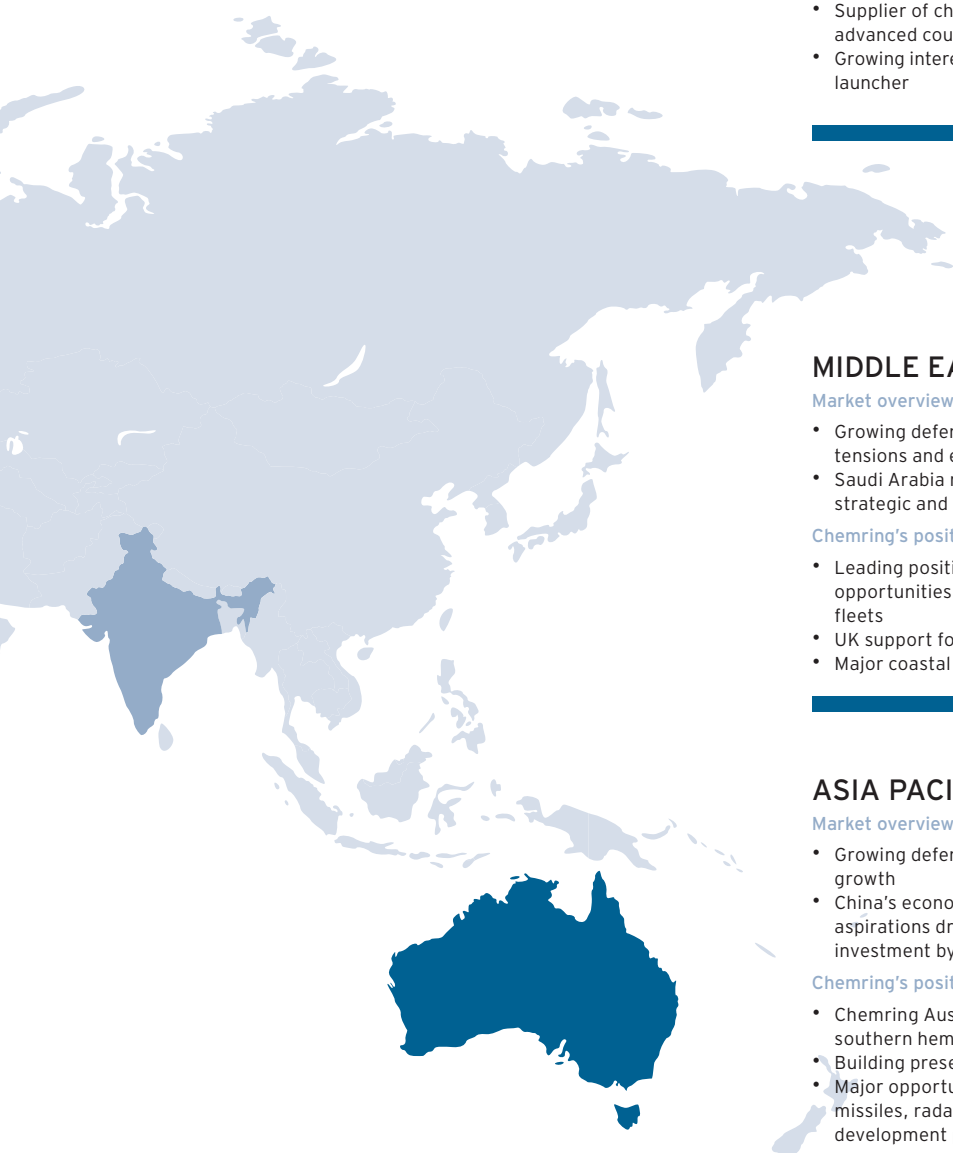
- Well-positioned for cyber security opportunity with regional partner
- Partnership on large-calibre ammunition

Regional defence spend*

\$69bn

KEY TO MAP

- WHERE WE OPERATE
- GROWTH POTENTIAL



EUROPE

Market overview

- Declining defence spend
- Several national strategic defence reviews
- Pockets of growth in newer NATO countries

Chemring's position

- Well positioned for key IED detection and electronic warfare opportunities
- Supplier of choice for traditional and advanced countermeasures
- Growing interest in CENTURION naval launcher

Regional defence spend*

\$280bn

MIDDLE EAST & NORTH AFRICA

Market overview

- Growing defence spend driven by regional tensions and economic growth
- Saudi Arabia maintaining its position as strategic and economic hub for the region

Chemring's position

- Leading position to win countermeasure opportunities for large combat aircraft fleets
- UK support for cyber security collaboration
- Major coastal defence opportunity

Regional defence spend*

\$142bn

ASIA PACIFIC

Market overview

- Growing defence spend driven by economic growth
- China's economic growth and strategic aspirations driving increased focus and investment by US and its allies

Chemring's position

- Chemring Australia well-positioned in southern hemisphere
- Building presence in India
- Major opportunities in countermeasures, missiles, radar and ammunition development programmes

Regional defence spend*

\$212bn

* Source: The Military Balance 2013 (excludes Iran, Syria, North Korea, Russia and China)

Market review

The global defence market is dominated by US and European budget reductions which overwhelm growth in Asia Pacific, the Middle East and South America

Chemring's business is driven by national defence departments which are either its immediate customers or the end-users of products incorporating its components. The global defence market has suffered several years of decline since its peak in 2010 and this macro trend is likely to continue until 2015 before it begins to recover. There are at least two coincident drivers for this. The first is that the US and NATO are winding down their military presence and combat operations in Iraq and Afghanistan, which at their peak intensity drove US Overseas Contingency Operations ("OCO") spending of more than \$150 billion per year over and above the baseline US defence budget. The second is the financial crisis, which has forced debt-laden governments to take vigorous measures across all departments to reduce their deficits. Most countries appear to have completed their most draconian cuts but many have revised the long-term view of their strategic military ambition and are proposing a permanently smaller force structure to support this.

United States

The US represents 40% of the world's defence spend and its rapid decline since 2010 dominates the overall market trajectory. With a decline in military operations, OCO funding has halved since 2010. This downward trend has been exacerbated by Washington's fractured politics which have crippled budget processes. The US Government's FY13 budget has been sequestered down by 10% from the departments' original requests. This had a direct impact on Chemring's performance in 2013, when the furlough of government officials in October impacted the ability of the Group's US businesses to ship products, causing some deliveries to slip beyond the year end. The recently hailed Bipartisan Budget Act, announced in December 2013, partially alleviates the sequester but total budgeted spend for 2014 will be down on the current year.

UK and Europe

The UK and Europe have also cut their budgets since the 2010 peak and these cuts will continue, with 2017 levels as much as 5% down on 2012 levels. Defence spending in Europe is well below the NATO commitment of 2% of GDP, and the top spending countries in Europe (UK, France, Germany and Italy) are reducing spend and all have conducted major reviews of future force requirements, scaling back both strategic ambition and required force structure. Turkey and Poland are the only major players in NATO which are increasing their spend, as they upgrade older equipment to modern standards.

Middle East and North Africa

This region continues to face instabilities, ranging from the systemic Arab-Israeli tensions to the extended civil war in Syria, unrest in Egypt, and Iran's uncertain position on its nuclear programme. Saudi Arabia is the largest defence player in the region, and its oil-driven economic growth, combined with aspirations to remain the local force of stability and peace, mean that it is likely to continue to grow its spend.

Asia Pacific

This region has enjoyed strong economic growth, enabling increased funding to support national capability upgrades throughout the region. China is not an accessible market but its accelerating defence spending and increasingly aggressive posture have driven a major shift in US regional focus, as well as encouraging other fast-growing economies in the region to accelerate their own spend. India, in particular, is modernising its defence capabilities, although faltering economic growth and a declining rupee have eroded real growth. The country still imports approximately 65% of its military equipment requirements, and the currency decline has therefore had a particularly pernicious effect on its buying power. Its policy of "make / buy Indian" aims to address this but has so far failed to transform the local defence industrial base.

South America

South America is dominated by Brazil, and its recent economic slowdown has reduced its ability to maintain the defence spending growth rates seen recently. Brazil's regional economic dominance means that its defence requirements are more driven by security challenges than in deterring a traditional full scale military attack by a neighbour. Two key programmes are SISFRON, an integrated border monitoring system, and SISGAAS, to secure the Amazon. In addition, Brazil has established CDCiber to build a capability to protect state IT systems from cyber-attacks.

Impact on Chemring segments

For Chemring, national defence budgets are an important environmental backdrop but they only form part of the picture. The Group's four strategic product business segments operate with different drivers across defence markets. In addition, the Group is actively seeking to grow its presence in other markets where it is already establishing a foothold.

Countermeasures

It is believed that the countermeasures market is close to customers' minimum sustaining rates of production, from which the industrial base still has the capability to respond to surge demand from extended military operations. The Group expects the market to slowly recover from these levels over the next few years, driven by exports and new platforms' achievement



of full operational capability. There has been some relaxation of export restrictions on advanced countermeasure technologies, and it is expected that some new customers will add these to their inventory of decoys. In addition, the fleet build-up and achievement of full operational capability for the Joint Strike Fighter and Typhoon will drive a need for significant war stocks of the unique decoys required for each of these platforms. In addition, the recent successful demonstration firings of the CENTURION launcher and the interest they have inspired suggest that there is real potential for the system, which should also reinvigorate a flat naval countermeasures market.

Sensors & Electronics

Chemring's Sensors & Electronics products are innovation-led, frequently developed in response to Urgent Operational Requirements ("UORs"). Whilst the operational tempo has reduced, recent conflicts have demonstrated the vulnerability of modern forces against asymmetric threats. As a result, counter-IED doctrine is becoming a key element of defence thinking and the equipment is migrating into core defence budgets, to establish a sustained capability for future operations. The HMDS is the most important example of this for Chemring but the Group's electronic warfare and electronic countermeasures products are other candidates. The Sensors & Electronics segment also has capabilities in fast-growing government and commercial information network protection markets, where the growing threat posed by cyber-attacks is creating opportunities for new protection technologies. Finally, this segment has the technology and products to solve a diverse range of problems in telecoms, medical, industrial and consumer markets, offering most scope to enable the Group to diversify away from dependence on defence.

Pyrotechnics & Munitions

The global military pyrotechnic and ammunition market has suffered a steep decline following the drop-off in military activity in Afghanistan. However, in regions where there is growth in defence spending and major capability upgrades, there is some growth in demand as countries buy war stockpiles of ammunition and pyrotechnics to support this.

Energetic Sub-Systems

The Energetic Sub-Systems market remains steady, driven by the existing operational military aircraft fleets, long-term missile production programmes, and a sustained tempo of military and civilian satellite launches and deployments. This segment has some non-military applications, including space and the oil and gas markets, and the Group expects demand to remain steady in these niches.

Pictured:
A HH-60H Seahawk helicopter launches flares.

Business highlights

OPERATIONAL

"Operational performance improvements beginning to show benefits in challenging defence markets."

Good progress with Performance Recovery Programme

- Creation of leaner, simpler organisation with elimination of divisional structure and overhead.
- Integration of four pairs of businesses to exploit synergies.

Completion of Strategic Planning Process

- Clear view of priorities for future investment.
- Identified potential non-core businesses.

Maintaining world lead

- HMDS transitioning to Program of Record.
- Sustained position of countermeasures for next-generation platforms.

International business development

- Growing presence in Middle East and Asia-Pacific markets through local partnerships.



See pages 2 and 3 for [further information](#)



Pictured:

A bomb disposal expert carrying a disrupter.



Pictured:

HMS Dragon's Lynx helicopter fires infra-red flares during an exercise over the T45 destroyer. (Crown Copyright)

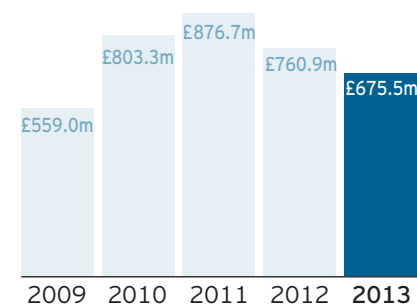
FINANCIAL

"Chemring's improving operational performance has been offset by the effects of a deteriorating external trading environment, largely as a result of budgetary pressures on global defence spending, which have manifested in delays in order placement in all of its markets."

Order book

£675.5m

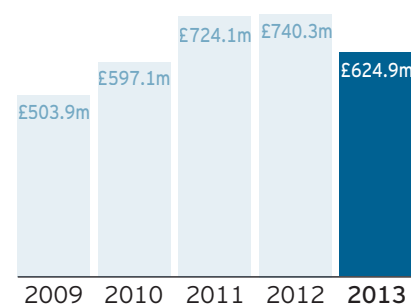
2012: £760.9m



Revenue

£624.9m

2012: £740.3m



Underlying operating profit

£72.1m

2012: £88.3m



See pages 28 and 33 for further information

Segmental highlights

Countermeasures

Creation of Chemring Countermeasures USA by integration of Alloy Surfaces and Kilgore Flares.

Revenue

£125.0m

Sensors & Electronics

Building on continued success of HMDS, with growing international interest and new detection technologies, applications and non-defence opportunities.

Revenue

£211.3m

Pyrotechnics & Munitions

Improving operational performance.

Revenue

£200.6m

Energetic Sub-Systems

Integration of Hi-Shear with Chemring Energetic Devices.

Revenue

£88.0m

COUNTERMEASURES

 See more information online
www.chemring.co.uk

Our business units:

Chemring Countermeasures USA – incorporating Alloy Surfaces and Kilgore Flares – manufactures infra-red (IR) air countermeasures, and is the only dedicated manufacturer of covert multi-spectral special material decoys.

The business is the foremost supplier of airborne expendable IR decoy flares, and serves as the sole-source IR decoy flare supplier for some of the world's most sophisticated and advanced airborne platforms. Kilgore was the first expendable IR decoy flare manufacturer to introduce full automation to the decoy manufacturing process, bringing a new level of safety and quality to the industry not previously seen.

Chemring Countermeasures – based in the UK, is a world leader in the design, development and manufacture of advanced expendable countermeasures for air and sea platforms, and is also developing next generation launchers for deploying naval decoys.

Chemring Australia – Australia's only onshore manufacturer of aircraft expendable countermeasures, and supplier of a range of pyrotechnic and military training products.

Analysis

Revenue in the Countermeasures segment was £125.0 million, down 23.4% on the previous year. This was primarily due to a lower opening order book in the US and UK, resulting from the drawdown from Afghanistan, but also reflected US Department of Defense delays in product acceptance, order funding and awards. Both sequestration and continuing resolution have caused delays to orders and sales, especially in relation to special material decoys. Further issues were experienced as a result of the US Government shutdown in October 2013. Sales at the Group's Australian operation reduced as a result of lower expenditure by the Australian Defence Force. The closing order book for Countermeasures was £160.8 million, down 24.6% on the previous year, reflecting generally lower order intake, particularly in the US, due to the effects of the drawdown from Afghanistan.

Activities during the year

The two US countermeasures business units have been integrated to form Chemring Countermeasures USA. This is enabling the Group to reduce overheads, retain the best management talent, reduce costs when volumes are low, and take advantage of synergies. It has also enabled the Group to focus operational and quality improvement resource on the significant challenges at Kilgore. The integration is delivering cost savings and, more importantly, is improving performance to customers.

The US Government shutdown in October 2013 resulted in the closure of the DCMA, the government agency with responsibility for inspecting and approving products for delivery to the US Department of Defense. This closure impacted deliveries in the final weeks of the year, the effects of which were particularly felt at Kilgore, which also continued to be impacted by production quality issues. Further steps are being taken to strengthen the management team at this business, and in the past six months a new General Manager and a new Health, Safety & Environment Manager have been appointed. These appointments are already having a meaningful impact on the business, and relationships with customers have improved significantly as a consequence.

The inclusion of decoy dispensers on the Joint Strike Fighter, with the significant costs associated with embedding these into the airframe and the development of a dedicated suite of flares for this platform, gives confidence that the Group's countermeasures technology will remain a critical element of defensive aids for military aircraft.

Chemring Countermeasures USA has developed a number of new evolutions of its special material decoys, and has successfully flight-tested a new MJU-66 decoy. This decoy, which will be used on multiple platforms, including the F-16, A-10 and C130 transport aircraft, will be fielded in 2014. In addition, the ASD-1292 decoy, which is an advanced IR decoy that was developed to beat multiple advanced threats, was successfully flight-tested in 2013. It is now scheduled for further testing in 2014 by a number of US agencies and

Order book
£160.8m
 (2012: £213.3m)

Revenue
£125.0m
 (2012: £163.2m)

services. In flight-testing, this flare has been shown to be an effective single decoy solution against legacy and most advanced IR threats.

Chemring Countermeasures USA continues to win new export orders. In 2013, the business received two FMS purchase orders from the US Army for M211 sales to a Middle Eastern customer, with further FMS orders expected shortly from other customers in the region.

Interest in Chemring Countermeasures USA's MJU-7A/B decoy remains high worldwide, as those countries using the F-15 move away from the older technology MJU-10 to the MJU-7A/B. This decoy can be used on the F-15 and F-16 fighters, as well as the C17 transport aircraft, which has opened up new markets in India, the UAE and Oman.

In Europe, Chemring Countermeasures and Chemring Technology Solutions have engaged in their first joint development. This relates to the CENTURION naval decoy launcher, where Phase 3 of development of the launcher software has successfully been completed. These businesses have also co-operated in the development of an air countermeasure electronic sequencer – a small circuit board which fits inside a standard flare cartridge case to provide accurate time delays for a single flare capable of firing multiple shots. This not only increases the decoy deployment capacity within existing aircraft dispenser constraints, but also opens up technical and market opportunities in air countermeasures.

The CENTURION launcher continues to generate significant interest. Originally conceived by Chemring Countermeasures to deliver accurate placement of countermeasures for anti-ship missile defence, the CENTURION launcher is now also being offered as a multi-role system, capable of deploying a wide range of additional effectors. These include acoustic decoys and short-range missiles.

Since the year end, Chemring Countermeasures, in collaboration with Raytheon Missile Systems, successfully conducted a first “proof of concept” by launching a Raytheon Javelin missile from the CENTURION launcher.

Underlying operating profit
£13.2m
 (2012: £20.4m)

Underlying operating margin
10.6%
 (2012: 12.5%)

Outlook

The outlook for the air countermeasures market is expected to remain challenging in the short term, with the decline in NATO procurement outpacing growth in non-NATO markets. While Chemring has sole-source qualified positions on the two major new platforms, Joint Strike Fighter and Typhoon, delays in aircraft deliveries and expected in-service dates will lead to the deferment of procurements of war reserves and training rounds for these fleets.

Encouragingly, these delays are driving capability extensions to existing platforms and there is heightened interest in Chemring's countermeasure products from non-NATO customers. There is also a growing capability gap in customers' naval countermeasures, with resulting interest in naval decoys and launchers. However, the timing of orders in the current tight budget environment remains uncertain.

While demand for countermeasures has fallen dramatically in recent years, the Group considers that it is now close to minimum sustaining volumes. This ensures that production lines can be maintained at a high state of readiness to quickly ramp-up output when new threats arise. Chemring's principal customers are maintaining some development effort to ensure their capability against the next generation of threats but until budgets recover, a material improvement in production volumes will be dependent upon the new aircraft programmes entering service.

SENSORS & ELECTRONICS

 See more information online
www.chemring.co.uk

Our business units:

Chemring Sensors & Electronic Systems – incorporating Non-Intrusive Inspection Technology (NIITEK) and Chemring Detection Systems – is the leading US manufacturer of vehicle-mounted ground penetrating radar mine detection systems, and the leading developer and supplier of vehicle-mounted chemical and biological detection systems.

Chemring Technology Solutions – incorporating Roke Manor Research and Chemring EOD – is a world class developer of detection, portable electronic warfare and network protection technologies. It also manufactures a range of products for detection, assessment and neutralisation of improvised explosive devices and unexploded ordnance.

Analysis

Revenue in the Sensors & Electronics segment was £211.3 million, 7.7% lower than the previous year, and was underpinned by ongoing fulfilment of the \$579 million multi-year HMDS ground penetrating radar indefinite delivery, indefinite quantity ("IDIQ") contract. The closing order book for Sensors & Electronics was £106.2 million, up 5.5% on 2012, as a result of major orders for HMDS and chemical and biological detection products.

Activities during the year

Chemring has integrated two US operations to create a single business unit – Chemring Sensors & Electronic Systems. This integration allows the Group to leverage its technology capabilities, co-ordinate customer interaction and maximise efficiencies within the supply chain.

Trading at Chemring Sensors & Electronic Systems was strong, and included completion of the initial \$161.3 million delivery order placed under the HMDS IDIQ contract. Orders totalling \$141.0 million were placed under this contract during the year, with these orders expected to be fulfilled in the period to May 2014. Encouragingly, the Group has continued to receive interest in its ground penetrating radar from other NATO countries, with sales to Australia, Italy, Turkey and Spain during the year.

During the year, Chemring Sensors & Electronic Systems and Chemring Australia were recognised in a prestigious Australian defence industry award for their work in helping to deliver Australia's protected route clearance capability. The award recognised the close relationship between defence and industry that is required to deliver complex military procurement projects in a timely and cost-effective manner.

The ground penetrating radar product range, which began with the large-scale HMDS, is expanding into smaller scale solutions designed to deliver capability to dismount troops. These solutions include a vehicle-mounted squad support unit designed for fast-moving infantry, an autonomous mine detection system mounted on a man-packable robot R-VISOR, and handheld ground penetrating radar and metal detector solutions. These solutions have continued to receive strong research and development funding from the US Department of Defense.

The HMDS programme has historically been funded as an Urgent Operational Requirement (UOR), driven by demand for Iraq and Afghanistan, but is currently transitioning into a long-term capability and is expected to be funded from the US Department of Defense's core budget through a Program of Record.

In October 2013, Chemring Sensors & Electronic Systems was awarded a \$10.6 million contract by the US Army for the procurement of six HMDS test systems. These will be used for advanced testing in preparation for a long-term HMDS procurement from base budget funds. This is a significant development, potentially securing the position of HMDS as a long-term capability for the US military. Both the R-VISOR robot-mounted ground penetrating radar and handheld detection solutions are also expected to transition to Programs of Record during 2014. The operational and logistical life cycle of these systems is expected to be over ten years. The ground penetrating radar technology used in these solutions is being augmented by additional capabilities, including sensors from Chemring Technology Solutions, to enhance performance.

Order book
£106.2m
 (2012: £100.7m)

Revenue
£211.3m
 (2012: £228.9m)

Internationally, all of the HMDS orders received this year have been delivered. Several countries deployed these systems into the current theatre of operations in the Middle East with great success. Additionally, after the Turkish Ministry of National Defence received its initial delivery of HMDS and R-VISOR systems, it is planning further expansion of this fleet. These systems, are now being used as an active detection solution for the Turkish forces in conflict zones. The initial Italian "Minebuster" systems are currently undergoing testing at multiple sites around Italy. Additionally, the South Korean Ministry of National Defense began trials on a robot-mounted mid-scale solution in late 2013.

Chemring Detection Systems also performed well during the year, and in January 2013, was awarded a \$28.5 million delivery order against a multi-year IDIQ contract to supply chemical detection systems to the US Army. This is the final order expected to be placed under the IDIQ. Later in the year, the US Army placed a further order worth \$25.2 million for the production and delivery of thirty two Joint Biological Point Detection Systems. These systems will be installed in the Stryker Nuclear Biological Chemical Reconnaissance Vehicle.

In the UK, Roke Manor Research and Chemring EOD have been integrated to create Chemring Technology Solutions, with the explosive ordnance disposal business reporting alongside Roke's three other sectors of defence, security and technology solutions. Chemring Technology Solutions had a favourable sales mix in the year, weighted towards higher-margin product sales and away from its historical focus on contract-based research and development activity.

The Resolve electronic warfare manpack system continues to attract interest from around the world. Development of the product range continues, in order to meet users' needs for lighter, yet more capable, systems and in September, a lightweight version designed specifically for on-the-march missions was launched. Weighing just ten kilograms, the lightweight manpack system fits into a standard daysack, delivering dismounted soldiers more flexible electronic warfare capabilities. A focused push on the Group's strategic electronic warfare capability is also delivering positive results, with sales of the Locate product into Europe.

Underlying operating profit
£44.7m
 (2012: £44.9m)

Underlying operating margin
21.2%
 (2012: 19.6%)

The Group is raising the profile and level of investment in non-defence products and technology, and a number of concepts are showing early promise. Efforts continue to diversify into commercial markets. The SmartSwitch product, which delivers a complete framework to optimise mobile data user experience and maximise operator profitability, has been tested by several global mobile network operators. Product evaluations indicate that SmartSwitch is a technically superior product and a front runner for significant opportunities in 2014.

Alongside product development, there have been successes in winning customer-funded development, with Chemring Technology Solutions delivering over £1 million of specialist development capability to major customers.

Outlook

The long-term outlook for Sensors & Electronics is robust. Many countries acknowledge a significant and growing gap in their capabilities to deal with the persistent and rapidly evolving threat of IEDs. This is resulting in sustained interest in Chemring's detection, jamming and defeat products from both NATO and non-NATO markets.

Other programmes, such as the Stryker reconnaissance vehicle, will complete during 2014. The focus is therefore on investing in technology to ensure a strong position on new programmes as they arise. The Group will continue to invest and develop new detection offerings, including handheld and robot-mounted variants. There also continues to be significant interest in the Group's electronic warfare, security and cyber security solutions.

PYROTECHNICS & MUNITIONS



See more information online
www.chemring.co.uk

Our business units:

Simmel Difesa – a leading Italian-based supplier of naval ammunition, advanced fusing technology and missile components.

Mecar – a niche Belgian-based supplier of medium and large-calibre ammunition for light armoured vehicles.

Chemring Defence – incorporating Chemring Defence UK and Chemring Defence Germany – designs, develops and produces smoke and illumination pyrotechnics and payloads for military, OEM and safety customers.

Chemring Ordnance – a leading US manufacturer of military training pyrotechnics and ammunition for 40mm grenade launchers.

Analysis

Pyrotechnics & Munitions revenue was £200.6 million, a 19.6% reduction from 2012. This reduction was partially a consequence of mortar system delivery delays. The closing order book for Pyrotechnics & Munitions was £315.5 million, a reduction of 9.9%. Order intake included a \$42.1 million contract for the procurement and supply of non-standard ammunition for the US Government.

Activities during the year

A significant focus in Pyrotechnics & Munitions has been on enhancing operational performance and optimising routes to market, whilst developing a coherent and comprehensive product catalogue. These activities have started to deliver results. At Chemring Ordnance, the Anti-Personnel Obstacle Breaching System (APOBS) production line has been enhanced, resulting in improved gross margins. The overall staffing and facilities layout at Chemring Ordnance has also been revised, to raise efficiency and throughput.

At Simmel, a significant improvement in production efficiency has resulted from selective automation of processes and a general revision of layout and processes. This has resulted in greater than 20% cost savings on our naval ammunition packing lines.

Technology refreshments have also been used to improve margins, exemplified by the development of new micro-electronics for proximity fuzes, resulting in a 6% gross margin improvement for these products.

Naval

The naval ammunition market remains stable, with revenue at similar levels to 2012. However, order intake has been disappointing due to delays in receipt of significant orders from non-NATO customers, although the Group is confident of receiving these orders during 2014. Nonetheless, the Group received several orders from Middle Eastern customers and grew the level of naval munitions business with the NATO Support Agency.

In furthering market reach, Simmel has signed an agreement with a Turkish partner for the technology transfer of naval munitions. Initial activities will be focused on 40mm L70 munitions for the domestic market and selected export countries, mainly in the Caucasus area. Negotiations are also ongoing with a customer for the establishment of a co-production capability in the Middle East.

Land ammunition

Integration of the first turreted mortar system was completed during the year, and Mecar is working towards additional orders for these systems. Sales of munitions continued at historic levels, the majority of which were to strategic Middle Eastern customers. Whilst order intake was disappointing in numerical terms, this was due solely to the delay in receipt of a single strategic order, due to the customer's reassessment of requirements. This order is anticipated within the next quarter. The Group remains in a very strong position to exploit opportunities in the Egyptian marketplace when export licence approval activity resumes.

In seeking to develop its market presence, Chemring has signed a number of strategic agreements focused on technology sharing, co-production and joint marketing.

Order book
£315.5m
 (2012: £350.1m)

Revenue
£200.6m
 (2012: £249.5m)

**Underlying
operating profit**
£13.0m
 (2012: £21.2m)

**Underlying
operating margin**
6.5%
 (2012: 8.5%)

Mecar has signed agreements with Burkan in the UAE, and with Emgepron in Brazil, to have Mecar products assembled in-country for local market needs. The agreement with Emgepron puts Mecar in a strong position to meet the current 105mm tank and future 105mm light armoured vehicle (LAV) ammunition requirements, and provides a base to service other South American requirements. Following the signing of a strategic agreement with ATK, Mecar will complete the development of the 30mm APFSDS-T and 120mm HEP rounds in 2014, to increase its product portfolio in two new calibres.

During 2013, development of the 120mm mortar red phosphorus smoke round was completed, and the first production delivery will take place in 2014. Work has also now commenced on an improved 90mm MK8 TPFSDS round for the Belgian Army, which has a fleet of forty 90mm-armed LAVs.

Deliveries of 81mm mortar ammunition to NATO customers continued at a steady pace. However, the withdrawal of troops will result in a slowdown in requirements. The business is therefore actively pursuing opportunities in new markets for this product range.

Chemring Ordnance finished the year with strong order intake, exceeding its order forecast by over 50%. The order improvement was helped significantly by capturing a \$42 million non-standard ammunition contract for the US Government.

Outlook

The outlook for Pyrotechnics & Munitions is mixed. NATO demand is reducing but this is being offset by Chemring's leading positions in naval ammunition and certain large-calibre tank and armoured vehicle munitions. The Group will leverage its position in non-NATO markets, particularly where customers are building up national capabilities with new armoured vehicle fleets.



Pictured:
A paratrooper mortar platoon team fires 81mm shells in support of a patrol in Afghanistan. (Crown Copyright)

ENERGETIC SUB-SYSTEMS

 See more information online
www.chemring.co.uk

Our business units:

Chemring Energetic Devices – incorporating Chemring Energetic Devices and Hi-Shear Technology Corporation – is a leading US supplier of pyrotechnic and electromechanical systems for space, safety and military training applications.

The business is a leading supplier of space-qualified initiators and low-shock satellite separation systems, and a range of pyromechanisms for aircrew egress. It also develops advanced sub-systems for ballistic missile defence and tactical weapons.

Chemring Energetics – incorporating Chemring Energetics UK and Chemring Nobel in Norway – is a leading supplier of detonators, actuators, rocket motors, high explosive filling, canopy cutting cords and pyromechanisms for safety and aircrew egress, and demolition stores for the UK Ministry of Defence. It is also a leading supplier of high explosives and energetic binders to the defence, security, oil and gas industries.

Analysis

Energetic Sub-Systems revenue was £88.0 million, a 10.8% reduction from 2012. This was mainly as a result of the reduction in defence spending in the US and UK. The closing order book for Energetic Sub-Systems was £93.0 million, a reduction of 3.9%.

Activities during the year

The Group is integrating Hi-Shear with Chemring Energetic Devices to exploit common technology and production synergies. This integration is resulting in common systems and processes, which will facilitate better management of the operations. In addition, the integration is improving the loading of production facilities to alleviate manufacturing bottlenecks, and has resulted in a more co-ordinated sales force. The combined business will be better able to leverage volume and integrate technology development plans, while also having a streamlined management structure. The combined portfolio of defence and non-military customers provides an opportunity for future growth.

In December 2013, the conditional sale of Chemring Energetic Devices' business based in Clear Lake, South Dakota was agreed. The gross sales proceeds will be \$10.0 million (£6.1 million), subject to a working capital adjustment.

Chemring Nobel had its best ever revenue year, whilst further developing the site and its processes to ensure business continuity at this level. This business continues to develop its portfolio of products to suit the oil and gas industry, as well as the defence primes.

Chemring Energetics UK has successfully commissioned its state-of-the-art primary explosive remote manufacturing facility, built to replace an old labour-intensive facility. Product from the facility is now being qualified with customers.

Safety systems

Chemring Energetic Devices successfully qualified product on the Digital Recovery Sequencer, a new product that will generate sales every year from the US Air Force and international customers. Chemring Energetic Devices also won a product improvement programme for the US Air Force B-1B bomber ejection system components that will increase profitability from the manufacturing improvements. Additionally, the business received international orders for fourteen JCAST pilot flight gear testers, and completed qualification and received the first production order for the safe and arm fuze used on Lockheed Martin's smart version of the 2.75 inch Hydra missile.

Chemring Energetics UK continues to be the sole supplier of energetic material for Martin Baker Aviation ejection systems.

Order book**£93.0m**

(2012: £96.8m)

Revenue**£88.0m**

(2012: £98.7m)

Underlying operating profit**£11.3m**

(2012: £12.3m)

Underlying operating margin**12.8%**

(2012: 12.5%)

Space

Chemring Energetic Devices was awarded a \$5 million contract to produce the fore and aft thrusters used to separate the side-mounted booster modules on the Atlas V heavy lift launch vehicle. Hi-Shear was awarded a contract to develop a new standard initiator for NASA's Orion project.

Chemring Energetics UK is developing lead-free explosive cords for the European space market, which will be a move into a new sector for the business.

Missiles

Hi-Shear's newly developed and qualified electronic safe and arm fuze for the Missile Segment Enhancement programme nearly doubles the existing Patriot Advanced Capability missile performance envelope. The missile has successfully completed all flight qualification testing. Raytheon Missile Systems awarded a sole-source contract for the manufacture and future qualification of an ejector line cutter to be used on the US Navy's SM3-Blk2A ballistic missile defence missile. In the next phase of the programme, this cutter and its power cartridge will undergo a series of qualification tests to meet the US Navy's stringent performance requirements.

The Group has secured its position on a number of missile and space programmes, and its sole-source position on a number of programmes secures a good level of base activity.

Chemring Energetics UK has continued to work on its major contract for components for the Next Generation Light Anti-Tank Weapon. Sales under this contract have been delayed due to technical performance issues, and the business continues to work with its partners on the programme to complete delivery of its obligations.

Civil aerospace

Chemring Energetics UK has been selected and is supplying product into the safety system for the Boeing Dreamliner. The product has been qualified in the aircraft oxygen release system.

Demolition stores

In the UK, Chemring Energetics secured a £9.9 million contract to supply the UK Ministry of Defence with plastic explosive for a four year period commencing in April 2014. This contract strengthens Chemring's position as a leader in the supply of demolition products to the military. The contract was won after Chemring Energetics UK took part in the UK Ministry of Defence's competitive tendering process that started in July 2012.

A derivative of the SABREX family of flexible and explosively-efficient linear cutting charges has been successfully developed for the US Navy, and this is expected to generate more interest in this product from other areas of the US Department of Defense.

Outlook

The Energetic Sub-Systems segment is expected to be relatively flat in the near term. Growth will be generated by diversification into non-defence markets, with the development of bespoke products for fire suppression, security and space applications. Defence requirements will continue to reduce within NATO and emphasis will therefore be on securing positions in emerging markets, particularly the Middle East and Far East.

CEO questions and answers

Q: Given recent problems and the uncertainty in Chemring's traditional markets, what changes have you made to ensure the business is more resilient in the future?

A: We have achieved a great deal this year and made significant progress in realigning the business with the realities of the constrained defence spending environment that we are operating in, whilst also working hard to ensure that we have the correct management and reporting structures in place to more effectively drive business development across the Group. Under the Performance Recovery Programme, we have simplified the Group structure to become more coherent and integrated.

Operational performance has improved as a result, with new measures put in place to manage capacity, reduce waste, and ensure consistent quality in our products. In tandem, we've focused sharply on cash and cost management, with a culture of stringent cost awareness now embedded across the Group. The business is more streamlined and, importantly, resilient to market dynamics; the restructuring, office closures and reduction in headcount will realise savings of £10.0 million per annum from 2014. These operational changes will allow us to be more flexible and respond to changes in demand, whilst putting in place a stable foundation for the future.

Q: How has Chemring been affected by the spending cuts in the US caused by sequestration and the shutdown of the US Government at the beginning of October?

A: Spending cuts and uncertainty in the US have undoubtedly created testing conditions for all defence companies and we are no different. The US Government shutdown in October resulted in the closure of a large number of government departments. This included the Defense Contract Management Agency, the government agency with responsibility for inspecting and approving products for delivery to the US Department of Defense. This was extremely frustrating since it impacted on our October 2013 deliveries

to the US Department of Defense in the final few weeks of the financial year, and made it necessary for us to bring down market expectations.

Unpredictable events such as this have meant that we have had to adapt our business and have budgeted accordingly for 2014. It is prudent to assume that the effects of the US defence spending cuts will adversely affect Chemring during the coming year, although I would highlight that the US is still prioritising defence electronics spending and, as a result, we continue to see robust levels of demand for our Sensors & Electronics products.

Q: How well is Chemring placed to benefit from opportunities in non-NATO markets given the cuts to the US defence budget?

A: Non-NATO markets do represent an opportunity for Chemring and already account for over 25% of total Group revenues, through sales in more than twenty countries. However, they are not an instant remedy to the difficulties in our traditional markets: doing business in these geographies brings with it various cultural, political and commercial issues that aren't present in the US, UK and Europe.

Q: When do you envisage a return to more encouraging trends in the defence market?

A: The defence sector is dependent on so many external, non-cyclical factors that this is very difficult to predict. We expect US, UK and European markets to remain subdued in 2014 and 2015, with visibility continuing to be limited, particularly in the US. However, we are starting to see signs that the UK defence budget is stabilising, and are seeing key export markets such as the Middle East, India and Brazil

"We have achieved a great deal this year and made significant progress in realigning the business. Despite the headwinds we are facing in our core markets, I am optimistic about the Group's long-term prospects."

Mark Papworth, Chief Executive



continue to grow. Although US defence spending is likely to remain under pressure in the medium term, we are expecting a return to top-line budget growth there from 2016 onwards. In the meantime, there is much we can do by way of self-help to ensure Chemring's performance keeps improving, regardless of wider market trends that are, frankly, outside of our control.

Q: What are your priorities for 2014?

A: We have made good progress in our work to transform the way in which Chemring operates, and we will continue this during 2014, ensuring these changes are properly bedded-in and our integration programmes are complete. We will also focus on leveraging business development opportunities that the new Group structure engenders, including exploring non-military applications of our technology and increasing our presence in growing markets. We know that we have work to do to restore investor confidence given the issues of recent years. However, the recently completed Strategic Planning Process has confirmed the Group's market-leading positions and the strength of its technology in a number of areas. It also highlighted new defence and adjacent non-defence opportunities that the Group has yet to exploit. We have great people and technologies at Chemring, and there is much to aim for in 2014 and beyond.

Q: What is your longer term strategy for the business?

A: In November, we announced that we had concluded that there are a number of businesses within the Group which do not form part of the longer-term business strategy, and that we had started a process to divest of certain of these businesses. Our strategy is to reposition the portfolio for future growth through technology exploitation. We will focus on our core competencies, directing investment into those lines of business which have technologies, products and market positioning that provide opportunities to achieve sustainable high margins and revenue growth.

Q: In which geographies, markets and products do you see the best opportunities?

A: We've already identified opportunities to move beyond our traditional markets through the Performance Recovery Programme, and the Strategic Planning Process takes this further. As things stand, we think there is good potential to expand sales of our Sensors & Electronics products outside the US and the UK. These products are subject to preferential spend in many countries and we have well-established, market-leading technologies that will help us capitalise on

that. Non-NATO markets are obviously also a priority; we are particularly enthusiastic about India, a market where defence spending is set to double by 2017.

The Middle East is another region where we have identified positive trends in defence budgets, with Saudi Arabia particularly keen to invest in security.

Q: Have you been able to preserve the Group's safety record despite integrating businesses and reducing costs?

A: We are committed to ensuring the safety of all our employees, customers and the general public. This is ingrained in our Code of Business Principles, and the commitment of all management and staff to upholding them has remained undimmed by our restructuring programme. Integrating different businesses understandably brings challenges, but the creation of a safe working environment has been a priority in every instance. We've invested substantially in robotics and automated processes to protect employees working with volatile materials as part of a continual programme of improvements.

Q: How have you found your first full year in the job?

A: It's fair to say that things have been challenging but that is no less than I expected, given the well-documented issues that Chemring was facing when I arrived. The backdrop of constrained defence spending in the US is clearly affecting all defence companies at the moment but I have to admit that I was surprised by just how much room for improvement there was in terms of Chemring's operational capabilities. This gives us a great opportunity to turn the business around and we have already started to see some tangible benefits from the actions we have undertaken. Chemring has some excellent businesses with strong positions in markets that hold significant potential for the Group so, despite the headwinds we are facing in our core markets, I am optimistic about the Group's long-term prospects.

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Financial highlights

- Revenue from continuing operations down 15.6% to £624.9 million
- Underlying profit before tax £52.4 million
- Underlying operating margin 11.5% (2012: 11.9%)
- Underlying operating cash inflow £68.6 million

Group results

An analysis of underlying and total results is set out below:

	2013 Underlying £m	2013 Total £m	2012 Underlying £m	2012 Total £m
Revenue	624.9	624.9	740.3	740.3
Segmental operating profit/(loss)	82.2	(26.8)	98.8	47.5
Unallocated corporate costs	(10.1)	(10.1)	(10.5)	(10.5)
Operating profit/(loss)	72.1	(36.9)	88.3	37.0
Share of profit after tax of associate	–	–	0.1	0.1
Finance income	0.2	0.2	0.1	0.1
Finance expense	(19.9)	(19.9)	(18.4)	(18.4)
Profit/(loss) before tax	52.4	(56.6)	70.1	18.8
Tax	(10.6)	9.1	(15.1)	(5.6)
Profit/(loss) after tax	41.8	(47.5)	55.0	13.2

Results shown above are for continuing operations and exclude the results of the marine business, which was sold in July 2012. Underlying measures referred to are stated before costs relating to acquisitions and disposals, business restructuring and incident costs, profit on disposal of businesses, items deemed to be of an exceptional nature, impairment of goodwill and acquired intangibles, impairment of assets held for sale, amortisation of acquired intangibles and gains/losses on the movement in the fair value of derivative financial instruments.

A reconciliation of underlying and total operating profit is set out in note 5 of the group financial statements.

During the year, changes in foreign exchange rates, principally the depreciation of sterling against the US dollar, increased reported revenues by £8.0 million. At constant exchange rates, revenue was £616.9 million, a reduction of 16.7%.

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

	Revenue £m	Underlying operating profit* £m	2013 Underlying operating margin %	Revenue £m	Underlying operating profit* £m	2012 Underlying operating margin %
Countermeasures	125.0	13.2	10.6	163.2	20.4	12.5
Sensors & Electronics	211.3	44.7	21.2	228.9	44.9	19.6
Pyrotechnics & Munitions	200.6	13.0	6.5	249.5	21.2	8.5
Energetic Sub-Systems	88.0	11.3	12.8	98.7	12.3	12.5
Segment results	624.9	82.2	13.2	740.3	98.8	13.3
Unallocated corporate costs		(10.1)			(10.5)	
		72.1	11.5		88.3	11.9

Countermeasures revenue decreased by 23.4%, due to lower demand from the UK and US as a result of the continuing withdrawal from Afghanistan. In the US, volumes were also impacted by ongoing production delays caused by operational quality issues, most notably at Kilgore. However, the extent of these delays began to reduce towards the end of the year, due to the focus on operational improvements. Included within the results is revenue arising from the contract for the supply of aircraft countermeasures to a customer in the Middle East that was highlighted in the 2012 annual report.

Despite headcount reductions and other measures taken to improve efficiency, operating margins decreased to 10.6% (2012: 12.5%), reflecting the high fixed-cost base of the countermeasures production facilities. Development of the advanced countermeasure highlighted in the 2012 annual report is ongoing, with further customer trials due to be conducted in 2014.

Sensors & Electronics revenue reduced by 7.7% to £211.3 million (2012: £228.9 million), despite strong sales of HMDS to the US Department of Defense and growing sales in other markets. Operating margins increased to 21.2% (2012: 19.6%), reflecting the release of contingencies held back prior to customer acceptance of the first delivery order for the HMDS under the IDIQ contract. In addition, the sales mix at Chemring Technology Solutions was weighted toward higher margin product sales.

Pyrotechnics & Munitions revenue reduced by 19.6% to £200.6 million (2012: £249.5 million), due to lower activity levels resulting from order deferrals by a number of customers. Underlying operating profit decreased by 38.7% to £13.0 million (2012: £21.2 million). Operating margins were impacted by an adverse sales mix, notably lower demand for illumination products, and by the high fixed-cost nature of the munitions facilities. Deliveries on the Group's contract for the supply of vehicle-based mortar systems recommenced in the final quarter of the year, following the resolution of export licence and customer acceptance issues.

Energetic Sub-Systems revenue reduced to £88.0 million (2012: £98.7 million), with deliveries constrained by production issues at Chemring Energetic Devices in the US. Demand from the major customers of the Group's UK operation, including the UK Ministry of Defence, was also lower. Operating profit of £11.3 million (2012: £12.3 million) resulted in an operating margin of 12.8% (2012: 12.5%). Margins benefited from a reduction in sales of lower margin build-to-print products manufactured at the Clear Lake facility, for which a conditional sale agreement was signed in December 2013.

Unallocated corporate costs were £10.1 million (2012: £10.5 million), reflecting an element of the savings from the simplification of the Group's management structure and the closure of administrative offices in the UK and US.

As a result of these factors, the Group's underlying operating profit was £72.1 million (2012: £88.3 million), a decrease of 18.3%. The underlying operating margin was 11.5% (2012: 11.9%).

The total operating loss was £36.9 million (2012: £37.0 million profit). This loss is principally due to the higher level of non-underlying costs of £109.0 million (2012: £51.3 million) which are discussed below.

Net finance expense was £19.7 million (2012: £18.3 million). Included within finance expense is £0.5 million (2012: £0.8 million) in respect of retirement benefit obligations.

Underlying profit before tax was £52.4 million (2012: £70.1 million), a decrease of 25.2%. Including non-underlying items, the total loss before tax was £56.6 million (2012: £18.8 million profit).

Tax on underlying profit before tax was £10.6 million (2012: £15.1 million), representing an effective tax rate of 20.2% (2012: 21.5%). The tax rate is comparable to the UK corporation tax rate, and benefits from the utilisation of research and development tax credits, together with the recognition of certain tax losses within the Pyrotechnics & Munitions segment. The effective tax rate on the total loss before tax was 16.1% (2012: 29.8%), due to the higher proportion of non-underlying costs in the total result.

Underlying profit after tax was £41.8 million (2012: £55.0 million), a decrease of 24.0%. Including non-underlying items, the total loss after tax was £47.5 million (2012: £13.2 million profit).

Analysis of non-underlying items

The use of underlying measures, in addition to the total measures noted above, is considered by the Board to improve comparability of business performance between periods and, in line with past practice, certain items are classed as non-underlying as set out below:

	2013 £m	2012 £m
Acquisition and disposal related costs	3.2	8.2
Business restructuring and incident costs	11.7	11.9
Profit on disposal of business	–	(10.3)
Impairment of goodwill	50.9	22.5
Impairment of acquired intangibles	15.7	–
Impairment of assets held for sale	8.8	–
Intangible amortisation arising from business combinations	18.8	20.9
Gain on fair value movements on derivatives financial instruments	(0.1)	(1.9)
Total non-underlying items	109.0	51.3

Acquisition and disposal related costs of £3.2 million include £2.1 million in respect of a one-off provision relating to an onerous lease for a business sold in 2003. Business restructuring and incident costs of £11.7 million include costs relating to the major simplification of Chemring's management structure (£4.4 million) and business unit integration and restructuring (£5.5 million) that has been completed as part of the Performance Recovery Programme.

The profit on disposal of business in the prior year related to the sale of the Group's marine business in July 2012.

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Following a detailed review, goodwill relating to Hi-Shear of £50.9 million has been fully impaired as a result of lower expectations of future trading performance. In addition, an impairment of £15.7 million of acquired intangibles has been recognised in relation to Chemring Energetic Devices' Clear Lake facility, due to a decline in the market for its build-to-print products. In 2012, the goodwill impairment of £22.5 million related to Chemring Ordnance (£6.8 million) and Chemring Energetic Devices (£15.7 million). Impairment analysis is based on value-in-use calculations, with the impairments being primarily driven by business valuations negatively impacted by the challenging conditions facing the defence industry.

In December 2013, conditional agreement was reached for the sale of Chemring Energetic Devices' Clear Lake facility. Assets and liabilities relating to Clear Lake have been classified as held for sale at 31 October 2013, incurring a further impairment charge of £8.8 million.

The amortisation of intangible assets arising from business combinations was £18.8 million (2012: £20.9 million), with the decrease reflecting the fact that certain intangible assets are now fully amortised. This amortisation is treated as non-underlying to improve comparability and understanding of the results given its large size and its non-cash nature.

Shareholder returns

Underlying basic earnings per share were 21.6p (2012: 28.5p), a decrease of 24.2%. There was a basic loss per share of 24.6p (2012: 6.8p earnings per share).

The total dividend per share of 7.2p (2012: 9.5p) is covered 3.0 times (2012: 3.0 times) by underlying earnings per share.

Shareholders' funds at the year end were £383.8 million (2012: £433.5 million).

Pensions

The deficit on the Group's defined benefit pension schemes, as defined in IAS 19 (Revised) *Employee Benefits*, was £25.1 million (2012: £27.0 million). This principally relates to the Chemring Group Staff Pension Scheme (the "Scheme"), a UK defined benefit scheme whose assets are held in a separately administered fund. The Scheme was closed to future accrual in April 2012. A full actuarial valuation for the Scheme as at 6 April 2012 has been prepared and updated to 31 October 2013, using the projected unit credit method.

The actuarial valuation of the Scheme at 31 October 2013 showed a deficit of £24.2 million, compared to a deficit of £25.9 million in the prior year. Following discussions with the Scheme's trustees, a new funding structure has been agreed. This replaces the previous £20.0 million lump sum funding commitment, which would have fallen due for payment in June 2014, with contributions of £8.2 million in the year to 31 October 2014 and £5.0 million annually thereafter. The Group has given a bank guarantee and letters

of credit totalling £27.2 million (2012: £27.2 million) to the Scheme in respect of future contributions payable. Of these commitments, £20.0 million will progressively reduce as contributions are paid to the Scheme under the new funding structure.

Chemring will implement amendments to IAS 19 (Revised) *Employee Benefits* in its financial statements for the year ending 31 October 2014, and while there will be no resulting cash effect, the net interest cost associated with retirement benefit obligations is expected to increase by approximately £0.9 million per annum.

Chemring's UK employees are now offered membership of a defined contribution pension scheme. The majority of the Group's overseas pension arrangements are also defined contribution, save in those European countries where certain defined benefit pension arrangements are required.

Research and development

Research and development expenditure was £46.0 million (2012: £59.0 million). The reduction primarily reflects a lower level of customer-funded development projects. Continued investment in research and development is a key aspect of the Group's Performance Recovery Programme, and internally-funded research and development is expected to increase in 2014 as investment is made in product development, particularly within Sensors & Electronics. An analysis of research and development expenditure is set out below:

	2013 £m	2012 £m
Customer-funded research and development	27.1	34.4
Internally-funded research and development		
– expensed to the income statement	11.5	12.3
– capitalised	7.4	12.3
Total research and development expenditure	46.0	59.0

Amortisation of development and patent costs in the year was £5.9 million (2012: £4.6 million), reflecting a number of previously capitalised projects coming on-stream.

Cash flow

Underlying continuing operating cash flow was £68.6 million (2012: £114.9 million).

A summary of underlying Group cash flow from continuing operations is set out below:

	2013 £m	2012 £m
Underlying continuing operating profit	72.1	88.3
Depreciation and loss on disposal of fixed assets	22.3	19.1
Amortisation of development costs, patents and licences	5.9	4.6
Underlying continuing profit, before interest, depreciation and amortisation	100.3	112.0
(Increase)/decrease in working capital	(31.3)	19.9
Other movements	(0.4)	(17.0)
Underlying operating cash flow	68.6	114.9
Fixed asset expenditure	(19.7)	(41.1)
Tax	(0.5)	(6.1)
Interest	(20.4)	(23.8)
Underlying free cash flow	28.0	43.9

Expenditure on property, plant and equipment and capitalised development projects was £19.7 million (2012: £41.1 million). This includes £1.5 million (2012: £6.9 million) associated with the construction of new facilities at the Group's countermeasures sites in the UK and Australia. Other expenditure comprised numerous projects including health and safety related projects, to upgrade electricity supplies and automate production.

Tax payments were £0.5 million (2012: £6.1 million), reflecting the lower profits of the Group, receipt of refunds in respect of prior periods and timing of payments.

Interest payments reduced due to a lower level of gross debt during the year.

Working capital

A summary of working capital is set out below:

	2013 £m	2012 £m
Inventories	113.7	113.8
Trade receivables	76.2	90.9
Contract receivables	104.8	87.6
Trade payables	(62.8)	(100.2)
Advance payments	(17.4)	(11.7)
Accruals and deferred income	(48.9)	(45.6)
Other items	(40.0)	(41.5)
Total working capital	125.6	93.3

During September and October 2013, deliveries to customers in the Middle East were delayed due to constraints in available shipping capacity. Working capital at 31 October 2013 was higher as a consequence of these delays; however, this impact has largely unwound during the first quarter of the current financial year. Working capital has also risen due to a reduction in trade payables, reflecting a more sustainable approach towards creditor management. Contract accounting continues to be applied where appropriate, and contract accounted revenues represented 38% (2012: 37%) of total revenue.

The Group's working capital is a key focus area for management, and initiatives have been implemented to raise working capital efficiency, notably through the reduction of inventories and contract receivables. Working capital is expected to reduce during 2014, although the profile of certain major contracts is now expected to lead to this reduction being weighted towards the second half of the current financial year.

Net debt, facilities and going concern

Net debt at 31 October 2013 was £248.7 million (2012: £244.8 million). The Group had £126.8 million (2012: £143.9 million) of undrawn borrowing facilities at the year end.

The Group's debt facilities include a £230.0 million revolving credit facility with a syndicate of five banks. The facility, which is unsecured, provides both trade finance and funds for general working capital purposes. The term of this facility is to April 2015, with an option to extend for twelve months. In practice, it is intended that the facility will be refinanced during 2014.

In addition to the revolving credit facility, the Group has fixed interest loan notes in the US, repayable in November 2016 (\$80.0 million), November 2017 (£12.5 million and \$125.0 million), and November 2019 (\$200.0 million). The Group continues to have positive relationships with all its debt providers.

The Group is subject to two key financial covenants, which are tested quarterly, relating to the leverage ratio between underlying earnings before interest, tax, depreciation and amortisation ("underlying EBITDA") and debt, and the interest cover ratio between underlying EBITDA and finance costs. The revolving credit facility and the loan notes have differing covenant compliance calculations, with the primary difference being that the revolving credit facility uses consolidated net debt in calculating the leverage ratio, whereas the loan notes use total gross debt. In June 2013, Chemring successfully concluded a revision of financial covenants with its debt providers. In respect of the revolving credit facility, the maximum permitted ratio of net debt to underlying EBITDA was increased to 3.50 times at the April and July 2013 testing dates, and then reduced to 3.25 times at the October 2013 and January 2014 testing dates, before reverting to 3.00 times thereafter. The basis of calculation of this ratio was also amended so as to translate non-sterling denominated

Financial review

debt using average, rather than closing, rates of exchange. In respect of the loan notes, the permitted ratio of debt to underlying EBITDA was increased to 3.50 times for the four quarters mentioned above before reverting to 3.00 times thereafter, with this covenant continuing to be based upon total gross debt. This covenant also uses average exchange rates.

The Group complied with these covenants throughout the year, and this compliance is expected by the directors to continue for the foreseeable future. The result of the covenant tests at the year end are detailed below:

	2013	2012
Covenant ratios – revolving credit facility		
Maximum allowed ratio of consolidated net debt to underlying EBITDA	3.25x	3.00x
Actual ratio of consolidated net debt to underlying EBITDA	2.65x	2.14x
Minimum allowed ratio of underlying EBITDA to finance costs	4.00x	4.00x
Actual ratio of underlying EBITDA to finance costs	4.98x	6.71x
Covenant ratios – loan note agreements		
Maximum allowed ratio of consolidated total debt to underlying EBITDA	3.50x	3.00x
Actual ratio of consolidated total debt to underlying EBITDA	2.78x	2.79x
Minimum allowed ratio of underlying EBITDA to finance costs	3.50x	3.50x
Actual ratio of underlying EBITDA to finance costs	5.61x	6.86x

The composition of gross and net debt is set out below:

	2013 £m	2012 £m
Loan notes	(259.1)	(261.2)
Revolving credit facility	–	(71.1)
Other loans and finance leases	(3.8)	(8.5)
Gross debt	(262.9)	(340.8)
Cash	14.2	96.0
Net debt	(248.7)	(244.8)

The Group's level of debt, and therefore leverage, reflects the historic development of the Group through acquisition, together with the effect of growth in working capital and the substantial investment in production capacity. The Group continues to work towards a sustained reduction in debt through consistent conversion of operating profit to operating cash flow.

As part of their regular assessment of the business working capital and financing position, the directors have prepared a detailed trading budget and cash flow forecast for a period which covers at least twelve months after the date of approval of the financial statements. In assessing the forecast, the directors have considered:

- Trading risks presented by the current economic conditions in the defence market, particularly in relation to government budgets and spends.
- The impact of macroeconomic factors, particularly interest rates and foreign exchange rates.
- The status of the Group's financial arrangements and associated covenant requirements.
- Progress made in developing and implementing outcomes from the Strategic Planning Process, including the implications of disposing of businesses which do not form part of the Group's longer-term strategy.
- Mitigating actions available should business activities fall behind current expectations, including the deferral of discretionary overheads and restricting cash flows, together with the potential to dispose of non-core operations.

The long-term nature of the Group's business, taken together with the Group's order book, provide a satisfactory level of confidence to the Board in respect of trading.

The directors have acknowledged the latest guidance on going concern. They have made appropriate enquiries and taken into account factors which are detailed in the strategic report. As a consequence, the directors believe that the Company is well placed to manage its risks. Further details on the covenants are set out in note 24 of the group financial statements, which also details how the Group manages its liquidity risk.

Whilst the current volatility in financial markets has created general uncertainty, the Group continues to have working capital headroom. The Group has been in compliance with its revolving credit facility and loan note covenants throughout 2013 and is forecast to be in compliance for the coming twelve months. Additional sensitivity analysis has been prepared with a focus on the April 2014 covenant test date, when the permitted leverage ratios revert to 3.00 times, to consider the impact of a reduction in forecast EBITDA. This sensitised scenario includes identified mitigating actions that can be taken if needed and, based on the application of these, shows headroom on all covenant test dates. The directors, having considered the forecasts, the risks and associated mitigating actions, have a reasonable expectation that adequate financial resources will continue to be available for the foreseeable future. Thus, they continue to adopt the going concern basis in preparing the financial statements.

Key performance indicators

The Group's strategy is underpinned by focusing on a number of key performance indicators. The key indicators that the Board and senior management utilise to assess Group performance are set out below. Similar indicators are used to review performance of each of the Group's businesses, albeit that the exact nature of these varies between business units to reflect the differing nature of their operations.

Orders

The Group uses a number of key performance indicators relating to orders. These comprise order intake, order book and the level of order coverage for the balance of the current financial year. Details of order intake and order book by segment are as set out below:

	Order intake		Order book	
	2013 £m	2012 £m	2013 £m	2012 £m
Countermeasures	80.7	106.3	160.8	213.3
Sensors & Electronics	212.3	256.2	106.2	100.7
Pyrotechnics & Munitions	157.3	203.0	315.5	350.1
Energetic Sub-Systems	84.2	94.7	93.0	96.8
Group	534.5	660.2	675.5	760.9

The closing order book at 31 October 2013 of £675.5 million represents a 11.2% decrease on the prior year, reflecting the budget constraints which continue to affect the group's principal NATO markets and the deferral of order placement decisions in a number of non-NATO markets. As at 31 October 2013, of the orders on hand of £675.5 million, £477.7 million were for delivery in the year ending 31 October 2014.

Segmental underlying operating profit

	2013 £m	2012 £m
Countermeasures	13.2	20.4
Sensors & Electronics	44.7	44.9
Pyrotechnics & Munitions	13.0	21.2
Energetic Sub-Systems	11.3	12.3
Group	82.2	98.8

Segmental underlying operating profit is stated before charges for unallocated corporate costs and non-underlying items, as shown in note 6 to the group financial statements. Segmental underlying operating profit provides a consistent year-on-year measure of the trading performance of the Group's operations. It does not include significant non-recurring or exceptional costs that would distort a comparative assessment, nor does it include unallocated corporate costs associated with operating a public company. The segmental underlying operating profit decreased by 16.8% during the year, reflecting the reduction in revenue and the operating leverage effects associated with the high fixed-cost nature of certain of the Group's activities.

Underlying operating margin

	2013 %	2012 %
Countermeasures	10.6	12.5
Sensors & Electronics	21.2	19.6
Pyrotechnics & Munitions	6.5	8.5
Energetic Sub-Systems	12.8	12.5
Group	11.5	11.9

Operating margin is based on underlying segmental operating profit and provides an assessment of the profitability of the business. A focus on operating margin allows the impact of changes in revenue and cost base to be monitored, enabling comparisons to be made of management performance and trading effectiveness. The changes in margin of each segment reflect the weak market conditions, volume changes and performance improvement actions, as set out in this strategic report.

Underlying earnings per share

	2013	2012
Total	21.6p	28.5p
Change on previous year	(24.2)%	(43.0)%

Underlying earnings per share is a key measure for the Group, reflecting the combined trading performance together with the impact of funding structure and taxation. The decrease in the year reflects the Group's trading performance in difficult market conditions.

Debt to underlying EBITDA

	2013	2012
Revolving credit facility		
Actual ratio of consolidated net debt to underlying EBITDA	2.65x	2.14x
Maximum allowed ratio of consolidated net debt to underlying EBITDA	3.25x	3.00x
Loan note agreements		
Actual ratio of consolidated total debt to underlying EBITDA	2.78x	2.79x
Maximum allowed ratio of consolidated total debt to underlying EBITDA	3.50x	3.00x

The ratio of underlying EBITDA generated by trading to the Group's debt levels is a clear indicator of the leverage borne by the Group. The ratio is a specified financial covenant within the Group's principal debt finance facilities the revolving credit facility and the loan note agreements and the ratio under each of these measurement bases therefore forms a key performance indicator for the Group. The basis of calculation under the two facilities differs in some regards, notably in the use of gross debt for the loan note agreements, compared to net debt for the revolving credit facility. The Group's aim over the medium term is to reduce the ratio of net debt to underlying EBITDA to approximately 1.50 times.

Key performance indicators

Interest cover

	2013	2012
Revolving credit facility		
Actual ratio of underlying EBITDA to finance costs	4.98x	6.71x
Minimum allowed ratio of underlying EBITDA to finance costs	4.00x	4.00x
Loan note agreements		
Actual ratio of underlying EBITDA to finance costs	5.61x	6.86x
Minimum allowed ratio of underlying EBITDA to finance costs	3.50x	3.50x

Interest cover provides a simple metric of the ratio between the underlying EBITDA generated by trading and the finance costs incurred in servicing the Group's debt. It is an important indicator for the Group, and is a specified financial covenant under the revolving credit facility and loan note agreements. As with the ratio of debt to underlying EBITDA, there are certain differences in the bases of calculation of interest cover under the two facilities.

Underlying continuing operating cash flow

	2013 £m	2012 £m
Operating cash flow	68.6	114.9

Operating cash flow provides a measure of the cash generated by the Group's trading. It represents the cash that is generated to fund capital expenditure, interest payments, tax and dividends. In the Group's relatively short cycle business and with working capital being released, operating cash conversion closely follows operating profit. The Group's underlying operating cash flow decreased by 40.3% to £68.6 million during the year.

Safety

	2013	2012
Lagging indicators		
Fatalities	–	1
Lost time incidents	33	32
Significant energetic incidents not causing injury	–	–
Leading indicators		
Near misses reported and actioned	2,168	1,384

Many Chemring products involve the use of hazardous substances and energetic materials, and safety metrics are a fundamental part of the key performance indicators used to manage the business. All incidents and near misses are reported and investigated, in order to share findings and corrective actions throughout the Group. The Group's key lagging indicators are fatalities, the number of incidents that result in working time being lost through injury, and the number of energetic incidents that do not cause injury. In addition, the Group has a number of leading indicators,

principally the level of near misses. The active reporting of near misses is encouraged by employees in order to highlight potential risk issues and enable these to be considered and addressed on a timely basis. The Group has had no significant process safety incidents in the year but our occupational safety performance remains flat. Further details on health and safety matters are included in the corporate responsibility review.

Working capital and inventory

Working capital

	2013 Working capital £m	2012 Working capital £m
Countermeasures	26.1	23.6
Sensors & Electronics	16.8	12.1
Pyrotechnics & Munitions	81.8	46.1
Energetic Sub-Systems	20.8	25.0
Unallocated items	(19.9)	(13.5)
Group	125.6	93.3

Inventory

	2013 £m	2012 £m
Countermeasures	29.0	30.9
Sensors & Electronics	11.5	12.3
Pyrotechnics & Munitions	51.3	45.8
Energetic Sub-Systems	21.9	24.8
	113.7	113.8

Working capital is defined as inventories, trade and other receivables, contract receivables, trade and other payables, and provisions. A primary focus within working capital is inventory.

Optimum inventory levels drive both effective staff utilisation, ensuring staff are productive while awaiting materials, and cost efficiency. In addition, excess inventory results in second order costs such as increased storage and inventory management, write-off of ageing or obsolete inventory, and disposal costs, which can be significant for energetic materials. Chemring currently measures total inventory levels. However, further metrics to measure availability are being developed as part of a working capital management review.

Pictured right:

US Air Force pilot ejects from US Air Force Thunderbird at an air show at Mountain Home Air Force Base.



Principal risks and uncertainties

As described on pages 59 and 60, 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 three year plan for each business, the most significant 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 mitigating actions taken by the Group management to address these risks are also set out below. The Group also mitigates its risk exposure through an insurance programme that covers property and liability risks, where it is appropriate and cost effective to do so.

RISKS AND IMPACTS	KEY MITIGANTS
<p>Health and safety risks</p> <p>The Group's operations which utilise energetic materials are subject to inherent health and safety risks. From time to time, incidents may occur which could result in the temporary shutdown of facilities or other disruption to manufacturing processes, causing production delays and resulting in financial loss and potential liability for workplace injuries and fatalities.</p>	<p>The Board believes that responsibility for the delivery of world class safety standards is an integral part of operational management accountability, and is committed to ensuring that the Group's leadership operates with health and safety as the top priority and that the strength of the Group's safety culture and the quality of its protective systems deliver operations where all employees and visitors feel and are absolutely safe. A new safety leadership programme has been developed this year, which will be attended by the management teams of every business during 2014.</p> <p>All employees now receive a booklet setting out the Group's statements of intent in relation to delivery of its health and safety strategy and the behaviours required of them as individual employees. All employees are encouraged to report potential hazards, and to raise any health and safety concerns through the appropriate channels.</p> <p>The Group continues to invest in state-of-the-art process safety systems and equipment. The Group's safety and loss prevention programmes require detailed pre-construction reviews of process changes and new operations, and routine safety audits of operations are undertaken on a regular basis.</p> <p>All businesses are expected to proactively manage their own risks but, in addition, the top site risks at each business and their associated mitigation programmes are reviewed quarterly by the Risk Management Committee. Health and safety is included on the agenda at every Board meeting, and is discussed at the monthly Group Executive Committee meeting.</p> <p>Further details on the Group's approach to health and safety are set out in the corporate responsibility review.</p>
<p>Possible defence budget cuts</p> <p>Defence spending depends on a complex mix of political considerations, budgetary constraints and the requirements of the armed forces to address specific threats and perform certain missions. As such, defence spending may be subject to significant fluctuations from year to year. Given the large budget deficits and the prevailing economic conditions in many NATO countries, the Group expects there to be continued downward pressure on budgets, and consequently, defence expenditure could be severely impacted.</p>	<p>In recognition of the issues affecting the Group's traditional NATO markets, business development activities are being focused on non-NATO markets, where defence expenditure is forecast to grow strongly over the next five to ten years. The Group has made good progress on developing its routes to market in India, Saudi Arabia, the United Arab Emirates and Brazil.</p> <p>The Group has established a more focused international sales and business development team, and has implemented new processes to ensure that the businesses are successful in "winning every sales opportunity".</p> <p>The Group also continually assesses whether its planned organic growth strategies and product developments align with government priorities for future funding. Most product development programmes take between six and twelve months to complete, and this gives the Group the ability to quickly redeploy engineering staff to product areas where funding is more secure.</p> <p>The Group continues to closely monitor the position in all the key markets in which it operates.</p>

RISKS AND IMPACTS	KEY MITIGANTS
<p>Timing and value of orders</p> <p>The Group's profits and cash flows are dependent, to a significant extent, on the timing of award of defence contracts. 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 orders could affect the Group's earnings and achievement of its budget, in any given financial year.</p> <p>The Group anticipates that delays in the placement of orders by traditional NATO customers, as a result of budgetary constraints, are likely to continue in the short to medium term. If the Group's businesses are unable to continue trading profitably during periods of lower order intake, financial performance will deteriorate and assets may be impaired.</p>	<p>As referred to above, the Group is focusing on the expansion of its business in non-NATO markets, where defence expenditure is forecast to increase.</p> <p>Maximising order intake remains a key objective for the businesses, and they continue to address this through the strengthening of their sales and marketing resources. The businesses also continue to pursue long-term, multi-year contracts with their major customers wherever possible.</p> <p>The Group has undertaken various restructuring projects over the last year, which were aimed at restoring the profitability of those Group businesses which have suffered most from order delays in recent times.</p> <p>Site optimisation plans are now being developed to ensure that the Group utilises its manufacturing facilities as efficiently as possible, within the constraints imposed by export control legislation and customer requirements.</p>
<p>Political risks</p> <p>The Group is active in several countries that are suffering from political, social and economic instability. The Group's business in these countries may be adversely affected in a way that is material to the Group's financial position and the results of its operations.</p> <p>In addition, political unrest and changes in the political structure in certain non-NATO countries to which the Group currently sells could impact on their future defence expenditure strategy and the Group's ability to export products to these countries.</p> <p>During periods of unrest, delays in obtaining export licences can result in delayed revenues.</p>	<p>The Group's businesses strive to maintain relationships at all levels within the political structure of certain key countries, in order to ensure that they are aware of and can react to proposed changes, if and when they occur.</p> <p>The businesses implement financing arrangements for contracts with high risk customers, which are intended to mitigate the impact of a deterioration in the customer's financial position, and in certain circumstances, they may also procure political risks insurance.</p> <p>The Group is exploring opportunities for collaboration on the establishment of local manufacturing operations in certain countries, which will remove some of the uncertainty regarding export of products.</p> <p>The planned expansion in non-defence markets should also increase the Group's portfolio of products which are less sensitive from an export control perspective.</p>
<p>Operational risks</p> <p>The Group's manufacturing activities may be exposed to business continuity risks, arising from plant failures, supplier interruptions or quality issues. These could result in financial loss, reputational damage and loss of future business.</p>	<p>All of the Group's businesses are required to prepare business continuity plans.</p> <p>The Group has introduced new requirements in relation to the reporting of key performance indicators this year, in order to provide better visibility on operational performance and to facilitate the identification of potential production and quality issues at an early stage.</p> <p>The Group insures certain business interruption risks where appropriate.</p>

Principal risks and uncertainties

RISKS AND IMPACTS	KEY MITIGANTS
<p>Introduction of new products</p> <p>The Group's approach to innovation and continued emphasis on research and development activity ensures that it is continually adding new products to the range. There is a need to ensure that this new product development is completed in a timely manner, and to a standard which allows volume manufacturing to be undertaken and the production of products against high reliability and safety criteria to meet customers' requirements. Failure to achieve this may have both financial and reputational impacts.</p> <p>The Group also needs to ensure that it continues to upgrade its existing product range to compete with emerging technologies, and to avoid the risk of obsolescence or loss of business.</p>	<p>The Group has introduced a more focused product development and technology investment approach, in order to ensure that resources are applied appropriately across the Group in support of the three year plan. A Technology Review Board has been established to review all proposed research and development projects to ensure that key initiatives are being prioritised and to eliminate possible duplication of effort in different parts of the Group.</p> <p>Working groups have been established to drive and co-ordinate the Group's technology growth in certain key areas, such as cyber security.</p>
<p>Product liability and other customer claims</p> <p>The Group may be subject to product liability and other claims from customers or third parties, in connection with (i) the non-compliance of these products or services with the customer's requirements, due to faults in design or production; (ii) the delay or failed supply of the products or the services indicated in the contract; or (iii) possible malfunction or misuse of products. As many of the Group's products are single-use devices, it is often impossible to conduct functional testing without destroying the product, and this increases the risk of possible product failure, either in use or during customers' own sample-based functional tests.</p> <p>Substantial claims could harm the Group's business and its financial position. In addition, any accident, failure, incident or liability, even if fully insured, could negatively affect the Group's reputation among customers and the public, thereby making it more difficult for the Group to compete effectively.</p> <p>Material breaches in the performance of contractual obligations may also lead to contract termination and the calling of performance bonds.</p>	<p>The businesses maintain rigorous control of their production processes, monitoring critical parameters on a batch or unit basis. State-of-the-art techniques, including statistical process control or Six Sigma, are applied and, where appropriate, processes are automated to reduce the scope for human operator error. Detailed assessments of incoming components and materials are conducted to ensure compliance with specifications.</p> <p>Product liability claims from third parties for damage to property or persons are generally covered by the Group's insurance policies, subject to applicable insurance conditions.</p>

RISKS AND IMPACTS	KEY MITIGANTS
<p>Management resource</p> <p>The Group requires competent management to lead it through the next stage of its development. In challenging markets and difficult times, there is a need to retain and incentivise senior managers and key employees, in order to ensure that the operations of the Group do not suffer from loss of management expertise and knowledge.</p> <p>As the shape of the Group's business also changes, with an increased focus on electronics, there is a need to ensure that the businesses build an appropriate skill base to enable them to compete successfully in new markets and product areas.</p>	<p>A Group Human Resources Director was appointed during 2013, to oversee the future people strategy.</p> <p>The Group has introduced a new performance management system for 2014, which will facilitate improved monitoring of individual employees' development objectives and requirements. Alongside this, a talent database is being developed, which will provide improved visibility on skills and resources across the Group, and will open up opportunities for employees to progress their careers within different parts of the Group.</p> <p>Incentivisation arrangements have been streamlined and improved in certain areas of the business, to ensure that employees are suitably incentivised to deliver key strategic objectives.</p>
<p>Compliance and corruption risks</p> <p>The Group operates in over sixty countries worldwide, in a highly-regulated environment, and is subject to the applicable laws and regulations of each of these jurisdictions. The Group must ensure that all of its businesses, its employees and third parties providing services on its behalf comply with all relevant legal obligations, as non-compliance could result in administrative, civil or criminal liabilities, and could expose the Group to fines, penalties, suspension or debarment, and reputational damage.</p> <p>The nature of the Group's operations could also expose it to government investigations relating to import-export controls, money-laundering, false accounting, and corruption or bribery.</p>	<p>The Group has a central legal and compliance function which assists and monitors all Group businesses, supported by dedicated internal legal resource in the US. The Group's internal audit activities also incorporate a review of legal risks.</p> <p>The Group operates under a Global Code of Business Principles, which stipulates the standard of acceptable business conduct required from all employees and third parties acting on the Group's behalf. The Group has also adopted a Bribery Act Compliance Manual, incorporating all of its anti-bribery policies and procedures.</p> <p>A significant proportion of the Group's management have received training in relation to ethics and anti-corruption.</p>

Principal risks and uncertainties

RISKS AND IMPACTS	KEY MITIGANTS
<p>Environmental laws and regulations</p> <p>The Group's operations and ownership or use of real property is subject to a number of federal, state and local environmental laws and regulations, including those relating to discharge of hazardous materials, remediation of contaminated sites, and restoration of damage to the environment.</p> <p>At certain sites that the Group owns or operates, or formerly owned or operated, there is known or potential contamination for which there is a requirement to remediate or provide resource restoration. The Group could incur substantial costs, including remediation costs, resource restoration costs, fines and penalties, or be exposed to third-party property damage or personal injury claims, as a result of liabilities associated with past practices or violations of environmental laws or non-compliance with environmental permits.</p>	<p>All of the Group's businesses are certified to the environmental management system ISO14001, which requires the setting of environmental goals and objectives focused on local aspects and impacts.</p> <p>The Group has managed monitoring and remediation programmes at certain sites, for which appropriate financial provision has been made. In certain circumstances, the Group procures environmental liability insurance, subject to applicable insurance conditions.</p>
<p>Financial risks</p> <p>Details of the financial risks to which the Group is potentially exposed and details of mitigating factors are set out in the financial review and note 24 of the group financial statements.</p>	

Corporate responsibility review

The Group acknowledges its obligation to ensure the responsible operation of its business at all times, and is fully committed to sound and ethical business conduct in its interaction with key stakeholders (shareholders, employees, customers, business partners and suppliers), governments and regulators, communities and society, and the environment.

The Group's approach

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.

The Board recognises that the long-term success of the Group will be enhanced by a positive interaction with all of its stakeholders, and has determined that the Group's corporate responsibility initiatives should be focused on the following key areas:

- Health and safety
- Employee support and development
- Environmental protection
- Ethical business conduct

The Board intends that the Group's corporate responsibility approach will be fully embedded within its businesses, and the senior management bonus plan incorporates specific objectives in the above areas.

Further details of the Group's approach are set out below.

In the workplace

Health and safety

Policy and practices

The Board recognises that the highest levels of safety are required in order to protect employees, product end users and the general public. The Board believes that all incidents and injuries are preventable, and that all employees have the right to expect to return home safely at the end of every working day. The long-term strategies the Group has adopted are designed to ensure that it continually improves its performance and reduces risk.

The Chief Executive has overall responsibility for health, safety and environmental matters across the Group. The Group Director of Safety reports directly to the Chief Executive, and is responsible for the effective administration and implementation of the Group's health, safety and environment strategy. The Group Director of Safety is a member of the Group Executive Committee and reports on the performance of all businesses against agreed targets and 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 and safety 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 and safety within their business, and for providing adequate resources to satisfy the Board's requirements. All managing directors have health and safety related objectives incorporated within their annual bonus plan. Managers in the Group's businesses are required to enforce procedures, and to provide leadership and commitment to promote and embrace a positive health and safety culture. The Board emphasises the importance of individual responsibility for health and safety at all levels of the organisation, and expects employees to report potential hazards, to be involved in implementing solutions, and to adhere to rules and procedures.

A key element in the continual improvement of health and safety management is sharing best practice and lessons learnt from incidents across all of the Group's businesses. Accidents, incidents and near misses are investigated, with actions generated to prevent recurrence. Compliance audits are conducted and all findings are subject to corrective action reviews to ensure closure.

With the exception of Mecar, all of the Group's businesses are certified to the international health and safety management system OHSAS18001.

Culture and behaviour

In the last few years, the Group has made substantial investments in its manufacturing facilities to reduce the levels of risk. The Group continues to focus on ensuring that its buildings, processes and products are as safe as reasonably practicable for employees and product users, by driving improvements in process safety management systems, by investing in automation, remote operations and infrastructure, and also by improving risk control systems and asset integrity.

In 2013, the Group developed a new culture and behaviour improvement programme based on industry best practice. This safety leadership programme will be delivered to all senior leaders, who will then develop individual business improvement programmes. The Board believes that the Group's leaders foster the culture by setting expectations, building structure, teaching others and stewarding results.

Corporate responsibility review

It is expected that this additional focus on culture and behaviour will drive further improvements in the Group's overall safety performance.

Performance

Energetic events

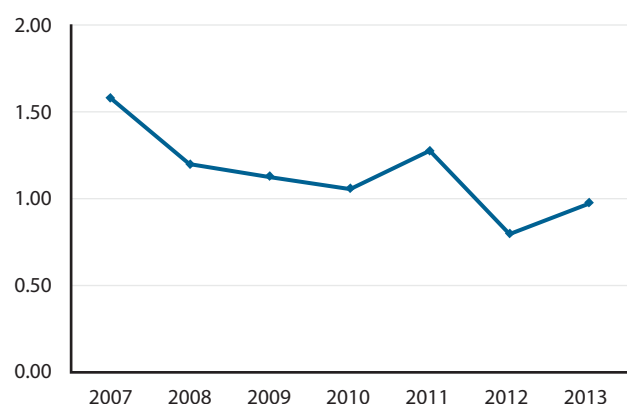
Whilst the Group takes all incidents seriously, particular attention is paid to those where employees sustain injury due to an energetic event. One such incident occurred during the year, which resulted in three days of lost time when an operator received minor burns at the Kilgore facility in Toone, Tennessee.

There were no energetic events during the year that caused significant damage to buildings or equipment.

Other lost time events

The Group collects and reports lost time incident rates using the US Occupational Safety and Health Administration (OSHA) rules. In 2013, there was a disappointing reduction in performance from a rate of 0.80 lost time incidents per 100 employees last year to 0.98 this year.

The Group's historical lost time incident rate performance per 100 employees is shown below:



The most common lost time injury types continue to be slips, trips and falls, and strains and sprains.

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 3,693 (2012: 4,193) employees based in seven countries.

Employment practices

The Group's policy is to provide equal opportunities for all employees, irrespective of race, nationality, gender, sexual orientation, marital status, religion or political belief, 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. The Group's employment practices policies are introduced at newly-acquired businesses at the earliest opportunity after they join the Group.

Human rights

The Group does not have a stand-alone human rights policy but its practices and policies adhere to internationally recognised human rights principles.

Gender diversity

A breakdown by gender of the number of persons who are directors of the Company, senior managers and other employees is set out below.

The Board currently has two female members, and remains committed to a minimum of at least 25% female representation on the Board. The Board recognises the importance of promoting diversity across the Group. In 2013, Dr Janice Turner, an employee of Chemring Technology Solutions, won the science category at the Women of the Future Awards. The Women of the Future Awards acknowledge the inspirational women of tomorrow across diverse sectors. The science category was new for 2013, and recognises young female scientists who are forging new ground in research and scientific achievement.

Directors



Senior managers



All Chemring employees



Ethnic diversity



Development and training

The Group continues to address training and development requirements for employees at all levels within the organisation. All businesses consider training needs for their employees at a local level, in order to ensure that they have the right skill base to deliver their three year strategic plan. The Board also reviews future management requirements and succession plans on an ongoing basis.

During the year, a Group-wide online performance management process was launched, which will standardise objective setting and performance classifications across the Group, as well as capturing personal development actions for employees.

In the UK, Chemring Technology Solutions continues to operate successful undergraduate placement and graduate development programmes, which have received external recognition.

Benefits

The Group aims to provide all employees with an attractive and competitive benefits package. US employees receive health care, and the Group is continuing to monitor proposed legislative changes to ensure compliance with any revised obligations which may be imposed. In the UK, January 2014 is the Group's staging date to comply with the pension scheme auto-enrolment legislation.

The Board is keen to encourage employees to join share schemes in order that they can share in the future success of the Group, and savings-related share plans are therefore offered to UK and US employees.

Communications

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. The businesses also engage their employees through representative bodies and trade unions.

The Group has recently completed its first all-employee engagement survey, for which there was a 78% response rate. Results are now being cascaded across the Group and plans formulated in response to the feedback received.

A Group magazine, "chemring-i", is published on a quarterly basis and distributed to all employees.

In the environment

Policy and practices

All of the Group's businesses are certified to the environmental management system ISO14001, which requires the setting of environmental goals and objectives focused on local aspects and impacts. In addition, expectations are set and performance is monitored across the Group.

Land quality

The Chemring Energetic Devices (formerly Scot) facility, which is based in Downers Grove, Illinois, USA, is located on a site which has "superfund" status under the US contaminated land (CERCLA) regime. The business continues to work with external consultants and the regulatory authorities to ensure that its legal obligations in relation to this matter are fully satisfied.

Mecar has been working with its local regulator in Belgium for some time to remediate historical contamination. It is anticipated that this will be an ongoing activity.

In addition, Simmel Difesa may become indirectly involved in proceedings related to environmental issues in the Colleferro region of Italy, where its principal manufacturing site is located.

The Group carries a £2.6 million provision in respect of pre-acquisition environmental liabilities, which the Board considers to be adequate (see note 25 of the group financial statements).

Incidents

There were no significant environmental incidents in the year.

Performance

Greenhouse gas emissions

The Group is required to report on all of the emission sources of entities that fall within its consolidated financial statements, as specified under the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013. The Group does not have responsibility for any emission sources of entities which are not included in its consolidated financial statements.

Absolute values have been converted to carbon dioxide equivalents using the UK Government Conversion Factors for Company Reporting 2013 produced by Ricardo-AEA. The reporting period covered aligns with the Group's financial year ended 31 October 2013. The Group has not reported on its Scope 3 emissions.

Corporate responsibility review

Scope 1 emissions

Combustion of fuel in any premises, machinery or equipment operated, owned or controlled by the Group

	Quantity (Mwh)	Conversion factor	CO ₂ e (tonnes)
Gas	61,184	0.18404	11,260
Heating oil	1,641	0.28594	469
Liquid petroleum gas (LPG)	409	0.21452	88

The use of any means of transport, machinery or equipment operated, owned or controlled by the Group

	Quantity (tonnes)	Conversion factor	CO ₂ e (tonnes)
Diesel	162	3.1885	517
Liquid petroleum gas (LPG)	113	1.4929	168
Petroleum	44	3.0058	132

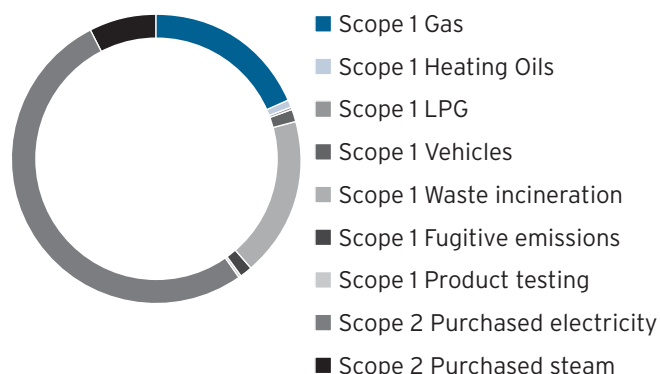
The operation or control of any manufacturing process	CO ₂ e (tonnes)
On-site waste incineration	10,865
Fugitive emissions	909
Product testing	9

With reference to the six Kyoto substances, the Group does not emit hydrofluorocarbons, perfluorocarbons or sulphur hexafluoride. Values for carbon dioxide, methane and nitrous oxides are included in the above figures.

Scope 2 emissions

Purchased energy	Quantity (Mwh)	Conversion factor	CO ₂ e (tonnes)
Electricity			
– Australia	1,001	0.84092	842
– Belgium	6,451	0.21956	1,416
– Germany	246	0.46089	113
– Italy	2,261	0.40631	919
– Norway	43,338	0.01669	723
– UK	15,443	0.44548	6,880
– USA	39,763	0.52225	20,766
Steam	20,903	0.21644	4,524

Total greenhouse gas emissions	Quantity (tonnes)
Scope 1	24,417
Scope 2	36,183
Total	60,600



Sources of emissions 2013

The above greenhouse gas report uses conversion factors provided by the UK Environment Agency. The Group's past conversion methodology differed from this, and to aid comparison, the following data uses historic converters to display emissions from electricity, gas and oil in carbon dioxide equivalents:

Source	2013 (tonnes CO ₂)	2012 (tonnes CO ₂)	2011 (tonnes CO ₂)	2010 (tonnes CO ₂)	2009 (tonnes CO ₂)
Electricity	43,244	44,576	46,459	38,303	36,334
Gas	11,437	13,630	14,676	14,033	12,512
Oil	6,229	5,726	7,222	3,111	2,008
Total	60,910	63,932	68,357	55,447	50,854

The Group uses sales revenue for intensity measurement, which it considers to be the most reliable comparator. The intensity progress for electricity, gas and oil over the last five years is shown below.

	2013	2012	2011	2010	2009
Total emissions (tonnes CO ₂)*	60,910	63,932	68,357	55,447	50,854
Group revenue (£million)*	625	740	730	571	504
Tonnes CO₂ per £million of revenue	97	86	94	97	101

* Group revenue and emissions exclude in-year acquisitions

All UK facilities participate in the CRC Energy Efficiency Scheme, with the exception of Chemring Energetics UK at Ardeer in Scotland, which operates under a Climate Change Agreement.

The Group participated in the 2013 Carbon Disclosure Project.

Waste

The Group's total waste generation increased during the year as a result of ongoing construction and renewal programmes.

	2013 (tonnes waste)	2012 (tonnes waste)	2011 (tonnes waste)	2010 (tonnes waste)	2009 (tonnes waste)
Recycled, non-hazardous	2,240	1,804	1,684	712	Not available
Recycled, hazardous	226	387	415	369	Not available
Not recycled, non-hazardous	1,080	1,028	1,018	1,161	Not available
Not recycled, hazardous	490	469	388	360	Not available
Total	4,036	3,688	3,505	2,602	1,876

Water

The Group's absolute water consumption varies each year within a narrow tolerance band, principally due to changes in product mix.

	2013 (m ³)	2012 (m ³)	2010 (m ³)	2010 (m ³)	2009 (m ³)
Total water consumption	1,606,541	1,646,906	1,441,000	1,550,000	1,762,000

In the community

Helping others

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. Each business has its own locally held charity budget, and at a Group level, charitable donations are considered on a monthly basis by the Executive Committee. The Group continues to sponsor the Red Devils and the UK Aerospace Youth Rocketry Challenge.

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, 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. The Group has relationships with several universities, whereby funding is provided for students' research activities.

Local impact

With regards to the impact of the Group's manufacturing activities on the local community, at locations where operations may inconvenience neighbours through product proofing, the businesses liaise with local residents to minimise any impact. The Group is also cognisant of the potential impact of its operations on the local environment, and is addressing this through its environmental strategy.

In the marketplace

Policy on the Sale of Goods and Services

In recent years, the scope of the Group's activities has broadened significantly, particularly with regards to the supply of components and sub-systems for various types of munitions. In addition, demand has increased for the supply of third party products to a number of customers. 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, to which customers and to which countries, and sets out a clear definition of what the businesses will not supply. All Group businesses are required to comply with this policy, which addresses both legal and ethical considerations with regards to certain products. The policy is reviewed and updated on a regular basis.

Ethics and business conduct

The Group has adopted a Global Code of Business Principles, which requires its employees, its businesses and all third parties who act on the Group's behalf to comply with the Group's standards of acceptable business conduct and applicable laws and regulations in all of the countries in which the Group operates.

Anti-bribery and corruption

Following implementation of the UK Bribery Act 2010, the Group adopted a Bribery Act Compliance Manual, which incorporates all of its anti-corruption policies and procedures. The Group's anti-bribery programme now incorporates the following:

- Requirements for bribery risk assessments to be carried out as part of normal operating procedures.
- Group-wide policies and procedures on the appointment of all sales partners and other third party advisers, stipulating due diligence and contractual requirements, approval levels, and monitoring and review processes.
- Regular training for management and employees working within commercial, sales and marketing, finance and human resource functions.
- Policies and procedures on the giving and receiving of gifts and hospitality.

The Group's US businesses have also adopted an ethical compliance programme to satisfy US Government requirements for ethical training for employees, compliance audits, a confidential reporting line for employees, and related investigation procedures.

The Group has a whistleblowing policy and procedures in place which enable all employees to raise concerns, in confidence, about possible improprieties. These arrangements reflect the requirements of the UK Bribery Act 2010.

CREATIVE PRODUCT INNOVATION



CASE STUDY

CENTURION

The innovative CENTURION launcher has had an excellent year, and continues to progress towards delivering a highly-capable and versatile system that has excellent utility across a range of platforms.

Conceived as a countermeasure launcher to introduce a step change improvement in naval anti-ship missile defence, the versatility of the CENTURION design has captured imagination. Already capable of firing both air countermeasures and anti-torpedo decoys, the system's ability to deploy short range surface-to-surface missiles has taken the launcher to a new dimension, making it a truly multi-role ship protection system.

This broad range of capability makes CENTURION suitable for ship classes ranging from patrol craft through to

major vessels. With its low weight, simple installation requirements and an ability to be rapidly deployed, the system is ideally suited to protect less well defended ships. This has significantly extended its potential market and has generated keen interest from around the globe.

The past year has seen the completion of Phase 3 proving test firings, outstanding levels of customer and industry interest, including from the UK Ministry of Defence and several NATO navies, and completion of a proof-of-concept missile launch, underscoring its multi-role capability.

The next stage of development will include design consolidation, software development and environmental testing, leading to a production standard system.











Governance

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Pictured Left:
CENTURION® completed successful proof firings on Salisbury Plain.

Board of directors

Name/Position/ Committee membership		Length of service on the Board (as at 23 January 2014)	Experience	Independent	Public board experience	Operational experience	International experience
Peter Hickson Non-Executive Chairman Remuneration Nomination (Chairman)		3 years 7 months	<ul style="list-style-type: none"> Finance experience from CFO positions Board experience at Chairman level Chartered Accountant 	N/A	✓	✓	✓
Mark Papworth Group Chief Executive		1 year 3 months	<ul style="list-style-type: none"> Extensive senior management experience in the servicing and manufacturing industries International experience 	N/A	✓	✓	✓
Steve Bowers Group Finance Director		1 year 1 month	<ul style="list-style-type: none"> Financial expertise Chartered Accountant 	N/A	✓	✓	✓
Sarah Ellard Group Legal Director & Company Secretary		2 years 4 months	<ul style="list-style-type: none"> Fellow of the Institute of Chartered Secretaries and Administrators Appointed Group Company Secretary in 1998 	N/A	✓		✓
Nigel Young Non-Executive Director Audit (Chairman) Remuneration		9 months	<ul style="list-style-type: none"> Previously Interim Chief Financial Officer of the Group from August 2012 to January 2013 Finance experience from CFO positions Chartered Accountant 	✓	✓	✓	✓
Andy Hamment Non-Executive Director Audit Remuneration		7 months	<ul style="list-style-type: none"> Extensive knowledge of the defence industry Senior Board experience 	✓	✓	✓	✓
Ian Much Senior Independent Non-Executive Director Audit Remuneration (Chairman) Nomination		9 years 2 months	<ul style="list-style-type: none"> Board experience at Chief Executive level Key shareholder representative 	✓	✓	✓	✓
Vanda Murray OBE Non-Executive Director Audit Remuneration Nomination		2 years 3 months	<ul style="list-style-type: none"> Board experience at Chief Executive level Fellow of the Chartered Institute of Marketing 	✓	✓	✓	✓

The structure of the Board

The Board consists of a balance of executive and non-executive directors who each bring a strong and in-depth mix of knowledge, business skills and experience to the Board's deliberations.

Legal/M&A experience	Finance experience	Government/ regulatory experience	Commentary
✓	✓	✓	Peter Hickson joined the Group as a non-executive director on 1 July 2010, and was appointed Chairman of the Board on 1 October 2010. Currently Chairman of Communis plc, and a non-executive director of Coalfield Resources plc. He has had senior management experience with a number of large international companies, and previous appointments include Chairman of Anglian Water Group, Senior Independent Director of London & Continental Railways Ltd, Finance Director of Powergen plc and non-executive directorships of Scottish Power plc, Marconi Corporation plc, RAC plc and Kazakhmys plc. He is also a trustee and Board member of Orbis Charitable Trust, the international sight saving charity, and a Fellow of the Institute of Chartered Accountants.
			Mark Papworth formerly worked at Wood Group plc, a leading FTSE 100 company, where he served as Chief Executive Officer of the Gas Turbines Services division from 2005 and also as an executive director on the Board from 2006. His career has covered high technology, service and manufacturing companies serving aerospace, energy and infrastructure markets. During his tenure at Wood Group, he implemented and delivered a strategic review, which resulted in a successful turnaround, improved manufacturing capabilities and substantial improvements in profitability.
			Prior to his time at Wood Group plc, Mark spent two years as Executive Vice President of Rolls-Royce Energy, based in the USA, and thirteen years with Alstom Power in various roles, finally as Managing Director of the Industrial Gas Turbines division.
✓	✓	✓	Steve Bowers was appointed Group Finance Director on 7 January 2013. He was formerly Finance Director of Umeco plc until its acquisition by Cytec UK Holdings Limited in July 2012.
			During Steve's time with Umeco he was involved in both acquisitions and disposals, as well as in the management of financial reporting, treasury functions and banking relationships. Prior to his appointment as Finance Director of Umeco, he held a number of financial roles, alongside the role of Company Secretary.
			He qualified as a Chartered Accountant with KPMG LLP and is a member of the Institute of Chartered Accountants.
✓		✓	Sarah Ellard was appointed as Group Legal Director on 7 October 2011, having been Group Company Secretary since 1998. Prior to joining the Group, Sarah trained and worked at Ernst & Young LLP. She is a Fellow of the Institute of Chartered Secretaries and Administrators.
✓	✓	✓	Nigel Young became a non-executive director on 1 May 2013. This followed his appointment as Interim Chief Financial Officer in August 2012. Nigel was previously finance director of ALVIS PLC, First Technology PLC and Babcock International PLC. He was also Group Finance Director of the FTSE 250 company Morgan Advanced Materials plc, until he retired in 2004. Since then, Nigel has undertaken a number of charitable, interim and consultancy roles including roles with the UK Atomic Energy Authority and McBride PLC.
			Nigel is Chairman of the Audit Committee.
✓		✓	Andy Hamment was appointed as a non-executive director on 1 July 2013. He is also a non-executive director of Senior PLC, and was previously Group Marketing Director and a main Board director of Ultra Electronics plc.
			Andy has worked in the defence and manufacturing industries for most of his career, primarily in business development and management roles. He joined Dowty in 1988 as Managing Director of its Controls business, and participated in the management buy-out that created Ultra Electronics.
✓			Ian Much joined the Group as a non-executive director in December 2004. He is Senior Independent Director and 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, Manchester United plc and Simplyhealth Group Ltd. He is currently Senior Independent Director and Chairman of the Remuneration Committee of Senior plc, and non-executive director and Chairman of the Remuneration Committee of BTG plc.
✓			Vanda Murray joined the Group as a non-executive director on 1 November 2011. She currently holds a portfolio of non-executive directorships, including Carillion plc, where she chairs the Remuneration Committee, The Manchester Airport Group plc, and Microgen plc. She also took up the role of Senior Independent Director of Fenner plc in January 2012. Previous appointments include Deputy Chairman of the North West Regional Development Agency, non-executive director of SIG plc, Chief Executive Officer of Blick plc, and UK Managing Director of Ultraframe PLC. She is a Fellow of the Chartered Institute of Marketing, and in 2002 was appointed OBE for Services to Industry and to Export.

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 2013.

Business review

The strategic report on pages 2 to 45 provides 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 group financial statements. There have been no significant events since the balance sheet date, other than as referred to in note 41 of the group financial statements.

Results and dividends

The loss attributable to the Group's shareholders for the year was £47.5 million (2012: £15.3 million profit). The directors recommend a final dividend of 3.8p per ordinary share which, together with the interim dividend of 3.4p per ordinary share paid in August 2013, gives a total for the year of 7.2p (2012: 9.5p). The final dividend is subject to approval by shareholders at the Annual General Meeting on 20 March 2014, and accordingly has not been included as a liability in these financial statements.

Directors and their interests

The present directors are shown on pages 48 and 49.

Peter Norriss resigned as a director on 20 March 2013, and Roger Freeman resigned as a director on 31 December 2013.

Mark Papworth was appointed as a director on 5 November 2012 and Steve Bowers was appointed as a director on 7 January 2013. These directors sought reappointment under Article 87.1 of the Company's Articles of Association at the last Annual General Meeting.

Nigel Young was appointed as a director on 1 May 2013 and Andy Hamment was appointed as a director on 1 July 2013. Both of these directors will be seeking reappointment under Article 87.1 of the Company's Articles of Association at the forthcoming Annual General Meeting.

In accordance with the Company's Articles of Association, all directors are required to submit themselves for re-election every three years. However, in order to ensure compliance with the UK Corporate Governance Code, all directors now voluntarily submit themselves for re-election at every Annual General Meeting.

Details of the service contracts between the Company and the executive directors are set out in the directors' remuneration report on page 72. The non-executive directors do not have service contracts with the Company.

The Company has made qualifying third party indemnity provisions for the benefit of its directors, which were in effect throughout the year and remain in force at the date of this report.

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 2013.

Information required as to directors' shareholdings is set out in the directors' remuneration report on page 82.

Substantial shareholdings

At 22 January 2014, 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 Conduct Authority:

Name	% Interest
Invesco Limited	19.9
Investec Asset Management Limited	6.4
UBS Global Asset Management	5.5
Old Mutual Asset Managers	5.1
JP Morgan Chase & Co.	4.9
Ameriprise Financial, Inc.	4.8
AXA S.A and its group of companies	4.8
Standard Life Investments Limited	4.6
Tameside MBC re Greater Manchester Pension Fund	4.2
Norges Bank	4.0
BT Pension Scheme Trustees Ltd as Trustees of the BT Pension Scheme	3.8
Cantillon Capital Management LLC	3.6
Hermes Equity Ownership Services Ltd	2.9

Employees and employee consultation

Details of the Group's employment policies and employee consultation practices are set out in the corporate responsibility review on pages 42 and 43.

Political donations

No political donations were made during the year (2012: £nil).

Contractual arrangements

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.

Share capital and shareholder rights

General

The Company's share capital consists of ordinary shares of 1p 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 issued share capital of the Company during the financial year are provided in note 27 of the group 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 forty eight hours before the meeting, by which shareholders must have been 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 (the "Act") requiring information about interests in shares, and has failed to supply such information within fourteen 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 Conduct 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 a 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 (the "Articles") may only be amended by special resolution at a general meeting of shareholders.

Issue of shares

Under the provisions of section 551 of the Act, the Board is prevented from exercising its powers under 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 passed 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. An ordinary resolution, seeking such authority, will be proposed at the forthcoming Annual General Meeting.

Section 561 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 571 of the Act to not apply the Act's pre-emptive requirements. Accordingly, a special resolution will be proposed at the forthcoming Annual General Meeting 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 561 of the Act. No issue of these shares will be made which would effectively alter the control of the Company without the prior approval of the shareholders in general meeting.

Purchase of own shares

The Company did not purchase any of its ordinary shares (2012: 1,215,000) during the year, and no ordinary shares (2012: 359,331) were distributed following vesting of awards under the Chemring Group Performance Share Plan. At 31 October 2013, the Company held a total of 2,198,814 ordinary shares in treasury (representing 1.1% of the ordinary shares in issue on 1 November 2013).

A special resolution 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 may consider holding repurchased shares pursuant to the authority conferred by this resolution as treasury shares. This will give the Company the ability to reissue treasury shares quickly and cost effectively, and will 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.

Directors' report

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

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

Date of awards	Total number of shares awarded	Number of participants receiving awards
21 November 2012	413,412	1
31 January 2013	1,260,059	27
27 June 2013	79,796	1
Total	1,753,267	29

The Chemring Group Restricted Share Plan (the "RSP")

The following deferred share awards were made under the RSP during the year:

Date of awards	Total number of shares awarded	Number of participants receiving awards
15 February 2013	542,032	34

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

On 30 July 2013, options were granted over 222,874 ordinary shares. Options over 2,577 ordinary shares were exercised during the year and options on 166,091 shares lapsed. Additional information is set out in note 31 of the group financial statements.

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

On 30 July 2013, options were granted over 55,997 ordinary shares. No options were exercised during the year and options on 65,515 shares lapsed. Additional information is set out in note 31.

Approach to share ownership

The Group actively encourages its employees to share in the future success of the Group. The sixth annual grant of options under the UK Sharesave Plan and the US Stock Purchase Plan, which were both launched in 2008, took place during the year.

Going concern

Details of the conclusions arrived at by the directors in preparing the financial statements on a going concern basis are set out in the financial review on page 32.

Statement of directors' responsibilities

The directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law, the directors are required to prepare group financial statements in accordance with International Financial Reporting Standards (IFRSs), as adopted by the European Union and Article 4 of the IAS Regulation, and have elected to prepare the parent company financial statements under IFRSs as adopted by the European Union. Under company law, the directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, IAS 1 *Presentation of financial statements* requires that directors:

- 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 IFRSs 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; and
- make an assessment of the Company's ability to continue as a going concern.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions, disclose with reasonable accuracy at any time the financial position of the Company, and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Directors' responsibility statement

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with International Financial Reporting Standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- the strategic report includes 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 that they face; and
- the annual report and financial statements, taken as a whole, are fair, balanced and understandable, and provide the information necessary for shareholders to assess the Company's performance, business model and strategy.

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 section 418 of the Companies Act 2006.

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 2013.

Auditors

A resolution to reappoint 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 20 March 2014, together with explanatory notes, appear in the separate Notice of Annual General Meeting sent to all shareholders.

Approved by the Board of Directors on 23 January 2014

Signed on behalf of the Board

Sarah Ellard

Group Legal Director & Company Secretary

Corporate governance report

Introduction by the Chairman

The Board is committed to upholding the highest standards on corporate governance, protecting and growing the shareholders' assets, and engaging in a fair and transparent manner with all of the Group's stakeholders. The Board takes responsibility for approving the Group's long-term goals and strategies, and provides overall financial and organisational control. The Board also ensures that the Group's businesses have appropriate and effective internal control and risk management systems.

The detailed report below sets out how the Company has applied the main and supporting principles of good governance set out in the UK Corporate Governance Code issued in September 2012 by the Financial Reporting Council (the "Code"). I would like to draw your attention to some specific examples of how the principles relating to the role and effectiveness of the Board have been applied in particular areas of focus this year:

Composition of the Board

Following the resignations of the former Chief Executive and Finance Director during 2012, Mark Papworth was appointed as Chief Executive on 5 November 2012, and Steve Bowers was appointed as Finance Director on 7 January 2013. In recruiting the new executive management team, the Board was keen to ensure that the team would have the requisite skills and experience to deliver the recovery of the Group's operational and financial performance, and to develop and oversee the future strategy for the Group. Whilst there is still much to do, the Board is pleased with the progress that has been made in these areas during the year.

Nigel Young, who was Interim Chief Financial Officer between August 2012 and January 2013, was appointed to the Board as a non-executive director on 1 May 2013 and became Chairman of the Audit Committee, succeeding Roger Freeman who retired from the Board on 31 December 2013. Nigel's detailed knowledge of the Group's businesses and their accounting systems is greatly assisting the activities of the Audit Committee in its oversight of the Group's financial controls and reporting.

Peter Norriss retired from the Board at the Annual General Meeting in March 2013, after nine years' service. In defining the requirements for his successor, the Board recognised that it would be beneficial to appoint another non-executive director with specific defence industry experience, and Andy Hamment, a former executive director of Ultra Electronics plc, was therefore appointed to the Board on 1 July 2013.

Setting of strategic aims

As referred to in the strategic report, the Board engaged in a comprehensive planning process towards the end of the financial year, which crystallised the strategy for the Group for the next three years. The process was particularly challenging on this occasion, given the need to realign the Group's strategy against the background of continuing difficult market conditions, and lack of visibility on future requirements in the Group's key markets. However, the Board now has a clear plan for delivering future shareholder value.

Remuneration arrangements

In anticipation of the changes to the requirements for reporting on and seeking approval for executive remuneration arrangements, which came into effect in August 2013, the Remuneration Committee engaged in a significant amount of work this year in developing a set of remuneration principles, which will be presented to shareholders for approval at the Annual General Meeting in March 2014. As part of this process, Ian Much, the Chairman of the Remuneration Committee, and I engaged with a number of our major shareholders to seek their feedback on the proposed principles. Further details are set out in the directors' remuneration report.

The Company has been in compliance with the provisions of the Code throughout the year ended 31 October 2013, with the exception that the performance evaluation of the Board has not been externally facilitated in the last three years. As indicated in last year's corporate governance report, given the significant changes in the composition of the Board over the last two years, we will undertake an externally facilitated evaluation during 2014. In the meantime, we will continue to assess our performance and identify areas for future improvement, both in terms of the composition and effective operation of the Board.

Peter Hickson

Chairman

The Board

Composition and operation of the Board

The Board currently comprises three executive directors and five non-executive directors (including the Chairman). The Board considers all of the non-executive directors to be independent in judgment and character, and considered Peter Hickson to be independent on his appointment as Chairman.

Although Nigel Young was employed as Interim Chief Financial Officer for a period of six months prior to his appointment as a non-executive director, the Board does not consider that this short period of employment impacted his independence and his contribution to the Board continues to be impartial and objective. Similarly, whilst Ian Much has now served as a non-executive director for a period of nine years and two months, he continues to fulfil both of his roles as Senior Independent Director and Chairman of the Remuneration Committee in an unbiased and objective manner, and his experience remains very valuable to the Board.

The directors' biographical details are set out on pages 48 and 49.

In accordance with the Company's Articles of Association, all directors are required to submit themselves for re-election every three years. However, in order to ensure compliance with the Code, all directors will voluntarily submit themselves for re-election at the forthcoming Annual General Meeting.

The Board meets at least ten times a year, and has a formal schedule of matters specifically reserved to it for consideration and approval, including:

- approval of the Group's three year plan;
- approval of annual budgets;
- approval of acquisitions, disposals and major capital expenditure;
- approval of policies on financing and treasury, ethical matters, and health and safety; and
- oversight of the Group's systems of financial control and risk management.

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;
- approval of capital expenditure within limits imposed by the Board; and
- developing and implementing risk management systems.

Further information on the Executive Committee is set out in the section of this report covering Board committees.

The Board continually reviews the content and presentation of Board papers, to ensure that the directors have sufficient information to make expedient and considered decisions in fulfilment of their fiduciary duties. The adoption of an electronic portal for dissemination of information to the Board has resulted in more efficient communication and improved access for the Board to minutes and other records.

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; 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, should the need 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 maintains directors' and officers' liability insurance in respect of legal action against its directors.

Corporate governance report
























Board activity throughout the year

The Board receives reports from the Chief Executive, the Group Finance Director, the Group Legal Director and the Group Director of Safety as standing agenda items at every scheduled Board meeting. Details of the other principal activities undertaken by the Board during the year are set out below:

November 2012 	December 2012 	January 2013 	February 2013 
Consideration of market and shareholder feedback following withdrawal of bid approach and issue of trading updates	Consideration and approval of management reorganisation	Approval of 2013 budget	Update on management reorganisation and business integrations
Review of draft budget for 2013	Consideration of potential business divestments	Approval of preliminary announcement and annual results	Discussion on current Board performance and opportunities for improving future effectiveness
Review of strategy for international joint ventures			Review of updated terms of reference for Board committees
Approval of integration of Chemring Sensors & Electronic Systems businesses			
March 2013 	April 2013 	May 2013 	June 2013 
Review of strategy for renegotiation of bank and note holder financing covenants	Discussion on the appointment of new non-executive directors	Discussion on US organisation and legal requirements	Approval of interim results
		Presentation and approval of new HSE strategy	
		Capital expenditure approval	
July 2013 	September 2013 	October 2013 	
Presentations from operational business heads	Presentations from financial advisers on proposed business divestments	Consideration and approval of trading update	
Review of Policy on the Sale of Goods and Services		Approval of 2014 budget	
Review of strategic objectives		Review of three year plan and Strategic Planning Process	

Meeting attendance

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

	Board (11 meetings)	Audit Committee (3 meetings)	Remuneration Committee (6 meetings)
Peter Hickson	 (11)	–	 (6)
Steve Bowers (appointed 7 January 2013)	 (9)	–	–
Sarah Ellard	 (11)	–	–
Roger Freeman (retired 31 December 2013)	 (11)	 (3)	 (6)
Andy Hamment (appointed 1 July 2013)	 (3)	 (1)	 (2)
Ian Much	 (11)	 (3)	 (6)
Vanda Murray	 (11)	 (3)	 (6)
Peter Norriss (retired 20 March 2013)	 (5)	 (1)	 (2)
Mark Papworth (appointed 5 November 2012)	 (11)	–	–
Nigel Young (appointed 1 May 2013)	 (5)	 (2)	 (3)

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

In addition to the scheduled meetings, a further three ad hoc Board meetings and two ad hoc Remuneration Committee meetings were convened during the year to deal with matters arising between scheduled meetings.

The Nomination Committee did not meet separately during the year, as the new appointments made during the year and related matters were dealt with by the Board as a whole.

The Chairman

The Company separates the roles of Chairman and Chief Executive in accordance with the recommendations of the 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 training and development needs of directors are identified and the performance of the Board is evaluated on a regular basis; ensuring effective communication with shareholders and acting as a conduit to ensure that the views of shareholders are communicated to the Board. The Chairman's other business commitments, which are detailed on page 49, were fully disclosed to the Board prior to his appointment, and the Board is comfortable that he has sufficient time available to commit to his role.

Non-executive directors

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, in a constructively challenging manner where appropriate. 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 four 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.

Ian Much served as the Senior Independent Director throughout the year.

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

The non-executive directors have letters of appointment covering, amongst other items, their terms of appointment and expected time commitment. These letters of appointment usually provide for a three year appointment, unless terminated earlier by and at the discretion of either party upon three months' written notice. Further details are set out in the directors' remuneration report on page 73, and copies

Corporate governance report

of the letters of appointment are available for inspection on request to the Company Secretary.

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.

Board performance evaluation

The performance of the Board and its effectiveness are subject to periodic review by the Chairman. The Chairman and the non-executive directors consider the individual performance of the executive directors as part of the annual remuneration review, and the Chairman and the Chief Executive review the performance of the non-executive directors. Any weaknesses identified as a result of the individual performance evaluations are considered during the overall evaluation of the Board and addressed appropriately.

There were a number of changes to the Board during 2012 and 2013, which required the Chairman, with the assistance of the non-executive directors, to undertake a full evaluation of the performance of the Board and an assessment of the additional skills, experience and knowledge that would improve its future effectiveness. The evaluation of the current individual directors has confirmed that they all continue to contribute effectively to the operation of the Board and demonstrate full commitment to their respective roles.

Given the various new appointments to the Board since 2012, the Board did not consider that it would be beneficial to appoint an external adviser to assist with a formal performance evaluation during 2013, and this exercise will instead be undertaken during 2014.

Diversity

The Board supports the principles set out in Lord Davies' Review into Women on Boards published in February 2011, as reflected by the fact that the Board has two female members. The Board also recognises the importance of promoting diversity across the Group, and remains committed to a minimum of at least 25% female representation on the Board.

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 Audit Committee comprises four independent non-executive directors. At the date of this report, the Audit Committee members were Nigel Young (Chairman), Andy Hamment, Ian Much and Vanda Murray.

Nigel Young succeeded Roger Freeman as Chairman of the Audit Committee on 1 May 2013. Nigel acted as Interim Chief

Financial Officer for the Company between August 2012 and January 2013, and was formerly Finance Director of Morgan Advanced Materials plc, ALVIS PLC, First Technology PLC and Babcock International PLC. The remaining members of the Committee have also served as executive directors of listed companies and as non-executive directors on other audit committees, and have extensive commercial and financial experience. The Board therefore considers that each member of the Audit Committee has the requisite recent and relevant financial experience to satisfy the requirements of the Code.

The Audit Committee met three times during the year. The Committee operates within formal written terms of reference, which are available on the Company's website, as referred to above.

The Audit Committee report is set out on pages 61 to 63.

Remuneration Committee

The Remuneration Committee comprises five independent non-executive directors. At the date of this report, the Remuneration Committee members were Ian Much (Chairman), Andy Hamment, Peter Hickson, Vanda Murray and Nigel Young.

Six scheduled Remuneration Committee meetings were held during the year, together with two ad hoc meetings. Further details on the Remuneration Committee and its activities, and the Company's policies on directors' remuneration are set out in the directors' remuneration report on pages 64 to 85.

Nomination Committee

The Nomination Committee comprises three independent non-executive directors. At the date of this report, the Nomination Committee members were Peter Hickson (Chairman), Ian Much and Vanda Murray.

Peter Hickson is Chairman of the Nomination 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 a new non-executive director during the year, the Board considered the specific knowledge and expertise which was required to enhance the Board's existing skill set. A brief was prepared, based on the Board's conclusions, and The Zygos Partnership (who also handled the recruitment of Mark Papworth and Steve Bowers) were retained to identify appropriate external candidates. The Chairman and the Senior Independent Director interviewed a selection of short-listed candidates initially, and thereafter, preferred candidates were invited to meet with the Chief Executive and certain other members of the Board. Following completion of this process, Andy Hamment was invited to join the Board on 1 July 2013. His defence industry and international experience were key factors in the Board's decision.

Executive Committee

The current members of the Executive Committee are:

- Mark Papworth (Group Chief Executive)
- Rik Armitage (Group Director – Strategy & Technology)
- Steve Bowers (Group Finance Director)
- Terry Bridgewater (Group Director of Safety)
- Richard Dellar (Group Director – Sales & International Business Development)
- Jim Devine (Group HR Director)
- Sarah Ellard (Group Legal Director & Company Secretary)
- Michael Flowers (Group Director – European Munitions)
- Stephen Grinham (Managing Director – Chemring Technology Solutions)
- Juan Navarro (President – Chemring North America)
- Rupert Pittman (Group Director of Communications & Investor Relations)

Mark Papworth chairs the Executive Committee, which meets monthly. The Executive Committee is responsible for the executive day-to-day running of the Group, 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 and other providers of capital

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 Chief Executive and the Finance Director, although the Chairman and the Senior Independent Director did attend meetings with certain shareholders during 2013. The other non-executive directors are also offered the opportunity to meet with major shareholders and attend meetings if so requested by major shareholders.

Communication with private investors is achieved largely through the medium of the interim report, interim management statements, and the annual report and accounts.

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. In line with best practice guidelines, voting at the forthcoming Annual General Meeting will be conducted by way of a poll. This allows all votes to be counted, not just those of shareholders who attend the meeting. Poll results will be published on the Company's website as soon as practicable following the conclusion of the meeting. The Notice of the Annual General Meeting is sent to shareholders at least twenty working days before the meeting.

In addition to issuing shares, the Company also finances its activities through external bank loans and by the issue of loan notes. The Board recognises the importance of maintaining good relationships with the providers of this capital, and the Chief Executive and the Finance Director brief the banks and note holders on a regular basis on the Company and its performance. The Board receives regular reports on any issues impacting these relationships.

Financial and business reporting

The statement of directors' responsibilities in respect of the financial statements and accounting records maintained by the Company is set out on page 52.

Having taken all the matters considered by the Board and brought to the attention of the Board during the year into account, we are satisfied that the annual report and accounts for the year ended 31 October 2013, taken as a whole, is fair, balanced and understandable. Furthermore, the Board believes that the disclosures set out on pages 2 to 45 of the annual report provide the information necessary to assess the Company's performance, business model and strategy.

Internal control and risk management

The Board reviews 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 annual review of the effectiveness of the Group's systems of internal control in compliance with provision C2.1 of the Code, the Board considered 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. Following completion of this process, each business establishes a three year plan and annual budget, which are subject to approval by the Board. The performance of each business against

Corporate governance report

budget and the prior year is reviewed on a monthly basis at both the operational management level and by the Board. Achievement of strategic business objectives and the associated risks are monitored by the Board on an ongoing basis.

- The Chief Executive, the Finance Director and other members of the Executive Committee attend review meetings with each of the businesses on a quarterly basis. In the case of the US businesses, formal Board meetings are also 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 are also appointed to the Boards of the Group's Italian, Norwegian and Australian subsidiaries.
- 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 auditors, who report regularly to the Audit Committee on their 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 advisers on a regular basis.
- The Group Director of Safety, supported by 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 has implemented a Bribery Act compliance manual incorporating its anti-bribery policies and procedures.

The Group's Risk Management Committee meets on a quarterly basis. At the date of this report, the members of the Risk Management Committee were Mark Papworth (Chairman), Steve Bowers, Terry Bridgewater, Sarah Ellard, Michael Flowers, Stephen Grinham and Juan Navarro. The Committee reviews the key risks associated with the achievement of the annual budget and the three year plan for each business, and the risk control procedures implemented. It also considers the top 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 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 2013, and it confirms that systems of internal control and risk management compliant with the 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.

Procedures to deal with directors' conflicts of interest

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 may possibly conflict with the interests of the Company. The Company's Articles of Association include provisions for dealing with directors' conflicts of interest in accordance with the 2006 Act. The Company has procedures in place to deal with situations where directors may have any such conflicts, which require the Board 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

Details of the conclusions arrived at by the directors in preparing the financial statements on a going concern basis are set out in the financial review on page 32.

Audit Committee report

Annual statement by the Chairman of the Audit Committee

I assumed the Chairmanship of the Audit Committee on 1 May 2013, having taken over from Lord Freeman, who had undertaken the role for the previous seven years.

I believe that the Audit Committee has a very important role to play in the governance of the Group's financial affairs, and I am committed to ensuring that we apply the requisite oversight to the Group's internal controls and risk management systems, and that we maximise the effectiveness and assurance that can be derived from our external and internal audit activities.

During my short tenure as the Group's Interim Chief Financial Officer, I gained a very valuable insight into the strengths and potential weaknesses of our current financial systems, and the different challenges faced by the businesses. I am confident that this will assist the Audit Committee with its governance role over the next few years.

Nigel Young

Chairman of the Audit Committee

Operation of the Audit Committee

The Audit 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 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 reviews annually its terms of reference and its effectiveness, and recommends to the Board any changes required as the result of such review.

Meetings

Meetings of the Committee are attended, at the invitation of the Chairman of the Committee, by the external auditors, the Chairman of the Board, the Finance Director and representatives from the Group finance and internal audit function. The Committee meets with the auditors on a regular basis without the executive directors being present. The Company Secretary acts as secretary to the Committee and minutes of meetings are circulated to all Board members.

The Audit Committee plans to meet four times in the current financial year.

Principal activities of the Audit Committee during the year

January 2013	June 2013	September 2013
Review of the Group's preliminary announcement and annual results for the year ended 31 October 2012	Review of the Group's half year results	Consideration of report from the Finance Director on topical issues
Consideration of the auditor's report on the results of their full year audit	Consideration of the auditor's report on the results of their interim review	Review and approval of the Group's future tax strategy
Review of the Group's revenue recognition and contract accounting policies and procedures	Review of the Group's revenue recognition and contract accounting policies and procedures	Review of policy on the provision of non-audit services by the external auditors
Goodwill impairment review	Goodwill impairment review for acquired businesses	Review of the Group's risk management systems and reporting
Consideration of the Group's going concern status	Consideration of accounting treatment of non-underlying items of expenditure	Consideration of the auditor's plan for the full year audit
Review of the internal control environment and the auditor's observations thereon	Consideration of updated segmental reporting	Reappointment of the auditors and approval of their fees
Consideration of the internal auditor's report	Review of the internal control environment and the auditor's observations thereon	Consideration of the internal auditor's report
	Presentation from the Group Legal Director on the Group's Bribery Act compliance programme	

Corporate governance report

Significant issues considered by the Audit Committee during the year

Revenue recognition and contract accounting policies and procedures

The Committee reviewed the Group's revenue recognition and contracting accounting policies and procedures, to ensure that they remained appropriate and that the Group's internal controls were operating effectively in this area. Advice was also sought from the external auditors. The Committee considered a detailed analysis of the key assumptions made on the contract accounting treatment of those contracts which had a material impact on the Group's results for the year ended 31 October 2013, and concluded that these were reasonable and appropriate.

Impairment of goodwill and other intangible assets

In January 2013, the Committee considered a paper prepared by management on their review of the carrying value of goodwill and intangible assets as at 31 October 2012, against updated forecasts for each of the relevant businesses. In view of the difficult trading conditions facing a number of the Group's businesses, an updated methodology was adopted for impairment testing, which included a sensitivity analysis based on further significant deteriorations in defence budgets in key markets. As a consequence of this review, the Committee concurred that it would be appropriate to recognise an impairment loss of £6.8 million in relation to Chemring Ordnance at the 2012 year end and £15.7 million in relation to Chemring Energetic Devices. The Committee also agreed that it would be appropriate to include a note in the 2012 financial statements on a possible future impairment charge in relation to Hi-Shear Technology Corporation.

In June 2013, the Committee considered an updated impairment review and concluded that it would be appropriate to recognise a further impairment loss of £15.7 million in relation to Chemring Energetic Devices in the half year results.

Going concern

In order to satisfy itself that the Group has sufficient financial resources to enable it to continue trading for the foreseeable future, the Committee regularly reviews the adequacy of the Group's financing facilities against future funding requirements and working capital projections. The Committee received regular reports from the Finance Director on the Group's financial covenant compliance position throughout the year, and was kept closely informed on the progress of discussions with the Group's banks and loan note holders regarding the renegotiation of the covenants which was completed in June 2013.

Based on its review of the Group's forecasts and detailed discussions with the external auditors, the Committee recommended to the Board the adoption of the going concern basis for the preparation of both the 2012 financial statements and the 2013 interim results.

Further details on the Group's going concern status can be found in the financial review on page 32.

Segmental reporting

In the first half of 2013, the Committee considered management's recommendations on an updated segmental reporting format to reflect the Group's new management and operational structure, and concurred that the proposed changes were appropriate.

External auditors

The Audit Committee is responsible for making recommendations to the Board on the appointment, reappointment and removal of the Company's external auditors. The Committee also undertakes an annual assessment of the auditors' independence and objectivity, taking into account relevant professional and regulatory requirements and the relationship with the auditors as a whole, including the provision of any non-audit services.

Audit effectiveness and tendering

Deloitte LLP have been the Company's auditors for many years, and were reappointed at the last Annual General Meeting in March 2013. During the year, the Committee agreed with Deloitte LLP that, in view of the various changes which had occurred within the Group, it would also be beneficial for a new Audit Partner to be appointed to bring a new perspective to the audit function. Accordingly, after a managed handover, Anna Marks succeeded Nigel Mercer on the engagement in May 2013.

In the opinion of the Committee, the relationship with the auditors currently works well, and having reviewed their independence and effectiveness, the Committee has not considered it necessary to date to require Deloitte LLP to re-tender for the audit work. Accordingly, the Committee has recommended to the Board that Deloitte LLP be proposed for reappointment as auditors at the forthcoming Annual General Meeting.

The Committee acknowledges the new recommendation in the Code that the external audit contract should be put out to tender at least every ten years. The appointment of the new Audit Partner in 2013 has provided fresh oversight of the audit process. Given this change, the Committee will keep under review the timing of its next tender process but does not currently intend that the audit will be put out to tender during 2014.

In assessing the effectiveness of the external auditors during the year, the Committee reviewed:

- the arrangements for ensuring the external auditors' independence and objectivity;
- the external auditors' fulfilment of the agreed audit plan and any variations from the plan;
- the robustness and perceptiveness of the auditors in their handling of the key accounting and audit judgments; and
- the content of the external auditors' reporting and internal control.

There are no contractual or similar obligations to restrict the choice of external auditors.

Auditor independence

The Committee keeps under review the level of any non-audit services which are provided by the external auditors, to ensure that this does not impair their independence and objectivity.

The Committee has adopted a policy which states that the external auditors should not be appointed to provide any corporate finance or similar consultancy services, unless the Committee agrees that their appointment would be in the best interests of the Company's shareholders in particular circumstances and would not create any direct conflict with their role as external auditors.

The policy does permit the provision of tax advisory services by the auditors, provided that the provision of such advice does not conflict with the external auditors' statutory responsibilities and ethical guidance.

During the year, Deloitte LLP provided the following additional services to the Group:

- tax compliance services relating to corporation tax returns and other overseas regulatory tax returns;
- tax advisory services relating to advice given on the Group's tax structures; and
- corporate finance services relating to various proposed financial transactions, where the auditors are considered best placed to perform these services.

Details of the amounts paid to the external auditors during the year for audit and other services are set out in note 6 to the group financial statements.

The Committee, in conjunction with the Finance Director, ensures that the Group maintains relationships with a sufficient choice of appropriately qualified alternative audit firms for the provision of non-audit services.

Internal audit

The Audit Committee is responsible for reviewing the work undertaken by the Group's internal audit function, assessing the adequacy of the internal audit resource, and recommending changes for increasing the scope of the internal audit activities.

The Group's internal audit programme incorporates an annual rolling review of all businesses, and focuses on both financial and non-financial controls and procedures. The Committee approves the annual internal audit plan and receives regular reports from the internal auditors.

The Committee considers that the Group's current internal audit resource is appropriate, given the size of the Group, but will continue to monitor the position closely.

Directors' remuneration report

Statement by the Chairman of the Remuneration Committee

Dear shareholder

As you will be aware, 2013 was another challenging year for the Group, with a change of both Chief Executive and Finance Director, sharp reductions in military budgets throughout our NATO markets, rapid destocking of consumables – which make up much of our sales – as troops withdrew from conflict areas such as Afghanistan, and the US Government shutdown as we approached our year end.

At the time of the appointment of the new Chief Executive and Finance Director, we made a number of temporary changes to our remuneration arrangements to reflect the uncertainties which they inherited and the fact that, in their first year, they would be operating under a budget, the preparation of which they had had no part in. For the current year beginning 1 November 2013, we are returning to a more conventional policy and I summarise the key changes below.

- The structure of the bonus plan was changed in 2013 from a 75%/25% split between financial measures and personal objectives to a 60%/40% split between the same metrics. This was to reflect the uncertainties in the integrity of the Group's budget, and to reflect the number of key, short-term actions which were required to be completed during 2013, to reposition the Company going forward. In addition, Mark Papworth and Steve Bowers were guaranteed a minimum bonus in their first year equivalent to 50% of base salary because of the uncertainties outlined above and the need to attract strong replacements over a very short period of time. The circumstances surrounding the appointment of these two executive directors were exceptional and this was fully disclosed to shareholders in last year's remuneration report.
- Mark Papworth and Steve Bowers will receive their guaranteed minimum bonuses for 2013 (with Steve Bowers' bonus being prorated to reflect his January 2013 start date) and Sarah Ellard (Group Legal Director & Company Secretary) will receive a below-target bonus of 36% of salary. 40% of the payouts will be deferred in shares for three years. The actual bonus payments due to the executive directors for 2013 are set out on page 77 of the remuneration report.
- In 2014, the weighting on financial measures in the annual bonus will be increased, with a requirement for achievement of threshold financial measures before any element of the personal objectives can become payable. The financial targets will again be based on a mix of earning per share ("EPS") and cash flow. The personal objectives will be measurable and consistent with the Group's longer-term goals. Details of the personal objectives and performance against them will be disclosed retrospectively in the 2014 annual report.
- When granting performance share plan awards to both the new executive directors and other senior executives in 2013, the Committee did not feel that they could set sufficiently robust three year EPS targets because of the uncertain conditions at that time and therefore absolute share price targets were set. The policy for 2014 and beyond will be to use two metrics, namely growth in underlying EPS and relative total shareholder return ("TSR") measured against an international peer group of defence sector companies. These measures have been selected by the Remuneration Committee as they are aligned to the success of the Group's recovery. EPS is a measure of the Group's overall financial success and TSR provides an external assessment of the Company's performance against companies of a similar size and complexity. TSR also aligns the rewards received by executives with the returns received by shareholders. Each will determine the vesting of 50% of the 2014 awards. 25% of each part of the award will vest for threshold or median performance, with full vesting of each part of the award for stretch or upper quartile performance. The EPS performance targets for 2014 have not yet been determined but in accordance with our normal practice, will appropriately reflect market expectations for the Company at the time of grant, as well as our own internal expectations. The performance targets will be disclosed in the relevant RIS announcement when the awards are granted.
- In reviewing the salaries of Mark Papworth and Steve Bowers for 2014, the Committee was cognisant of the circumstances which prevailed at the time of their recruitment in late 2012. We were very much aware that the condition of the Company at that time, combined with the deteriorating market conditions within the defence industry, meant that the Company was facing an extremely challenging and complex few years. Mark and Steve were selected as we believed that they had the drive and character to deliver the recovery which the Company required. However, we were aware of their relative inexperience and decided to adopt the principle outlined in our remuneration policy

of bringing them in below market rate, with a view to reviewing progress and bringing them up to that level when appropriate. Against this background and acknowledging the tremendous progress made in addressing the underlying issues facing the Company in their first year, Mark Papworth's salary has been increased by 5.6% to £475,000 and Steve Bowers' salary has been increased by 9.1% to £300,000. Sarah Ellard's salary has been increased by 3.1% to £216,500, in line with the general level of increases received by other employees.

Now that the increased salaries are considered by the Committee to represent the correct level for each role, the Committee anticipates that these salaries will be increased in line with those of the general workforce for the next few years.

- In 2014, we are also amending our policy on paying dividend equivalents on vested performance share plan awards and deferred bonus share awards. Currently, participants do not receive the value of dividends on their awards, and in order to increase alignment with shareholders and bring our arrangements into line with market practice, dividend equivalents will be paid on vested performance share plan awards and deferred bonus share awards granted from 2014.

Since the start of the current financial year I have discussed these changes with a number of our largest shareholders and the Committee has listened carefully to their comments. We welcome feedback from all interested parties and hope that you are able to support our policy and the way in which it has been applied in the year at the Annual General Meeting on 20 March 2014.

Ian Much

Chairman of the Remuneration Committee

Remuneration policy

This report sets out the information required by Part 4 of Schedule 8 to the Large and Medium Sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended). The report also satisfies the relevant requirements of the Listing Rules of the Financial Conduct Authority, and describes how the Board has applied the principles and complied with the provisions relating to directors' remuneration in the UK Corporate Governance Code.

The Remuneration Committee has been established by the Board and is responsible for executive remuneration. The Committee's terms of reference are available in full on the Company's website or from the Company Secretary on request.

In determining remuneration for the executive directors and other senior managers, the Remuneration Committee seeks to maintain a competitive package of rewards, which enables the Company to attract and retain the highest calibre of executive, without being excessive by reference to market rates across comparator companies. Performance-related elements form a significant proportion of the total remuneration package of each executive director, and take into account the individual contribution of each executive and the performance of the business against financial objectives, details of which are set out below. These variable elements are designed to align the interest of executives with shareholders, by ensuring that a significant proportion of remuneration is performance-related and delivered in shares.

The table below summarises the Committee's policy for the remuneration of executive directors, which, if approved by shareholders at the 2014 Annual General Meeting, will become binding immediately thereafter. Further details of the full policy are set out below the table on pages 66 and 67.

Directors' remuneration report

Element	Purpose and link to strategy	Operation
Salary	<ul style="list-style-type: none"> Reflects the performance of the individual, their skills and experience over time, and the responsibilities of the role Provides an appropriate level of basic fixed income, avoiding excessive risk arising from over reliance on variable income 	<ul style="list-style-type: none"> Reviewed annually on 1 January Benchmarked periodically against companies with similar characteristics and companies within the same sector Salaries take account of complexity of the role, market competitiveness, Group performance and the increases awarded to the wider workforce
Bonus	<ul style="list-style-type: none"> Incentivises annual delivery of financial, strategic and personal goals Maximum bonus only payable for achieving demanding targets Delivery of a proportion of bonus in deferred shares provides alignment with shareholders and assists with retention Allowing executives to receive, on vesting, the value of dividends which accrue on deferred shares helps align executives' rewards with shareholders' interests 	<ul style="list-style-type: none"> Paid in cash, with up to 40% deferred as a conditional award of shares Vesting of deferred shares is subject to continued employment (save in "good leaver" scenarios) at the end of three years from the award of the bonus The payment of any earned bonus remains ultimately at the discretion of the Committee Non-pensionable Executives are entitled to receive, on vesting of deferred share awards, the value of dividend payments that would otherwise have been paid on the deferred shares during the deferral period
Long-term incentive plan (performance share plan - "PSP")	<ul style="list-style-type: none"> Incentivises executives to achieve targets aligned to the Group's main strategic objectives of delivering sustainable growth and shareholder returns Allowing executives to receive, on vesting, the value of dividends (in cash or shares) which accrue on deferred shares helps align executives' rewards with shareholders' interests 	<ul style="list-style-type: none"> Annual grants of shares, which vest subject to the Group's performance measured over three years Executives are entitled to receive the value of dividend payments that would otherwise have been paid on vested awards All awards are subject to the discretions given to the Committee in the plan rules during the vesting period
All-employee share schemes	<ul style="list-style-type: none"> All employees, including executives, are encouraged to acquire shares by participating in the Group's all-employee share plans - the UK Sharesave Plan and the US Stock Purchase Plan 	<ul style="list-style-type: none"> The UK Sharesave Plan and US Stock Purchase Plans have standard terms Under the UK Sharesave Plan (the scheme applicable to the current executive directors), participants can enter into a savings contract, in return for which they are granted options to acquire shares at a discount to the market value of the shares at the start of the performance period The rules for the UK Sharesave Plan were approved by shareholders at the 2008 Annual General Meeting
Pension	<ul style="list-style-type: none"> Provides modest retirement benefits that reward sustained contribution 	<ul style="list-style-type: none"> Defined benefit scheme until 6 April 2010, in which pension at a rate of 1/80th of final pensionable salary plus a cash lump sum of 3/80ths accrued for each year of membership. Final pensionable salary was capped at the HMRC notional earnings cap, and the scheme assumed a normal retirement age of 65. The scheme is now closed to future accrual Cash supplement after 6 April 2010, subject to auto-enrolment in the Group Stakeholder Scheme from 1 January 2014
Other benefits	<ul style="list-style-type: none"> Provides a competitive package of benefits that assists with recruitment and retention 	<ul style="list-style-type: none"> Main benefits currently provided to UK executives are a fully-expensed company car or car allowance, life assurance, permanent health insurance and private medical insurance

Notes:

1. A description of how the Company intends to implement the policy set out in this table for 2014 is set out in the annual report on remuneration on pages 76 and 77. The remuneration policy for the executive directors and other senior executives is designed with regard to the policy for employees across the Group as a whole. However, there are some differences in the structure of the remuneration policy for senior executives. In general, these differences arise from the development of remuneration arrangements that are market competitive for the various categories of individuals. They also reflect the fact that, in the case of the executive directors and senior executives, a greater emphasis tends to be placed on performance-related pay in the market.

Maximum	Performance assessment
<ul style="list-style-type: none"> Salary increases will normally be in line with those received by the wider workforce More significant increases may be awarded at the discretion of the Committee, for example where there is a change in responsibilities, to reflect individual development and performance in the role 	<ul style="list-style-type: none"> None, although overall individual performance is a factor considered when setting and reviewing salaries
<ul style="list-style-type: none"> Chief Executive - 125% of salary Other executive directors - 100% of salary 	<ul style="list-style-type: none"> Mix of Group financial objectives and personal objectives - financial performance targets will determine the majority of the award and will typically include measures such as EPS and cash flow, although the Committee has discretion to set other targets Personal objectives will be measurable and linked to goals that are consistent with the Group's longer-term goals No bonus will be paid in respect of any element unless threshold financial performance targets have been achieved Performance below threshold results in zero payment. Payment rises from 0% to 100% of the maximum opportunity for levels of performance between threshold and maximum with 50% of the maximum payable for on-target performance The Committee has discretion to reduce (potentially to zero) any bonus payout based on its assessment of the health and safety performance of the Group or an individual business within the Group Includes a clawback mechanism in the event of a material misstatement of the Group's financial results
<ul style="list-style-type: none"> Normally 150% of base salary (although grants up to 200% of base salary may be made in exceptional circumstances such as on recruitment) 	<ul style="list-style-type: none"> Awards made prior to 2014 are based on the conditions described on page 81 of this report Awards from 2014 onwards will be subject to targets based on EPS growth and relative TSR vs a peer group of international defence sector companies. For the awards to be granted in 2014, each measure will determine the vesting of 50% of the award; however, the Committee will have discretion to set different weightings for awards in future years Targets for the EPS condition are set by the Remuneration Committee prior to each grant. Targets for the relative TSR condition are based on a sliding scale, with median representing threshold performance and upper quartile representing maximum performance For each measure, performance below threshold results in zero payment. Payment rises from 25% to 100% of the maximum opportunity for that measure for levels of performance between threshold and maximum Includes a clawback mechanism in the event of a material misstatement of the Group's financial results
<ul style="list-style-type: none"> Participation limits are those set by the relevant tax authorities from time to time 	<ul style="list-style-type: none"> N/A
<ul style="list-style-type: none"> Post 6 April 2010 - 20% of base salary cash supplement paid in lieu of occupational pension scheme membership However, from 1 January 2014, all UK employees, including the executive directors, are subject to auto-enrolment into the Group's defined contribution stakeholder scheme, with an employer contribution of 4% of base salary. If executives do not opt out of this scheme, their cash supplement will be reduced by 4% 	<ul style="list-style-type: none"> N/A
<ul style="list-style-type: none"> Company car up to an annual lease cost of £12,000 or cash allowance of up to £25,000 per annum Other benefits will be in line with market. The value of each benefits is based on the cost to the Company and is not pre-determined 	<ul style="list-style-type: none"> N/A

2. For the year ended 31 October 2013, Mark Papworth and Steve Bowers were each entitled to a minimum bonus of 50% of salary.

3. All-employee share plans do not have performance conditions. Executive directors are eligible to participate in the UK Sharesave Plan on the same terms as other employees.

4. Copies of the PSP rules are available on request from the Company Secretary.

5. As described on page 82, the Company operates share ownership guidelines requiring executive directors to acquire and hold a specified level of shareholding.

Directors' remuneration report

Committee discretions

The Committee operates the Group's variable incentive plans according to their respective rules and in accordance with HMRC rules where relevant. To ensure the efficient administration of these plans, the Committee will apply certain operational discretions. These include the following:

- selecting the participants in the plans on an annual basis;
- determining the timing of grants of awards and/or payment;
- determining the quantum of awards and/or payments (within the limits set out in the policy table above);
- determining the extent of vesting based on the assessment of performance;
- making the appropriate adjustments required in certain circumstances (e.g. change of control, rights issues, corporate restructuring events, and special dividends);
- determining "good leaver" status for incentive plan purposes and applying the appropriate treatment; and
- undertaking the annual review of weighting of performance measures, and setting targets for the annual bonus plan and PSP from year to year.

If an event occurs which results in the annual bonus plan or PSP performance conditions and/or targets being deemed no longer appropriate (e.g. a material acquisition or divestment), the Committee will have the ability to adjust appropriately the measures and/or targets and alter weightings, provided that the revised conditions or targets are not materially less difficult to satisfy.

Outstanding share incentive awards that remain unvested or unexercised at the date of this report, as detailed on pages 81 and 82 of the annual report on remuneration, remain eligible for vesting or exercise based on their original award terms.

Selection of performance metrics and targets

The performance-related elements of remuneration take into account the Group's risk policies and systems, and are designed to align the senior executives' interests with those of shareholders. The Committee reviews the annual bonus plan measures set for all of the Group's senior executives (not just the executive directors) every year, in order to ensure that they are aligned with the Group's strategy and to ensure consistent bonus arrangements amongst the senior executive team. All financial targets are set on a sliding scale. Non-financial targets are set at the beginning of the year based on individual and management team responsibilities.

The annual bonus plan performance metrics include a mix of financial targets and personal objectives, reflecting the key annual priorities of the Group. The financial metrics determine the majority of the bonus and normally include cash flow – a key measure of the Group's ability to invest in the business and pay dividends to its shareholders – and EPS, which reflects the Group's financial performance and is a key measure for its shareholders. The personal objectives agreed on an annual basis will be measurable and based on individual performance, and will be consistent with the achievement of the Group's longer-term goals.

The Remuneration Committee has decided to apply TSR and EPS performance conditions to awards to be made under the PSP in 2014 and future years, as these measures are directly aligned to the success of the Group's recovery. EPS is a measure of the Group's overall financial success and TSR provides an external assessment of the Company's performance against its peer group. TSR also aligns the rewards received by executives with the returns received by shareholders. The actual EPS performance targets for PSP awards to be granted in 2014 have not yet been determined but in accordance with the normal practice, will appropriately reflect market expectations for the Company at the time of grant, as well as the Board's own internal expectations. The performance targets will be disclosed in the relevant RIS announcement when the awards are granted. Further details on the TSR targets for 2014 awards are set out on page 77 of the annual report on remuneration.

The Committee will review the choice and relative balance of performance measures and the appropriateness of performance targets prior to each grant of awards under the PSP. The EPS targets are reset prior to each grant, following a review of internal and external expectations of future EPS growth for the Group. The TSR comparator group is reviewed prior to each grant to ensure it remains appropriate. The Committee retains discretion to set different targets for future awards, providing that, in the opinion of the Committee, the new targets are no less challenging in light of the prevailing circumstances than those set previously.

How employees' pay is taken into account

In addition to determining the remuneration arrangements for the executive directors, the Committee considers and approves the base salaries for sixteen other senior executives, and reviews salaries for the next tier of management at each of the Group's businesses. The Committee also receives information on general pay levels and policies across the Group. The Committee, therefore, has due regard to salary levels across the Group in applying its remuneration policy.

How the executive directors' remuneration policy relates to the wider Group

The remuneration policy described above provides an overview of the structure that operates for the most senior executives in the Group. Lower aggregate incentive quanta are applied at below executive level, with levels driven by market comparatives and the impact of the role.

Employees are provided with a competitive package of benefits, which typically includes participation in the Group's defined contribution pension arrangements.

Long-term incentives are provided to the most senior executives and those identified as having the greatest potential to influence performance within the Group. However, in order to encourage wider employee share ownership, the Company also operates a Sharesave Plan in the UK and a Stock Purchase Plan in the US, in which all UK and US employees are eligible to participate on completion of six months' service.

How shareholders' views are taken into account

The Remuneration Committee considers shareholder feedback received on the directors' remuneration report each year and guidance from shareholder representative bodies more generally. Shareholders' views are key inputs when shaping remuneration policy.

In December 2013 and January 2014, the Committee consulted with the Company's largest shareholders on the proposed changes for 2014, including the choice and weighting of performance measures in the incentive arrangements and the level of salary increases for the executive directors. The feedback received has been reflected in the policy that is presented in this report.

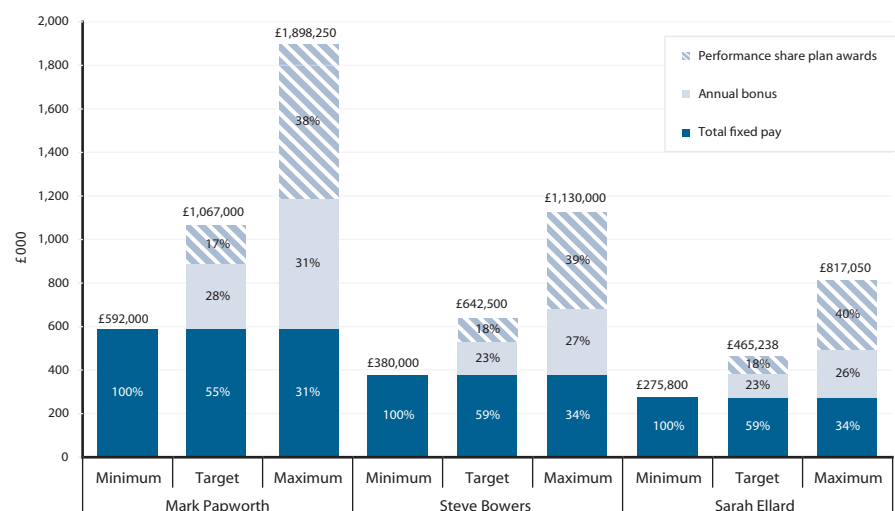
Legacy arrangements

For the avoidance of doubt, in approving this policy, authority is given to the Company to honour any commitments entered into with current or former directors (such as the payment of a pension or the unwinding of legacy share schemes) that have been disclosed to shareholders in previous directors' remuneration reports. Details of any payments to former directors will be set out in the annual report on remuneration as they arise.

Directors' remuneration report

Potential remuneration scenarios for executive directors

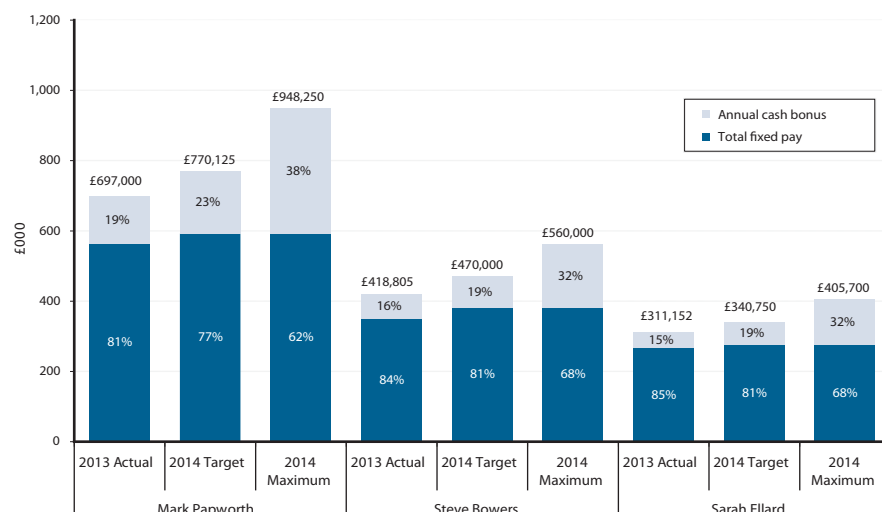
The chart below details the hypothetical composition of each executive director's remuneration package and how it could vary at different levels of performance under the future policy set out above. The executive directors will not receive either the "target" or "maximum" packages in 2014, as there are no performance share plan awards due to vest.



Assumptions:

1. Minimum = fixed pay only (2014 salary plus benefits plus pension cash supplement).
On target = fixed pay plus target annual bonus of 62.5% of salary for the Chief Executive and 50% for the other executive directors plus target PSP awards of 37.5% of salary for the Chief Executive and other executive directors.
Maximum = fixed pay plus maximum annual bonus of 125% of salary for the Chief Executive and 100% for the other executive directors plus maximum PSP awards of 150% of salary for the Chief Executive and other executive directors.
2. The PSP awards section of the bars is shaded, as these awards are subject to performance in future years and cannot ordinarily vest until three years after grant.
3. Salary levels (on which other elements of the packages are calculated) are based on those applying to 31 December 2013.
4. The value of taxable benefits is based on an estimated cost of £22,000 for Mark Papworth, £20,000 for Steve Bowers and £16,000 for Sarah Ellard.
5. Pension provision is 20% of salary for each director.
6. The executive directors may participate in all-employee share schemes on the same basis as other employees. The value that may be received under these schemes is subject to tax-approved limits. For simplicity, the value that may be received from participating in these schemes has been excluded from the above charts.

The additional chart below compares the actual realisable value of each executive director's remuneration package for 2013 with the potential scenarios set out above, taking account of the fact no deferred bonus shares or performance share plan awards are due to vest during 2013 or 2014.



Assumptions:

1. 2013 Actual = fixed pay (2013 annualised salary plus benefits plus pension cash supplement) plus the cash element of the 2013 bonus award.
2014 Target = fixed pay (2014 salary plus benefits plus pension cash supplement) plus target annual cash bonus of 37.5% of salary for the Chief Executive and 30% for the other executive directors.
Maximum = maximum annual cash bonus of 75% of salary for the Chief Executive and 60% for the other executive directors.
2. Other assumptions as above.

Policy on payments for loss of office

All new executive directors appointed will have service contracts which are terminable on a maximum of twelve months' notice. Provisions permitting the Company to make any termination payments by instalments, and requiring directors to mitigate their loss in such circumstances, will be included in each contract. The Remuneration Committee will exercise discretion in determining whether termination payments should be paid by instalments, taking account of the reason for the departure of the director and their prior performance. Other than in gross misconduct situations, the Company would expect to honour the contractual entitlements of terminated directors.

Other than in certain "good leaver" circumstances (including, but not limited to, redundancy, ill-health or retirement), no bonus would be payable unless the individual remains employed and is not under notice at the payment date. Any bonuses paid to a "good leaver" would be based on an assessment of their individual and the Company's performance over the period, and prorated for the proportion of the bonus year worked.

With regards to long-term incentive awards, the PSP rules provide that other than in certain "good leaver" circumstances, awards lapse on cessation of employment. Where an individual is a "good leaver", the Remuneration Committee's policy for future PSP awards will be to permit awards to remain outstanding until the end of the original performance period, when a pro rata reduction will be made to take account of the proportion of the vesting period that lapsed prior to termination of employment, although the Committee has discretion to partly or completely disapply prorating and the performance conditions in exceptional circumstances. The Remuneration Committee has discretion to deem an individual to be a "good leaver". In doing so, it will take account of the reason for their departure and the performance of the individual.

Deferred bonus share awards will also normally lapse on cessation of employment, unless the executive director is deemed to be a "good leaver" by the Remuneration Committee, as referred to above.

The Committee will have authority to settle legal claims against the Company (e.g. for unfair dismissal, discrimination or whistleblowing) that arise on termination. The Committee may also authorise the provision of outplacement services.

Directors' remuneration report

Executive directors' service agreements and loss of office payments

The current executive directors have rolling service contracts, details of which are summarised in the table below:

Provision	Detailed terms
Contract dates	Mark Papworth - 22 October 2012 (effective 5 November 2012) Steve Bowers - 2 January 2013 (effective 7 January 2013) Sarah Ellard - 2 November 2011 (effective 7 October 2011)
Notice period	Twelve months from both the Company and from the executive
Termination payment¹	Contracts may be terminated without notice by the payment of a sum equal to the sum of salary due for the unexpired notice period plus the fair value of any contractual benefits (including pension) Payments may be made in instalments and in these circumstances there is a requirement to mitigate loss
Incentive arrangements	A pro-rata bonus may also become payable for the period of active service, along with vesting of outstanding performance share plan and deferred bonus share awards (see above)

Notes:

1. Mark Papworth's contract originally contained additional provisions in the event of a change of control; however, these ceased to apply from 5 November 2013.

The executive directors' service contracts are available for inspection at the Company's registered office.

Recruitment of executive directors

Salaries for new hires (including internal promotions) will be set to reflect their skills and experience, the Company's intended pay positioning, and the market rate for the applicable role.

Where it is appropriate to offer a below median salary initially, the Committee will have the discretion to allow phased salary increases over a period of time for newly-appointed directors, even though this may involve increases in excess of the rate for the wider workforce and inflation.

Benefits will be provided in line with those offered to other executive directors, taking account of local market practice, with relocation expenses or arrangements provided if necessary. Tax equalisation may also be considered if an executive is adversely affected by taxation due to their employment with the Company. Legal fees and other costs incurred by the individual may also be paid by the Company.

The aggregate incentive opportunity offered to new recruits will normally be no higher than that offered under the annual bonus plan and the PSP to the existing executive directors. Different performance measures and targets may be set initially for the annual bonus plan, taking into account the responsibilities of the individual and the point in the financial year at which they join. Any increases in incentive quantum offered above this limit will be contingent on the Company receiving shareholder approval for an amendment to its approved policy at its next general meeting.

Current entitlements (benefits, bonus, share schemes) may be bought out on terms that are no more favourable than a like-for-like basis (with a comparable time horizon, fair value and subject to performance conditions). The Group's existing incentive arrangements will be used to the extent possible, although awards may also be granted outside of these schemes, if necessary, and as permitted under the Listing Rules.

In the case of an internal hire, any outstanding variable pay awarded in relation to the previous role will be allowed to pay out according to its terms of grant (adjusted as relevant to take into account the Board appointment).

Policy for non-executive directors

Element	Purpose and link to strategy	Operation	Maximum	Performance assessment
Non-executive directors' and Chairman's fees	<ul style="list-style-type: none"> Takes account of recognised practice and set at a level that is sufficient to attract and retain high-calibre non-executives 	<ul style="list-style-type: none"> The Chairman is paid a single fee for all his responsibilities. The non-executive directors are paid a basic fee. The Chairs of the Remuneration Committee and the Audit Committee each receive additional fees to reflect their extra responsibilities When reviewing fee levels, account is taken of market movements in non-executive director fees, Board committee responsibilities, ongoing time commitments, the general economic environment and the level of increases awarded to the wider workforce Fee increases, if applicable, are normally effective from April of each year Non-executive directors do not participate in any pension, bonus or share incentive plans. However, the Company provides private medical insurance in respect of Peter Hickson and his spouse In exceptional circumstances, additional fees may be paid where there is a substantial increase in the time commitment required of non-executive directors 	<ul style="list-style-type: none"> N/A 	<ul style="list-style-type: none"> N/A

Non-executive directors' letters of appointment

Non-executive directors do not receive compensation for loss of office but are appointed for a fixed term of three years, renewable for further three year terms if both parties agree and subject to annual re-election by shareholders. Peter Hickson's appointment may be terminated on six months' notice by either party, and the other non-executive directors' appointments may be terminated on three months' notice by either party.

The following table shows details of the terms of appointment for the non-executive directors:

Name	Date original term commenced	Date current term commenced	Expected expiry date of current term
Peter Hickson (Chairman)	1 July 2010 (Chairman since 1 October 2010)	1 July 2013	30 June 2016
Andy Hamment	1 July 2013	1 July 2013	30 June 2016
Ian Much	1 December 2004	1 December 2013	Rolling
Vanda Murray	1 November 2011	1 November 2011	31 October 2014
Nigel Young	1 May 2013	1 May 2013	30 April 2016

Directors' remuneration report

Annual report on remuneration

This part of the report has been prepared in accordance with Part 3 of Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended), and 9.8.6R of the Listing Rules. The annual report on remuneration will be put to an advisory shareholder vote at the 2014 Annual General Meeting. The information on pages 76 to 85 has been audited.

The Remuneration Committee and its advisers

Members of the Remuneration Committee







Name	From	To
Ian Much (Chairman)	1 December 2004	Present
Roger Freeman	26 May 2006	31 December 2013
Andy Hamment	1 July 2013	Present
Peter Hickson	1 July 2010	Present
Vanda Murray	1 November 2011	Present
Peter Norriss	1 May 2004	20 March 2013
Nigel Young	1 May 2013	Present

The Group Legal Director & Company Secretary acts as secretary to the Committee and the Chief Executive attends meetings by invitation but no executive director or other employee is present during discussions relating to their own remuneration.

Meetings

The Remuneration Committee met formally six times during the year. In addition, two additional ad hoc meetings were convened to deal with matters arising between scheduled meetings. Details of the attendance of the Committee members at scheduled meetings are set out on page 57 of the corporate governance report.

Principal activities of the Remuneration Committee during the year

December 2012 	January 2013 	February 2013 	March 2013 
Approval of remuneration packages for the new Finance Director and HR Director	Approval of senior management bonus payments for the 2012 financial year	Briefing on the new directors' remuneration reporting requirements	Consideration of future remuneration policy for executive directors
	Approval of annual salary increases for the Group Legal Director & Company Secretary and other members of the senior management team		Approval of 2013 bonus plan targets
	Consideration of short-term retention arrangements for key employees below Board level across the Group		Approval of termination arrangements for certain senior executives
	Approval of performance condition and granting of awards under the performance share plan		
	Consideration of letter to major shareholders on remuneration-related matters		
	Approval of directors' remuneration report		
June 2013 	September 2013 		
Further consideration of future remuneration policy	Review of policy on contractual notice periods for senior executives		
Approval of performance share plan award			

Advisers

During the year, the Committee retained New Bridge Street (an Aon Hewitt company, part of Aon plc) to advise on remuneration and incentive plan related matters and the setting of remuneration for new appointments. New Bridge Street was appointed by the Committee and is a signatory to the Remuneration Consultants' Group Code of Conduct, which sets out guidelines to ensure that its advice is independent and free from undue influence. The Company received no other services from New Bridge Street, or any other part of the Aon group of companies, during the year. The fees paid to New Bridge Street in 2013 were £65,936 (2012: £27,198). The Committee reviews the performance and independence of its advisers on an annual basis.

The Committee consults internally with the Chief Executive, Mark Papworth, and the Group Legal Director & Company Secretary, Sarah Ellard.

Directors' remuneration report

Application of the remuneration policy for 2014

Base salary

The executive directors' salaries were reviewed in early January 2014. The salary increases, which took effect from 1 January 2014, are set out below. The background to the increases applied to Mark Papworth's and Steve Bowers' salaries are set out in the statement by the Chairman of the Remuneration Committee on pages 64 and 65. The percentage increase applied to Sarah Ellard's salary was consistent with the average salary increase to UK employees.

	Salary as at 1 January 2013 (or date of appointment, if later)	Salary as at 1 January 2014	% Increase
Mark Papworth	£450,000	£475,000	5.6%
Steve Bowers	£275,000	£300,000	9.1%
Sarah Ellard	£210,000	£216,500	3.1%

Fees for the Chairman and non-executive directors

As detailed in the remuneration policy, the Company's approach to setting the non-executive directors' remuneration takes account of recognised practice, and is set at a level that is sufficient to attract and retain high-calibre non-executives. Details of the fees are set out below:

	Fees as at 1 January 2013	Fees as at 1 January 2014	% Increase
Chairman's fees	£170,000	£187,000	10% ¹
Other non-executive directors' base fee	£55,000	£55,000	-
Audit Committee Chair fee	£8,000	£8,000	-
Remuneration Committee Chair fee	£8,000	£8,000	-

Notes:

1. The Chairman's annual fees of £187,000 have been fixed for his current three year term of appointment, which expires on 30 June 2016. His previous annual fee of £170,000 was also fixed for his original three year term.

Annual bonus plan performance targets

The annual bonus plan for 2014 will largely operate on a similar basis to 2013. However, in 2013, the weighting of personal objectives was increased to 40% of the total bonus opportunity on an exceptional basis, reflecting the importance of delivering key strategic and operational goals in the year. For the 2014 bonus plan, the weighting of personal objectives for Mark Papworth and Sarah Ellard has reverted back to 25% of the total bonus opportunity. However, Steve Bowers' personal objectives will contribute to 35% of his bonus opportunity for 2014, as the Committee feels that a slightly greater weighting on personal objectives is appropriate for Steve, given the importance of addressing the currently complex position in relation to debt holders and improving financial management in the business. The personal objectives set for Steve will reflect these priorities, and will include targets relating to the Group's discussions with debt holders and restructuring the balance sheet.

In 2014, the performance measures and weightings for the annual bonus plan will therefore be as follows:

Measure	As a percentage of maximum bonus opportunity		
	Mark Papworth	Steve Bowers	Sarah Ellard
EPS	37.5%	32.5%	37.5%
Cash flow	37.5%	32.5%	37.5%
Personal objectives	25.0%	35.0%	25.0%

No bonus will be payable in respect of the personal objectives unless threshold performance has been achieved against both the EPS and cash flow targets. Further details of the targets are not being disclosed prospectively as these are commercially sensitive. A detailed description of the personal objectives and performance against them will be included in next year's annual report on remuneration.

The 2014 bonus plan is consistent with the policy detailed in the remuneration policy in terms of maximum bonus opportunity, deferred share arrangements and clawback.

Long-term incentive targets

The policy for annual awards granted to the executive directors under the PSP in 2014 and beyond will be to use two metrics, namely growth in adjusted EPS and relative TSR measured against an international peer group of defence sector companies as listed below. Each metric will determine the vesting of 50% of the 2014 awards. 25% of each part of the award will vest for threshold or median performance, with full vesting of each part of the award for stretch or upper quartile performance. The EPS performance targets for 2014 have not yet been determined but in accordance with the Committee's normal practice, will appropriately reflect market expectations for the Company at the time of grant, as well as the Board's own internal expectations. The performance targets will be disclosed in the relevant RIS announcement when the awards are granted.

The defence sector peer group for the 2014 awards comprises: Alliant Techsystems; BAE Systems; Cobham; Cohort; Esterline Technologies; Finmeccanica; FLIR Systems; L3 Communications; Manroy; Qinetiq Group; Raytheon; Rheinmetall; Rockwell Collins; and Ultra Electronics.

Directors' emoluments

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

	Year	Salaries and fees £000	Taxable benefits ¹ £000	Bonus (cash and deferred shares) ³ £000	PSP £000	Pension benefits ² £000	Total £000
Executives							
Mark Papworth (appointed 5 November 2012)	2013	450	20	225	-	90	785
	2012	-	-	-	-	-	-
Steve Bowers (appointed 7 January 2013)	2013	226	15	115	-	45	401
	2012	-	-	-	-	-	-
Sarah Ellard	2013	208	16	76	-	42	342
	2012	200	16	-	49	40	305
Non-executives							
Roger Freeman ⁴ (retired 31 December 2013)	2013	63	-	-	-	-	63
	2012	63	-	-	-	-	63
Andy Hamment (appointed 1 July 2013)	2013	18	-	-	-	-	18
	2012	-	-	-	-	-	-
Peter Hickson	2013	176	2	-	-	-	178
	2012	170	2	-	-	-	172
Ian Much ⁴	2013	63	-	-	-	-	63
	2012	63	-	-	-	-	63
Vanda Murray	2013	55	-	-	-	-	55
	2012	55	-	-	-	-	55
Peter Norriss (retired 20 March 2013)	2013	23	2	-	-	-	25
	2012	55	2	-	-	-	57
Nigel Young (appointed 1 May 2013) ^{4,5}	2013	32	-	-	-	-	32
	2012	-	-	-	-	-	-
Total remuneration	2013	1,314	55	416	-	177	1,962
	2012	606	20	-	49	40	715

Notes:

1. Comprises a fully-expensed company car for Sarah Ellard (annual lease cost £9,000) or cash allowance (£20,000 for Mark Papworth and £18,000 for Steve Bowers), plus private medical insurance.
2. The executive directors receive a cash supplement of 20% of salary in lieu of occupational pension scheme membership.
3. 40% of any bonus is delivered as an award of deferred shares.
4. Nigel Young and Ian Much each receive an additional fee of £8,000 per annum, included in the figures above, in respect of their Chairmanship of the Audit Committee and the Remuneration Committee respectively. Roger Freeman also received this additional fee during his tenure as Chairman of the Audit Committee. Ian Much also serves as the Senior Independent Director but he receives no additional fee for this role.
5. Nigel Young's emoluments do not include the remuneration he received during his appointment as Interim Chief Financial Officer, prior to his appointment to the Board.

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

Directors' remuneration report

Details of variable pay earned in the year

Annual bonus

The Committee has consistently set highly challenging bonus targets for the achievement of maximum bonuses. No bonuses were paid to executive directors for 2011 and 2012, and the executive directors did not receive maximum bonuses in any of the prior three years.

As disclosed last year and as described in the Statement by the Committee Chairman as part of their recruitment terms, Mark Papworth and Steve Bowers each had an entitlement to a minimum bonus of 50% of salary for 2013 only.

In 2013, the annual bonus plan threshold performance was not achieved in relation to either the EPS or cash flow targets, as a consequence of the difficult trading conditions which impacted the Group's performance during the year. The actual financial performance targets are not disclosed, as they are considered to be commercially sensitive. The performance against the personal objectives element of the annual bonus plan is set out below:

Personal objectives (40% of bonus opportunity)		Performance against individual objectives	Overall performance against objectives - % of salary	Bonus cash - % of salary	Deferred share award - % of salary
Mark Papworth	• Develop a new health and safety strategy for the Group, and implement improvements to the existing arrangements	●	38.5%	30% ¹	20% ¹
	• Completion of organisational restructuring activities	●			
	• Complete integration of six business units	●			
	• Progression of potential divestments	●			
	• Develop key customer relationships	●			
	• Progression of certain joint venture arrangements	●			
	• Implementation of enhancements to the Group's integrity programme	●			
Steve Bowers	• Secure amendments to the Group's financing covenants	●	36%	25% ²	16.7% ²
	• Deliver improvements to the Group's financial reporting process and financial systems	●			
	• Implement an enhanced financial forecasting regime	●			
	• Develop enhanced treasury and tax strategies	●			

Personal objectives (40% of bonus opportunity)		Performance against individual objectives	Overall performance against objectives - % of salary	Bonus cash - % of salary	Deferred share award - % of salary
Sarah Ellard	<ul style="list-style-type: none"> • Completion of organisational restructuring activities • Progression of potential divestments • Progression of certain joint venture arrangements • Completion of restructuring of pension arrangements • Rationalisation of Group property portfolio • Review of operating policies and procedures following organisational restructuring • Implementation of enhancements to the Group's integrity programme 	<ul style="list-style-type: none"> ● ● ● ● ● ● ● 	36%	21.6%	14.4%

Notes:

1. Mark Papworth was entitled to a 50% minimum bonus for 2013.
2. Steve Bowers was also entitled to a 50% minimum bonus for 2013 - this has been prorated to reflect his January 2013 start date to a total bonus of 41.7%.
3. Details of personal objectives have been included above to the extent that such disclosure is not commercially sensitive.
4. Vesting of deferred bonuses is subject only to continued service.

Directors' remuneration report

Performance share plan

Vesting of 2011 PSP awards

The PSP awards granted on 19 January 2011 were based on the Group's performance to 31 October 2013. The performance condition for these awards was as follows:

Condition	Threshold vesting	Full vesting	Actual	Vesting
Total earnings per share growth per annum (not compound) over three financial years	RPI + 10% p.a. (25% vests for awards up to 100% of salary) RPI + 25% p.a. (for any additional awards over 100% of salary)	RPI + 25% p.a. (for awards up to 100% of salary) RPI + 35% p.a. (for awards up to 150% of salary)	(19.1%)	0%

Based on the above, all PSP awards granted on 19 January 2011 will lapse. Only one current executive director received an award under this grant. Details of the award are provided below:

Executive	Vesting date	Number of shares at grant	Number of shares to vest	Number of share to lapse	Value of dividends
Sarah Ellard	19 January 2014	25,520	Nil	25,520	Nil

PSP awards granted in the year

On 21 November 2012 and 31 January 2013, the following conditional awards of shares were granted to the executive directors under the PSP:

Executive	Date of grant	Value of award	Closing share price on date of grant	Number of conditional shares awarded	Face value	% that vests at threshold	Vesting determined by
Mark Papworth	21 November 2012	200% of salary	217.0p	413,412	£897,104	25%	Average share price between
Steve Bowers	31 January 2013	150% of salary	283.6p	149,564	£424,164	25%	1 August 2015 and
Sarah Ellard	31 January 2013	150% of salary	283.6p	114,213	£323,908	25%	31 October 2015

Award levels were calculated based on the closing share price on the trading day immediately preceding the date of grant. The face value of each award shown above is based on the closing share price on the date of grant.

Performance conditions for outstanding awards

The awards made to the executive directors in November 2012 and January 2013 are subject to a performance condition based on the Company's average share price over a three month period from 1 August 2015 to 31 October 2015. The targets for these awards (and other outstanding awards to executive directors) are summarised in the table below:

	Measure	Director	Awards to executive directors	Threshold vesting	Full vesting
Awards made on 19 January 2011	Total earnings per share growth¹ per annum (not compound) over three financial years	Sarah Ellard	150% of salary	RPI + 10% p.a. (25% vests for awards up to 100% of salary) RPI + 25% p.a. (for any additional awards over 100% of salary)	RPI + 25% p.a. (for awards up to 100% of salary) RPI + 35% p.a. (for any additional awards up to 150% of salary)
Awards made on 27 January 2012	Total earnings per share growth¹ per annum (not compound) over three financial years	Sarah Ellard	150% of salary	3% p.a. (15% vests) 5% p.a. (25% vests) 10% p.a. (for any additional awards over 100% of salary)	10% p.a. (for awards up to 100% of salary) 12.5% p.a. (for any additional awards up to 150% of salary)
Awards made on 21 November 2012	Average share price from 1 August 2015 to 31 October 2015	Mark Papworth	200% of salary	275p (25% vests)	500p or more (100% vests)
Awards made on 31 January 2013	Average share price from 1 August 2015 to 31 October 2015	Steve Bowers Sarah Ellard	150% of salary	350p (25% vests)	500p or more (100% vests)

Notes:

1. Earnings per share is calculated on a fully-diluted and normalised basis, as specified by the Committee prior to grant.

Summary of outstanding PSP awards

	At 1 November 2012	Awarded during the year	Lapsed during the year	Number of shares under award		Date of vesting	Closing share price on date of grant (p)
				Vested during the year	At 31 October 2013		
Mark Papworth	-	413,412	-	-	413,412	21 November 2015	217.0
	-	413,412	-	-	413,412		
Steve Bowers	-	149,564	-	-	149,564	31 January 2016	283.6
	-	149,564	-	-	149,564		
Sarah Ellard	16,460	-	16,460	-	-	20 January 2013	615.0
	25,520	-	-	-	25,520	19 January 2014	636.8
	79,197	-	-	-	79,197	27 January 2015	387.3
	-	114,213	-	-	114,213	31 January 2016	
	121,177	114,213	16,460	-	218,930		

Notes:

1. None of the awards granted on 20 January 2010 vested as the threshold earnings per share performance target was not met.

2. As explained above, the awards granted on 19 January 2011 will lapse as the threshold earnings per share performance target has not been met.

Directors' remuneration report

Sharesave awards

On 30 July 2013, the following options were granted to the executive directors under the Chemring Group 2008 UK Sharesave Plan:

Executive	Number of share options	Exercise price	Exercise date
Mark Papworth	6,276	239p	1 October 2018 - 1 April 2019
Steve Bowers	6,276	239p	1 October 2018 - 1 April 2019
Sarah Ellard	3,765	239p	1 October 2016 - 1 April 2017

Deferred share awards

As no bonuses were paid to the executive directors for 2011 and 2012, there are no outstanding deferred share awards.

Directors' shareholdings

Shareholding guidelines apply to executive directors and other participants in the PSP. Executive directors are expected to build-up and maintain a shareholding in the Company equivalent to one year's basic salary, by retaining 50% of the after-tax gain on vested PSP awards until such time as the guidelines have been met. Other participants in the PSP are expected to retain a shareholding equivalent to 25% to 50% of their basic salary.

The interests of the directors in the ordinary shares of the Company at 31 October 2013 are shown below. All are beneficial holdings.

	Legally owned (number of shares)	Value of legally owned shares as % of salary ¹	Guideline met?	Unvested and subject to performance conditions under the PSP					
				2011 award	2012 award	2013 award	Total at 31 Oct 2013	Sharesave	
Mark Papworth	100,000	48%	No	-	-	413,412	413,412	6,276	
Steve Bowers	-	-	No	-	-	149,564	149,564	6,276	
Sarah Ellard	48,875	50.6%	No	25,520	79,197	114,213	218,930	3,765	
Roger Freeman	1,750	-	-	-	-	-	-	-	
Andy Hamment	50,000	-	-	-	-	-	-	-	
Peter Hickson	160,000	-	-	-	-	-	-	-	
Ian Much	26,500	-	-	-	-	-	-	-	
Vanda Murray	3,000	-	-	-	-	-	-	-	
Nigel Young	-	-	-	-	-	-	-	-	

Notes:

1. Based on the number of shares legally owned, prevailing base salary and share price of 217.5p, at 31 October 2013.

The directors' share interests at 31 October 2013 include shares held by the directors' adult children, as required by the Companies Act 2006.

There have been no changes to the directors' interests in shares since 31 October 2013.

Pension

The following table sets out the pension benefits earned by Sarah Ellard during her former membership of the Chemring Group Staff Pension Scheme.

	Total benefit accrued at 31 Oct 2012		Transfer value of accrued benefit at 31 Oct 2012	Total benefit accrued at 31 Oct 2013		Transfer value of accrued benefit at 31 Oct 2013	Increase in transfer value during year (less members' contributions)
	Pension £p.a.	Cash £		Pension £p.a.	Cash £		
Sarah Ellard	23,948	71,844	429,659	23,948	71,844	460,587	30,928

Notes:

1. Transfer values represent liabilities of the applicable scheme, and do not represent sums paid to individuals.
2. Transfer values have been calculated in accordance with the Occupational Pension Scheme (Transfer Value) Regulations 1996.
3. Sarah Ellard left pensionable service on 6 April 2010 and therefore has not accrued additional pension over the year. The accrued benefits shown are the benefits at the date of exit.
4. The scheme provided pension at a rate of 1/80th of final pensionable salary plus a cash lump sum of 3/80ths for each year of membership. Final pensionable salary was capped at the HMRC notional earnings cap, and the scheme assumed a normal retirement age of 65. Early retirement is permissible from age 55 but accrued benefits are reduced accordingly using the early retirement factors in force at the date of early retirement.

Loss of office payments

No compensation for loss of office was paid to any director during the year. The principles governing compensation for loss of office are set out on page 71.

Payments to past directors

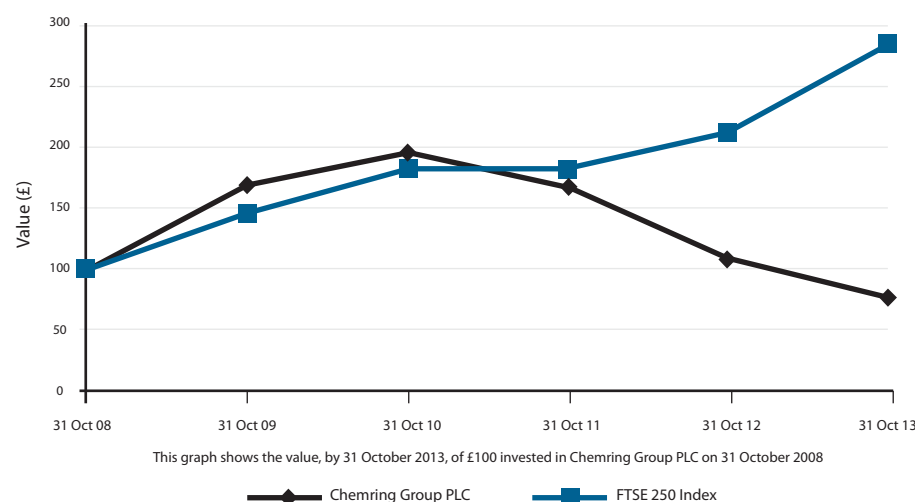
No payments were made to past directors during the year.

Performance graph and table

The following graph shows the Company's cumulative total shareholder return over the last five financial years relative to the FTSE 250 Index. 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.

Total shareholder return

Source: Thomson Reuters



Directors' remuneration report

Chief Executive's remuneration

The total remuneration figures for the Chief Executive during each of the last five financial years are shown in the table below. It should be noted that Mark Papworth was not in this position for all five years shown but replaced David Price on 5 November 2012. The total remuneration figure for 2012 includes the payment made to David Price for loss of office.

The total remuneration figure includes the annual bonus based on that year's performance and vested PSP awards based on the three year performance period ending in the relevant year. The annual bonus payout and PSP award vesting level as a percentage of the maximum opportunity are also shown for each of these years.

		David Price			Mark Papworth
	2009	2010	2011	2012	2013
Total remuneration (£000)	1,309	1,391	1,239	1,325	785
Annual bonus (% of maximum)	94%	62%	0%	0%	40%
PSP awards vesting (% of maximum)	100%	100%	100%	54.375%	0%

Percentage change in the Chief Executive's remuneration

The table below shows the percentage change in the Chief Executive's total remuneration (excluding the value of any PSP awards and pension benefits receivable in the year) between the 2012 and 2013 financial years, compared to that of the average for all eligible employees of the Group.

	% Change from 2012 to 2013		
	Salary	Benefits	Annual bonus
Chief Executive	(14.3%)	(39.4%)	N/A
Average of other employees	1.3%	8.1%	66.6%

Relative importance of spend on pay

The following table shows the Company's actual spend on pay (for all employees) relative to dividends and retained profits.

	2013 £m	2012 £m	% change
Staff costs	172.1	189.8	(9%)
Dividends	13.9	18.4	(24%)
Retained profits	172.5	235.8	(27%)

£1.3 million of the staff costs figure for 2013 relates to pay for the executive directors. This is different to the aggregate of the single figures for the year under review due to the way in which share-based awards are accounted for.

The dividends figures relate to amounts payable in respect of the relevant financial year.

Shareholder voting on the directors' remuneration report at the 2013 Annual General Meeting

At last year's Annual General Meeting held on 20 March 2013, the directors' remuneration report received the following votes from shareholders:

	Total number of votes	% of votes cast
For	134,182,731	95.71%
Against	6,009,646	4.29%
Total votes cast (for and against excluding withheld votes)	140,192,377	100%
Votes withheld ¹	3,927,751	2.73%
Total votes cast (including withheld votes)	144,120,128	100%

Notes:

1. A vote withheld is not a vote in law and is not counted in the calculation of the proportion of votes cast "for" and "against" a resolution.

Approval of the directors' remuneration report

The directors' remuneration report was approved by the Board on 23 January 2014.

Signed on behalf of the Board

Ian Much

Chairman of the Remuneration Committee

A person in military gear is sitting on the ground in a forest, operating a laptop. The background is a dense forest with large trees and fallen leaves on the ground. The overall tone is blue and grey.

MARKET LEADING TECHNOLOGIES

CASE STUDY

RESOLVE

RESOLVE is a state-of-the-art field proven electronic surveillance and attack system. It is designed for the interception, geolocation, exploitation and denial of tactical communications in the HF to UHF frequency bands, including "modern waveforms". The underlying technology has been developed at Chemring Technology Solutions over many years, building on world class expertise in RF and signal processing techniques.

A single RESOLVE system can be used in isolation to provide both full spectrum surveillance and direction finding (DF) capabilities, and when networked with

other RESOLVE systems it is then possible to position fix targets using angle of arrival techniques.

A version of the equipment first came into service with the UK Ministry of Defence under urgent operational requirement (UOR) in 2011, requiring the eventual delivery of over seventy systems. Development of the underlying technology has continued and more than 100 RESOLVE systems are now in-service or on order with numerous customers in Europe, Australia and the Middle East with strong interest from South, Central and Northern America, the Far East, and Eastern Europe.



Financial statements

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Pictured left:
RESOLVE integrated tactical electronic warfare system in semi-static configuration.

Independent auditor's report to the members of Chemring Group PLC

Opinion on financial statements of Chemring Group PLC	<p>In our opinion:</p> <ul style="list-style-type: none"> • the financial statements give a true and fair view of the state of the Group's and the parent company's affairs as at 31 October 2013 and the Group's loss for the year then ended; • the group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; • the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and • the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation. <p>The financial statements comprise the consolidated income statement, the consolidated statement of comprehensive income, the consolidated and parent company balance sheets, the consolidated cash flow statement, the group statement of changes in equity, the parent company reconciliation of movements in shareholders' funds and the related notes 1 to 41. The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).</p>
Going concern	<p>As required by the Listing Rules we have reviewed the directors' statement contained within the directors' report on page 32 that the Group is a going concern. We confirm that:</p> <ul style="list-style-type: none"> • we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate; and • we have not identified any material uncertainties that may cast significant doubt on the Group's ability to continue as a going concern. <p>However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's ability to continue as a going concern.</p>

Our assessment of risks of material misstatement

The assessed risks of material misstatement described below are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team:

RISK	HOW THE SCOPE OF OUR AUDIT RESPONDED TO THE RISK
<p>Revenue recognition on:</p> <ul style="list-style-type: none"> significant long-term contracts, due to the financial effects of judgments, including future milestone success, associated with determining the percentage of contract completion at the balance sheet date and risks associated with completing the contract; and delivery of goods, due to the complex contractual terms with regards to the transfer of risk and reward and therefore the appropriate point at which revenue should be recognised. 	<p>Our audit work assessed the adequacy of the design and implementation of controls over long-term contract accounting. We reviewed the contract risk registers and evidence for the progress made against the contract to confirm that revenue and profit recognised to date are based on management's current best estimate of the degree of contract completion. We understood and challenged management's assumptions by referring to evidence including signed contract terms and latest project status reports, and discussing contract progress and future risks with contract engineers. We also assessed the reliability of management estimates through consideration of the historical accuracy of prior period management estimates.</p> <p>In response to the risk of inappropriate revenue cut-off arising from complex contractual terms, we reviewed contractual evidence to understand how the specific terms were captured and the appropriate revenue recognition policies applied. We then performed a sample test of sales recognised either side of the year end to substantiate that the appropriate terms of the relevant contracts had been satisfied and that the risks and rewards associated with the contract had passed to the customer. We used external evidence such as shipping documentation or client acceptance where available, to confirm that revenue had been recognised in the appropriate period.</p>
<p>Valuation of goodwill and intangible assets arising on historical acquisitions, due to management's assertions regarding their recoverable amount. There are a number of key judgments in determining the recoverable amount, including growth rates in future cash flow forecasts and discount rates applied to these forecasts.</p>	<p>We challenged the assumptions used by management within their annual impairment assessment through benchmarking to independently available data, peer group analysis, and our understanding of the secured orders underpinning the Group's cash flow forecasts. In addition, valuation specialists within the audit team provided additional challenge over the discount rate applied to these cash flows through the use of external confirmation and benchmarking. Having audited the assumptions within management's annual impairment assessment, we checked the arithmetical accuracy of the impairment model using these assumptions to corroborate their conclusions with respect to the recoverability of the carrying value of goodwill and other intangibles.</p>
<p>Taxation, specifically where provisions are made in respect of judgments taken in the various tax jurisdictions in which the Group operates. These provisions are judgmental as a result of their nature and technical complexity.</p>	<p>We evaluated the appropriateness of management's assumptions and estimates in their assessment and valuation of the tax risks within the Group, including corroboration with correspondence on the status of tax compliance and tax audits in the various jurisdictions in which the Group operates, benchmarking against our assessment of the range of potential outcomes in respect of the uncertain tax treatments adopted, involving tax specialists within the audit team to provide detailed knowledge and expertise in assessing tax treatments in certain jurisdictions.</p>

Independent auditor's report to the members of Chemring Group PLC

RISK	HOW THE SCOPE OF OUR AUDIT RESPONDED TO THE RISK
<p>Appropriateness and completeness of judgmental provisions made by management in respect of obsolete inventory, product failures, and legal claims in respect of the outcome of these issues.</p>	<p>We recalculated and challenged management's estimates for the provisions in conjunction with our understanding of the potential liability as set out in contract terms.</p> <p>In respect of provisions held for obsolete inventory, we attended stockcounts and analysed the nature, ageing and turnover of inventory in order to identify potentially obsolete goods. We also considered the movement of inventory at risk by reference to post year-end usage or secured orders. We also challenged the quantum of management's provision using these findings.</p> <p>For product failures, we challenged the level of provisioning by verifying the actual failure costs incurred to date and the products in circulation subject to customer dispute using external evidence, such as correspondence with third parties.</p> <p>In response to legal risks, we circularised the Group's external legal advisers and reviewed legal costs incurred in the year to confirm the completeness of legal cases to which the Group is party. Through external evidence including submitted legal advice and discussion with management, we sought to corroborate the basis for management's expectations over likely outcomes and their subsequent quantification of the related provisions.</p>
<p>Appropriateness of the going concern principle.</p>	<p>We reviewed management's consideration of the adoption of the going concern principle with particular focus on the impact of the changes to the Group's strategy. Our work included challenging management's forecasts, which are also used to support their impairment review, by assessing the accuracy of previous forecasts, and comparing the short-term forecasts against trading since the balance sheet date. In light of this we considered the extent of working capital headroom, covenant compliance and the availability and quantum of mitigating actions to address potential sensitivity scenarios for a period of twelve months from the signing of the financial statements.</p> <p>The Audit Committee's consideration of these risks is set out on page 62.</p> <p>Our audit procedures relating to these matters were designed in the context of our audit of the financial statements as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the financial statements is not modified with respect to any of the risks described above, and we do not express an opinion on these individual matters.</p>

Our application of materiality	<p>We determined materiality for the Group to be £5 million, which is below 10% of underlying pre-tax profit, and below 2% of equity. Pre-tax profit has been normalised to align our materiality to the reported results that are of interest to the users of the financial statements. This has been achieved by removing amortisation of intangible assets and other volatile non-underlying items, namely: acquisition and disposal related costs and business restructuring and incident costs, impairment of goodwill and intangible assets, impairment of assets held for sale and gains on fair value movements on derivative financial instruments.</p> <p>We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £100,000, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identify when assessing the overall presentation of the financial statements.</p>
An overview of the scope of our audit	<p>Our Group audit was scoped by obtaining an understanding of the Group and its environment, including Group-wide controls, and assessing the risks of material misstatement at the Group level. Based on that assessment, we focused our Group audit scope primarily on the audit work at eleven of the Group's seventeen principal business units which were subject to a full audit. In addition, the remaining six business units were subject to an audit of specific account transactions and account balances, where the extent of our testing was focused on our Group audit risks and our assessment of the risk of material misstatement.</p> <p>The seventeen locations represent the principal business units within the Group's reportable segments and account for 94% of the Group's net assets, 96% of the Group's revenue and 98% of the Group's profit before tax. They also provided an appropriate basis for undertaking audit work to address the risks of material misstatement identified above. Our audit work at the seventeen units was executed at levels of materiality applicable to each individual entity, which were lower than Group materiality.</p> <p>At the parent entity level we also tested the consolidation process and carried out analytical procedures to confirm that there were no significant risks of material misstatement of the aggregated financial information of the remaining components not subject to audit or audit of specified account balances.</p> <p>The Group audit team follows a programme of planned visits that has been designed so that the Senior Statutory Auditor or another senior member of the Group audit team visits each of the significant overseas components locations at least once every three years. Every year, regardless of whether we have visited or not, we include the component audit partner and other senior members of the component audit team in our team briefing, direct the scope of their work for the purposes of our Group audit, discuss their risk assessment and review documentation of the findings from their work.</p>

Independent auditor's report to the members of Chemring Group PLC

Opinion on other matters prescribed by the Companies Act 2006	<p>In our opinion:</p> <ul style="list-style-type: none"> the part of the directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006; and the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.
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MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION	
Adequacy of explanations received and accounting records	<p>Under the Companies Act 2006 we are required to report to you if, in our opinion:</p> <ul style="list-style-type: none"> we have not received all the information and explanations we require for our audit; or adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or the parent company financial statements are not in agreement with the accounting records and returns. <p>We have nothing to report in respect of these matters.</p>
Directors' remuneration	<p>Under the Companies Act 2006 we are also required to report if, in our opinion, certain disclosures of directors' remuneration have not been made or the part of the directors' remuneration report to be audited is not in agreement with the accounting records and returns. We have nothing to report arising from these matters.</p>
Corporate governance report	<p>Under the Listing Rules we are also required to review the part of the corporate governance report relating to the Company's compliance with nine provisions of the UK Corporate Governance Code. We have nothing to report arising from our review.</p>
Our duty to read other information in the annual report	<p>Under International Standards on Auditing (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is:</p> <ul style="list-style-type: none"> materially inconsistent with the information in the audited financial statements; or apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or otherwise misleading. <p>In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the annual report is fair, balanced and understandable, and whether the annual report appropriately discloses those matters that we communicated to the Audit Committee which we consider should have been disclosed. We confirm that we have not identified any such inconsistencies or misleading statements.</p>

Respective responsibilities of directors and auditor	<p>As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.</p> <p>This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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 auditor's 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.</p>
Scope of the audit of the financial statements	<p>An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.</p>

Anna Marks (Senior statutory auditor)

for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Reading, UK
23 January 2014

Consolidated income statement

for the year ended 31 October 2013

		2013			2012		
	Note	Underlying performance* £m	Non-underlying items* £m	Total £m	Underlying performance* £m	Non-underlying items* £m	Total £m
Continuing operations							
Revenue	4,5	624.9	–	624.9	740.3	–	740.3
Operating profit/(loss)	5,6	72.1	(109.0)	(36.9)	88.3	(51.3)	37.0
Share of profit after tax of associate	17	–	–	–	0.1	–	0.1
Finance income	8	0.2	–	0.2	0.1	–	0.1
Finance expense	9	(19.9)	–	(19.9)	(18.4)	–	(18.4)
Profit/(loss) before tax	5	52.4	(109.0)	(56.6)	70.1	(51.3)	18.8
Tax	10	(10.6)	19.7	9.1	(15.1)	9.5	(5.6)
Profit/(loss) after tax		41.8	(89.3)	(47.5)	55.0	(41.8)	13.2
Discontinued operations							
Profit after tax from discontinued operations	33	–	–	–	2.1	–	2.1
Profit/(loss) after tax		41.8	(89.3)	(47.5)	57.1	(41.8)	15.3

		2013			2012		
	Note	Underlying performance* £m	Non-underlying items* £m	Total £m	Underlying performance* £m	Non-underlying items* £m	Total £m
Earnings/(loss) per ordinary share							
Continuing operations							
Basic	12	21.6p	(46.2)p	(24.6)p	28.5p	(21.7)p	6.8p
Diluted	12	21.2p	(45.8)p	(24.6)p	28.1p	(21.4)p	6.7p
Continuing operations and discontinued operations							
Basic	12	21.6p	(46.2)p	(24.6)p	29.6p	(21.7)p	7.9p
Diluted	12	21.2p	(45.8)p	(24.6)p	29.2p	(21.4)p	7.8p

* Further information about non-underlying items can be found in notes 5 and 6. For 2012, the non-underlying items charge of £51.3 million is shown net of £10.3 million profit on disposal arising from the sale of the marine business, as shown in note 33.

Consolidated statement of comprehensive income

for the year ended 31 October 2013

	Note	2013 £m	2012 £m
(Loss)/profit after tax attributable to equity holders of the parent		(47.5)	15.3
Items that will not be reclassified subsequently to profit or loss			
Actuarial gains/(losses) on defined benefit pension schemes	35	0.7	(2.7)
Movement on deferred tax relating to pension schemes	26	(0.9)	0.7
		(0.2)	(2.0)
Items that may be reclassified subsequently to profit or loss			
Exchange differences on translation of foreign operations		13.6	(20.1)
Deferred tax on exchange differences on translation of foreign operations		(1.8)	0.7
		11.8	(19.4)
Total comprehensive expense attributable to equity holders of the parent		(35.9)	(6.1)

Consolidated statement of changes in equity

for the year ended 31 October 2013

	Share capital £m	Share premium account £m	Special capital reserve £m	Revaluation reserve £m	Translation reserve £m	Retained earnings £m	Own shares £m	Total £m
At 1 November 2012	2.0	230.7	12.9	1.3	(39.6)	235.8	(9.6)	433.5
Loss after tax	–	–	–	–	–	(47.5)	–	(47.5)
Other comprehensive income/(expense)	–	–	–	–	13.6	(2.0)	–	11.6
Total comprehensive income/(expense)	–	–	–	–	13.6	(49.5)	–	(35.9)
Ordinary shares issued	–	–	–	–	–	–	–	–
Dividends paid	–	–	–	–	–	(14.7)	–	(14.7)
Share-based payments (net of settlement)	–	–	–	–	–	0.9	–	0.9
At 31 October 2013	2.0	230.7	12.9	1.3	(26.0)	172.5	(9.6)	383.8

	Share capital £m	Share premium account £m	Special capital reserve £m	Revaluation reserve £m	Translation reserve £m	Retained earnings £m	Own shares £m	Total £m
At 1 November 2011	2.0	230.6	12.9	1.4	(19.5)	254.6	(6.6)	475.4
Profit after tax	–	–	–	–	–	15.3	–	15.3
Other comprehensive expense	–	–	–	–	(20.1)	(1.3)	–	(21.4)
Total comprehensive (expense)/income	–	–	–	–	(20.1)	14.0	–	(6.1)
Ordinary shares issued	–	0.1	–	–	–	–	–	0.1
Dividends paid	–	–	–	–	–	(31.1)	–	(31.1)
Share-based payments (net of settlement)	–	–	–	–	–	(1.8)	–	(1.8)
Transactions in own shares	–	–	–	–	–	–	(3.0)	(3.0)
Transfers between reserves	–	–	–	(0.1)	–	0.1	–	–
At 31 October 2012	2.0	230.7	12.9	1.3	(39.6)	235.8	(9.6)	433.5

Consolidated balance sheet

as at 31 October 2013

	Note	£m	2013 £m	£m	2012 £m
Non-current assets					
Goodwill	13	168.3		214.8	
Development costs	14	32.7		31.0	
Other intangible assets	14	135.5		167.4	
Property, plant and equipment	15	222.3		240.0	
Interest in associate	17	1.5		1.4	
Deferred tax	26	21.7		16.9	
			582.0		671.5
Current assets					
Inventories	18	113.7		113.8	
Trade and other receivables	19	203.9		193.0	
Cash and cash equivalents	20,38	14.2		96.0	
Derivative financial instruments	24	1.5		1.0	
Assets held for sale	34	6.7		–	
			340.0		403.8
Total assets			922.0		1,075.3
Current liabilities					
Borrowings	21,38	(0.4)		(74.0)	
Obligations under finance leases	22	(1.6)		(1.7)	
Trade and other payables	23	(176.7)		(201.5)	
Provisions	25	(2.7)		(2.8)	
Current tax		(15.4)		(5.2)	
Derivative financial instruments	24	(0.4)		(0.1)	
Liabilities held for sale	34	(1.1)		–	
			(198.3)		(285.3)
Non-current liabilities					
Borrowings	21,38	(259.4)		(262.1)	
Obligations under finance leases	22	(1.4)		(2.9)	
Trade and other payables	23	(2.3)		(4.3)	
Provisions	25	(10.3)		(4.9)	
Deferred tax	26	(38.8)		(52.7)	
Preference shares	27	(0.1)		(0.1)	
Retirement benefit obligations	35	(25.1)		(27.0)	
Derivative financial instruments	24	(2.5)		(2.5)	
			(339.9)		(356.5)
Total liabilities			(538.2)		(641.8)
Net assets			383.8		433.5
Equity					
Share capital	27		2.0		2.0
Share premium account			230.7		230.7
Special capital reserve			12.9		12.9
Revaluation reserve			1.3		1.3
Translation reserve			(26.0)		(39.6)
Retained earnings			172.5		235.8
			393.4		443.1
Own shares	29		(9.6)		(9.6)
Equity attributable to equity holders of the parent			383.8		433.5
Total equity			383.8		433.5

These financial statements of Chemring Group PLC (registered number 86662) were approved and authorised for issue by the Board of directors on 23 January 2014.

Signed on behalf of the Board

Mark Papworth
Director

Steve Bowers
Director

Consolidated cash flow statement

for the year ended 31 October 2013

	Note	2013 £m	2012 £m
Cash flows from operating activities			
Cash generated from continuing underlying operations	36	68.6	114.9
Cash generated from discontinued underlying operations	33	–	3.3
Cash generated from underlying operations	36	68.6	118.2
Acquisition and disposal related costs	32	(3.8)	(5.5)
Business restructuring and incident costs	5	(8.9)	(10.1)
		55.9	102.6
Tax paid		(0.5)	(6.1)
Net cash inflow from operating activities		55.4	96.5
Cash flows from investing activities			
Dividends received from associate		–	0.1
Purchases of intangible assets		(7.4)	(11.0)
Purchases of property, plant and equipment		(12.3)	(30.1)
Receipt of finance income		0.2	–
Receipts from sales of businesses (net of cash transferred)	33	–	21.8
Net cash outflow from investing activities		(19.5)	(19.2)
Cash flows from financing activities			
Dividends paid	11	(14.7)	(31.1)
Finance expense paid		(20.6)	(23.8)
New borrowings		–	12.5
Capitalised facility fees paid		(1.7)	–
Repayments of borrowings		(79.1)	(23.0)
Repayments of finance leases		(1.7)	(1.8)
Purchase of own shares	29	–	(4.8)
Net cash outflow from financing activities		(117.8)	(72.0)
(Decrease)/increase in cash and cash equivalents		(81.9)	5.3
Cash and cash equivalents at beginning of the year		96.0	91.9
Effect of foreign exchange rate changes		0.1	(1.2)
Cash and cash equivalents at end of the year	20,38	14.2	96.0

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 50 to 53. These financial statements are the consolidated financial statements of Chemring Group PLC and its subsidiaries ("the Group").

The financial statements are presented in pounds sterling and rounded to the nearest £0.1 million. Foreign operations are included in accordance with the policy set out in note 3.

Going concern

The directors have, at the time of approving the financial statements, a reasonable expectation that the Group and the Company have adequate resources to continue to adopt the going concern basis of accounting in preparing these financial statements. Further detail is contained in the statement on going concern on page 32.

2. Adoption of new and revised standards

In the year ended 31 October 2013, the following revised standard was adopted and has affected the amounts reported in these financial statements:

- Amendments to IAS 1 *Presentation of Financial Statements (amended June 2011)*.

The Group has applied the amendments titled *Presentation of Items of Other Comprehensive Income* to IAS 1 in advance of the effective date (annual periods beginning on or after 1 July 2012). The amendment increases the required level of disclosure within the statement of comprehensive income.

The impact of this amendment has been to analyse items within the statement of comprehensive income between items that will not be reclassified subsequently to the income statement and items that will be reclassified subsequently to the income statement in accordance with the respective IFRS to which the item relates. The amendments have been applied retrospectively, and hence the presentation of items in the consolidated statement of comprehensive income has been restated to reflect the change. Other than the above mentioned presentation changes, the application of IAS 1 does not result in any impact on profit or loss, comprehensive income and total comprehensive income.

The following IFRIC interpretations, amendments to existing standards and new standards were adopted in the year ended 31 October 2013 but have not impacted the reported results or the financial position:

- Amendments to IFRS 7 *Financial Instruments: Disclosures*; and
- Amendments to IAS 12 *Income Taxes*.

Changes in accounting policies

At the date of authorisation of these financial statements, the following standards and interpretations that are potentially relevant to the Group and which have not been applied in these financial statements were in issue but not yet effective (and in some cases had not yet been adopted by the European Union):

- IFRS 13 *Fair Value Measurement*;
- IAS 19 (Revised) *Employee Benefits*;
- Annual Improvements to IFRSs (2009 – 2011) Cycle;
- IFRS 7 (amended) *Disclosures – Offsetting Financial Assets and Liabilities*;
- IFRS 9 *Financial Instruments*;
- IFRS 10 *Consolidated Financial Statements*, IFRS 12 *Investment Entities*, IAS 27 (Revised) *Separate Financial Instruments*;
- IAS 36 (amended) *Recoverable Amount Disclosures for Non-Financial Assets*;
- IAS 39 (amended) *Novation of Derivatives and Continuation of Hedge Accounting*; and
- IFRIC Interpretation 21 *Levies*.

The directors do not expect that the adoption of these standards and interpretations will have a material impact on the financial statements of the Group in future periods, except as follows:

- IFRS 9 *Financial Instruments* will impact both the measurement and disclosures of financial instruments;
- IFRS 7 (amended) *Disclosures – Offsetting Financial Assets and Liabilities* will increase the disclosure requirements where netting-off procedures are in place for financial assets and financial liabilities;
- IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, IFRS 12 *Investment Entities*, IAS 27 (Revised) *Separate Financial Instruments* and IAS 28 (Revised) *Investment in Associates and Joint Ventures* – these will restrict the presentation options of the results of joint ventures, which the Group expects to enter into, in the financial statements; and
- IAS 19 (Revised) *Employee Benefits* – this will impact the measurement of the various components representing movements in the defined benefit pensions obligations and associated disclosures, but not for the Group's total obligation.

Beyond this information, it is not practicable to provide a reasonable estimate of the effect of these standards until a detailed review has been completed.

Notes to the group financial statements

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 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 years 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 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.

The Company and all of its subsidiaries make up their financial statements to the same date. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Operating profit

Operating profit is stated before the share of results of associates and before finance income and expense.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts, VAT and other revenue related taxes.

Sale of goods

Revenue from the sale of goods is recognised when all of the following conditions are satisfied:

- the Group has transferred to the buyer the significant risks and rewards of ownership, typically on formal acceptance;
- the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the Group; and
- the costs incurred or to be incurred in respect of the transaction can be measured reliably.

Rendering of services

Revenue from a contract to provide services is recognised by reference to the stage of completion of the contract.

Contract accounting

For appropriate contracts, when the outcome can be estimated reliably, revenue and costs are recognised by reference to the stage of completion at the balance sheet date. This is normally measured by the proportion of contract costs incurred for work performed to date against the estimated total contract costs, except where this would not be representative of the actual stage of completion. Variations in contract work, claims and incentive payments are included to the extent that the amounts can be measured reliably and their receipt is considered probable.

When the outcome of such contracts cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred where it is probable they will be recoverable. Contract costs are recognised as expenses in the period in which they are incurred. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Investment income

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established (provided that the economic benefits will flow to the Group and the amount of income can be measured reliably).

Interest income is recognised when it is probable that the economic benefits will flow to the Group and the amount of revenue can be measured reliably. 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 that asset's net carrying amount on initial recognition.

Acquisitions and disposals

On acquisition of a subsidiary, associate or jointly controlled entity, the cost is measured as the fair value of the consideration. The assets, liabilities and contingent liabilities of subsidiary undertakings that meet the IFRS 3 (revised 2008) *Business Combinations* recognition criteria are measured at the fair value at the date of acquisition, except that:

- deferred tax assets or liabilities and liabilities or assets relating to employee benefit arrangements are recognised and measured in accordance with IAS 12 *Income Taxes* and IAS 19 *Employee Benefits* respectively;
- liabilities or equity instruments related to the replacement by the Group of an acquiree's share-based payment awards are measured in accordance with IFRS 2 *Share-based Payments*; and
- assets (or disposal groups) that are classified as held for sale, in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* are measured in accordance with that standard.

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 subsidiary undertakings are changed where necessary to be consistent with those of the Group.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period (see below), or additional assets or liabilities recognised, to reflect new information obtained about facts and circumstances that existed as at the acquisition date that, if known, would have affected the amounts recognised as at that date.

The measurement period is from the date of acquisition to the date the Group obtains complete information about facts and circumstances that existed as at the acquisition date, subject to a maximum period of one year.

In accordance with IFRS 3 (Revised) *Business Combinations*, acquisition costs are expensed through the income statement. Acquisition and disposal related costs refer to external costs incurred in acquiring and disposing of companies, together with the costs of aborted bids and the establishment of joint ventures.

Non-current assets held for sale

Non-current assets and disposal groups classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset or disposal group is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Intangible assets

Goodwill

The purchased goodwill of the Group is regarded as having an indefinite useful economic life and, in accordance with IAS 36 *Impairment of Assets*, is not amortised but is subject to annual tests for impairment. On disposal of a subsidiary, associate or jointly controlled entity, the amount attributable to goodwill is included in the determination of the profit or loss on disposal.

Acquired intangibles

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 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:

Technology	– average of ten years
Customer relationships	– average of ten years
Order books	– average of two years

Development costs

Development costs that qualify as intangible assets are capitalised as incurred and, once the relevant intangible asset is ready for use, are amortised on a straight-line basis over their estimated useful lives, averaging three years (2012: three years).

Patents and licences

Patents and licences are measured initially at purchase cost and are amortised on a straight-line basis over their estimated useful lives, averaging seven years (2012: ten years).

Property, plant and equipment

Other than historically revalued land and buildings, property, plant and equipment is held at cost less accumulated depreciation and any recognised impairment loss. Borrowing costs on significant capital expenditure projects are capitalised and allocated to the cost of the project. No

Notes to the group financial statements

3. Accounting policies (continued)

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:

Freehold buildings	– up to fifty years
Leasehold buildings	– the period of the lease
Plant and equipment	– up to ten years

Investments in associates

The results and the assets and liabilities of associates are accounted for using the equity method of accounting. Any excess of the cost of investment over the Group's share of the fair value of identifiable assets and liabilities within the associate at the date of acquisition is accounted for as goodwill that is included in the carrying value of the investment and is assessed for impairment as part of that investment.

Impairment of non-current assets

Assets that have indefinite lives are allocated to the Group's cash-generating units and tested for impairment at least 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 the asset's 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.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to prepare for their intended use or sale, are added to the cost of those assets, until such time as the assets are subsequently ready for their intended use or sale. Once the assets are ready for their intended use, these capitalised borrowing costs are depreciated in line with the underlying asset.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in the income statement in the period in which they are incurred.

Government grants

Government grants are not recognised until there is reasonable assurance that the Group will comply with the conditions attaching to them and that the grants will be received.

The benefit of a government loan at a below-market rate of interest is treated as a government grant, measured as the difference between proceeds received and the fair value of the loan based on prevailing market interest rates.

Government grants towards staff retraining costs are recognised as income over the periods necessary to match them with the related costs and are deducted in reporting the related expense.

Government grants relating to property, plant and equipment are treated as deferred income and released to the income statement over the expected useful lives of the assets concerned.

Tax

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

Current tax payable is based on taxable profit for the year. Taxable profit differs from 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 excludes items of income or expense 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 represents amounts 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 taxable 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.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities, when they relate to income taxed by the same tax authority, and the Group intends to settle its current tax assets and liabilities on a net basis.

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, in accordance with the requirements of the Companies Act 1985.

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 these 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 these financial statements.

In preparing the financial statements of each Group company, 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 retranslated 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 retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in the income statement for the period.

In order to hedge its exposure to certain foreign exchange risks, the Group enters into forward foreign exchange

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 these 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.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

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 change in value.

Financial liabilities and derivative financial 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 and hedge accounting

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, forward foreign exchange 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 forward foreign exchange contracts and interest rate swaps where appropriate, with movements in fair value taken to equity for cash flow hedges and the income statement for fair value hedges, 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 third party valuers.

Where derivative financial instruments do not meet the criteria for hedge accounting, the changes in fair value are immediately recognised in the income statement.

Hedges of net investments in foreign operations

Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in the statement of comprehensive income and accumulated in the translation reserve. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Embedded derivative financial instruments

Embedded derivative financial instruments that are not closely related to the host contract are treated as separate derivative financial instruments, 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 income statement and are presented in the statement of comprehensive income.

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 of the asset 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 interest on the remaining balance of the obligation.

All other leases are operating leases, for which 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 of an award is measured at the date of grant and reflects any market-based vesting conditions. Non-market based vesting conditions are excluded from the fair value of the award. At the date of grant, the Company estimates the number of awards expected to vest as a result of non-market based vesting conditions, and the fair value of this estimated number of awards is recognised as an expense in the profit and loss account on a straight-line basis over the vesting period. 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.

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 remeasured at each balance sheet date, with changes in the fair value recognised in the income statement for the period.

Post balance sheet events

In accordance with IAS 10 *Events after the Balance Sheet Date*, the Group continues to disclose events that it considers material, 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 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:

Assessment of contract accounting

The Group has contracts that fall into different accounting periods. In assessing the allocation of revenues and costs to individual accounting periods, and the consequential assets and liabilities, the Group estimates the total revenues and costs forecast to arise in respect of the contract and the stage of completion based on an appropriate measure of performance as described under the revenue recognition policy on page 100. The Group utilises assumptions and projections, principally relating to future material, labour and overhead costs. As a consequence, there is a risk that total contract costs will exceed those originally estimated and the margin will decrease. Changes to initial assumptions, which are reviewed on a regular basis, may result in revisions to estimated costs and anticipated margins. These are recognised in the period in which the estimated costs are determined. The determination of appropriate accounting policies for recognising revenue and costs in respect of these contracts requires judgment, in particular (i) whether contract accounting is the most appropriate method of recognising revenue on these contracts; and (ii) the appropriate measure of stage of completion of the contract.

Goodwill impairment

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 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 (see note 13). In reviewing the carrying value of goodwill of the Group's various businesses, the Board has considered the separate plans and cash flows of these businesses consistent with the requirements of IAS 36 *Impairment of Assets*. The plans and cash flows of these businesses have factored in the possible impacts of sequestration and continuing resolution in the US and the difficult economic conditions for the defence industry in general.

Tax

The largest category of deferred tax asset which contains significant estimation uncertainty and which requires management judgment in assessing its recoverability relates to tax losses carried forward (see note 26).

Applicable accounting standards permit the recognition of deferred tax assets only to the extent that it is probable that future taxable profits will be available to utilise the tax losses carried forward. The assessment of future taxable profits involves significant estimation uncertainty, principally relating to an assessment of management's projections of future taxable income based on business plans and ongoing tax planning strategies. These projections include assumptions about the future strategy of the Group, the economic and regulatory environment in which the Group operates, future tax legislation, and customer behaviour, amongst other variables (see note 26 for details of tax losses on which deferred tax assets have not been recognised).

Assets and liabilities acquired under business combinations

Under IFRS 3 (Revised) *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 assets and estimate their useful economic lives (see note 14). Assets and liabilities are recognised on acquisition when relevant, which include deferred tax assets on losses (see note 26).

Notes to the group financial statements

3. Accounting policies (continued)

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).

Legal

The Group is subject to legal proceedings and other claims arising in the ordinary course of business. The Group is required to assess the likelihood of any adverse judgments or outcomes, as well as potential ranges of probable losses. A determination of the amount of reserves required for these matters is based on a careful analysis of each individual issue with the assistance of outside legal counsel. However, actual claims incurred could differ from the original estimates.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle that obligation, and a reliable estimate can be made of the amount of the obligation. The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Environmental provisions

Where the Group is liable for decontamination work or the restoration of sites to their original condition, an estimate is made of the costs needed to complete these works, discounted back to present values where appropriate, relying upon independent expert third party valuers where appropriate.

Restructuring provisions

A restructuring provision is recognised when the Group has developed a detailed formal plan for the restructuring, and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement the plan or announcing its main features to those affected by it. The measurement of a restructuring provision includes only the direct expenditures arising from the restructuring and not those associated with the ongoing activities of the entity.

Warranties

Provisions for the expected cost of warranty obligations under local sale of goods legislation are recognised at the date of sale of the relevant products, based upon the best estimate of the expenditure required to settle the Group's obligation.

Non-GAAP information

In the analysis of the Group's financial performance and position, operating results and cash flows, information is presented to provide readers with additional information that is prepared on a non-GAAP basis and which is regularly reviewed by management. However, this additional information is not uniformly defined by all companies and so may not be comparable with similarly titled measures and disclosures by other companies. Additionally, certain information presented is derived from amounts calculated in accordance with IFRS but is not itself an expressly permitted GAAP measure. Such non-GAAP measures should not be viewed in isolation or as an alternative to the equivalent GAAP measure.

Contingent liabilities

The Group exercises judgment in recognising exposures to contingent liabilities related to pending litigation or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation, as well as other contingent liabilities. Judgment may be necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and/or to quantify the possible range of the financial settlement.

4. Revenue

All of the Group's revenue is derived from the sale of goods, including revenue recognised in respect of contract-accounted arrangements, and provision of services. The following table provides an analysis of the Group's revenue by destination:

Revenue by destination	2013 £m	2012 £m
Continuing operations		
UK	109.9	112.0
USA	280.7	348.5
Europe	60.5	84.8
Australia and Far East	44.6	60.4
Middle East	123.8	120.5
Rest of the world	5.4	14.1
	624.9	740.3
Discontinued operations		
UK	–	1.0
USA	–	2.5
Europe	–	6.7
Australia and Far East	–	3.4
Rest of the world	–	1.5
	–	15.1
	624.9	755.4

Revenue from contract accounting in the above figures amounted to £240.5 million (2012: £275.8 million). The decrease since 2012 reflects the decline in revenue compared to the prior year.

In addition to the revenues shown above, finance income of £0.2 million (2012: £0.1 million) has been recognised.

The directors consider the only countries that are significant in accordance with IFRS 8 *Operating Segments* are the USA and the UK, as disclosed above, and the Kingdom of Saudi Arabia, which is included within the Middle East category. Sales to the Kingdom of Saudi Arabia generated revenue of £97.6 million (2012: £92.8 million).

5. Business segments

IFRS 8 *Operating Segments* requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the Chief Executive and the Board of directors to allocate resources to the segments and to assess their performance. For management purposes, the Group's operating and reporting structure has been revised during the year to better cluster similar businesses together within the following four operating segments – Countermeasures, Sensors & Electronics, Pyrotechnics & Munitions, and Energetic Sub-Systems. These segments are the basis on which the Group reports its segmental information. The principal activities of each segment are as follows:

Countermeasures	Expendable active and passive countermeasures for naval and air platforms and land-based electronic warfare equipment.
Sensors & Electronics	IED detection equipment, chemical and biological threat detection equipment, IED electronic countermeasures, explosive ordnance disposal equipment and demilitarisation services.
Pyrotechnics & Munitions	Signals and illumination devices and payloads, cartridge/propellant actuated devices, pyrotechnic devices for satellite launch and deployment, missile and ammunition components, propellants, warheads, fuzes, medium and large-calibre ammunition.
Energetic Sub-Systems	Separation sub-systems, actuators and energetic materials.

Notes to the group financial statements

5. Business segments (continued)

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

Revenue	2013 £m	2012 £m
Continuing operations		
Countermeasures	125.0	163.2
Sensors & Electronics	211.3	228.9
Pyrotechnics & Munitions	200.6	249.5
Energetic Sub-Systems	88.0	98.7
	624.9	740.3
Discontinued operations		
Pyrotechnics & Munitions	–	15.1
	624.9	755.4
Underlying operating profit		
Continuing operations		
Countermeasures	13.2	20.4
Sensors & Electronics	44.7	44.9
Pyrotechnics & Munitions	13.0	21.2
Energetic Sub-Systems	11.3	12.3
	82.2	98.8
Unallocated corporate costs	(10.1)	(10.5)
	72.1	88.3
Discontinued operations		
Pyrotechnics & Munitions	–	3.1
Underlying operating profit including discontinued operations	72.1	91.4
Acquisition and disposal related costs (see note 32)	(3.2)	(8.2)
Business restructuring and incident costs (see note 5)	(11.7)	(11.9)
Profit on disposal of business (see note 33)	–	10.3
Impairment of goodwill (see note 13)	(50.9)	(22.5)
Impairment of acquired intangibles (see notes 13 and 14)	(15.7)	–
Impairment of assets held for sale (see note 34)	(8.8)	–
Intangible amortisation arising from business combinations (see note 14)	(18.8)	(20.9)
Gain on the movement in the fair value of derivative financial instruments (see note 24)	0.1	1.9
Non-underlying items	(109.0)	(51.3)
Operating (loss)/profit from continuing operations	(36.9)	37.0
Share of profit after tax of associate	–	0.1
Finance income	0.2	0.1
Finance expense	(19.9)	(18.4)
(Loss)/profit before tax from continuing operations	(56.6)	18.8
Tax	9.1	(5.6)
(Loss)/profit after tax from continuing operations	(47.5)	13.2
Profit after tax from discontinued operations	–	2.1
(Loss)/profit after tax for the year	(47.5)	15.3

The accounting policies of the reportable segments are the same as the Group's accounting policies described in note 3. Segment profit represents the profit earned by each segment, without allocation of corporate costs including directors' salaries, non-underlying items, the share of profit of associates, finance income and expense, and tax. This is the measure reported to the Group Chief Executive for the purpose of resource allocation and assessment of segment performance.

Unallocated corporate costs

Unallocated corporate costs were £10.1 million (2012: £10.5 million), with the reduction due largely to the saving of costs associated with the Group's former London office which was vacated in late 2012.

Intra-group transactions

There are no material intra-group transactions included within the figures for revenue and profit disclosed in this note.

Business restructuring and incident costs

In 2013, restructuring costs of £11.7 million related to a major simplification of the divisional management structure (£4.4 million), business unit integration and restructuring (£5.5 million), excess property costs (£1.1 million) and incident and other costs (£0.7 million). There is a £2.8 million difference between the expense in the income statement and the amount appearing in the cash flow statement due to the timing of payments and non-cash movements. In 2012, restructuring costs related to the closure of the Group's Marshall, Texas site (£3.3 million), the restructuring of the Group's US countermeasures businesses (£2.5 million), the restructuring of the Group's UK operations (£2.6 million), and an additional £1.5 million relating to several smaller restructuring projects. There were also a number of Board changes during the year, resulting in associated costs of £2.0 million. The balance of the costs related to recruitment, and various other legal and professional fees.

The following table shows an analysis of non-underlying items by segment:

Non-underlying items by segment	2013 £m	2012 £m
Countermeasures	2.6	3.3
Sensors & Electronics	9.7	8.9
Pyrotechnics & Munitions	8.5	8.9
Energetic Sub-Systems	79.9	21.9
Non-segmental	8.3	8.3
	109.0	51.3

Information about major customers

Included in segmental revenues are revenues of £206.7 million (2012: £289.6 million) and £84.1 million (2012: £89.7 million), which arose from sales to the Group's two largest customers respectively. The largest customer had sales reported in all four of the Group's business segments, whilst sales to the second largest customer primarily arose in the Pyrotechnics & Munitions segment. These were the only individual customers where direct sales account for more than 10% of Group revenue for the year.

The Group does not disclose assets or liabilities by segment in the monthly management accounts provided to the Executive Committee or the Board of directors. The *Improvements to IFRSs* amendment document issued in April 2009 only requires to be disclosed that information that is provided to the chief operating decision maker as a key decision making tool. The Group has adopted this amendment in order to clarify that the chief operating decision maker does not use this information as a key decision tool. IFRS 8 *Operating Segments* requires a geographic analysis of non-current assets, and a disclosure of non-current assets by location is therefore shown below:

Non-current assets by location	2013 £m	2012 £m
UK	222.8	219.7
USA	195.8	283.6
Europe	136.8	138.7
Australia and Far East	26.6	29.5
	582.0	671.5

Notes to the group financial statements

6. Operating profit

The following table shows an analysis of operating profit from continuing operations:

	2013 £m	2012 £m
Revenue from continuing operations	624.9	740.3
Cost of sales	(438.1)	(552.5)
Administrative expenses	(114.7)	(99.5)
Acquisition and disposal related costs (see note 32)	(3.2)	(8.2)
Business restructuring and incident costs (see note 5)	(11.7)	(11.9)
Profit on disposal of business (see note 33)	–	10.3
Impairment of goodwill (see note 13)	(50.9)	(22.5)
Impairment of acquired intangibles (see notes 13 and 14)	(15.7)	–
Impairment of assets held for sale (see note 34)	(8.8)	–
Intangible amortisation arising from business combinations (see note 14)	(18.8)	(20.9)
Gain on the movement in the fair value of derivative financial instruments (see note 24)	0.1	1.9
Non-underlying items	(109.0)	(51.3)
Operating (loss)/profit from continuing operations	(36.9)	37.0

Operating profit is stated after charging/(crediting):

		2013 £m	2012 £m
Research and development costs	– customer-funded	27.1	34.4
	– internally-funded	11.5	12.3
Amortisation	– arising from business combinations	18.8	20.9
	– development costs	5.5	4.3
	– patents and licences	0.4	0.3
Depreciation of property, plant and equipment	– owned assets	19.8	15.8
	– leased assets	0.3	0.1
Loss on disposal of non-current assets		2.2	3.4
Operating lease rentals	– plant and machinery	2.5	1.1
	– other	1.0	0.8
Government grants		(0.1)	–
Foreign exchange losses		0.8	4.1
Staff costs (see note 7)		172.6	189.8
Cost of inventories recognised as an expense		266.1	364.8
Acquisition and disposal related costs (see note 32)		3.2	8.2
Business restructuring and incident costs (see note 5)		11.7	11.9
Profit on disposal of business (see note 33)		–	(10.3)
Impairment of goodwill (see note 13)		50.9	22.5
Impairment of acquired intangibles (see notes 13 and 14)		15.7	–
Impairment of assets held for sale (see note 34)		8.8	–
Auditor's remuneration (see opposite)		1.7	1.2

A detailed analysis of the auditor's remuneration on a worldwide basis is provided below:

	2013 £m	2012 £m
Auditor's remuneration		
Fees payable to the Company's auditor and its associates for:		
– the audit of the Company's annual accounts	0.5	0.4
– the audit of the Company's subsidiaries, pursuant to legislation	0.4	0.4
	0.9	0.8
Other services		
Audit-related assurance services	0.1	0.1
Tax services – compliance	0.3	0.1
Tax services – advisory	0.2	0.2
Corporate finance services	0.2	–
	0.8	0.4
	1.7	1.2

Included in the fees for the audit of the Company's annual accounts is £0.2 million (2012: £0.1 million) in respect of the parent company.

A description of the work of the Audit Committee is set out in the corporate governance report on pages 61 and 63, and includes an explanation of how auditor objectivity and independence is safeguarded when non-audit services are provided by the auditor. No services were provided by the auditor pursuant to contingent fee arrangements.

During the year, the Group incurred professional fees with other accountancy firms for the provision of corporate finance services of £nil (2012: £1.0 million).

7. Staff costs

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

	2013 Number	2012 Number
Production	3,057	3,332
Administration, sales and marketing	850	883
	3,907	4,215

At the year end, the number of employees was 3,693 (2012: 4,193).

The costs incurred in respect of these employees (including share-based payments) were:

	2013 £m	2012 £m
Wages and salaries	146.2	160.3
Social security costs	19.9	21.9
Other pension costs	6.5	7.6
	172.6	189.8

There has been a decrease in total wages and salaries since 2012, reflecting the fall in average employee numbers.

Notes to the group financial statements

8. Finance income

	2013 £m	2012 £m
Bank interest	0.2	0.1

9. Finance expense

	2013 £m	2012 £m
Bank overdraft and loan interest	5.1	4.0
Loan notes interest	15.0	15.1
Medium term loan interest	–	1.0
Finance lease interest	0.3	0.3
Amortisation of debt finance costs	2.0	1.6
Unwinding of discount on provisions	–	0.2
Interest cost of retirement benefit obligations (see note 35)	0.5	0.8
Capitalised interest on qualifying assets (see note 15)	(3.0)	(4.6)
	19.9	18.4

Borrowing costs capitalised in the cost of qualifying assets are calculated by applying a rate of 7% (2012: 7%) to expenditure on such assets.

10. Tax

	2013 £m	2012 £m
Current tax charge	(12.3)	(5.7)
Deferred tax credit (see note 26)	21.4	0.1
Current year tax credit/(charge) for continuing operations	9.1	(5.6)

The tax charge relating to discontinued operations amounted to £nil (2012: £0.5 million).

Income tax in the UK is calculated at 23.4% (2012: 24.9%) of the taxable profit for the year. Tax for other jurisdictions is calculated at the rates prevailing in those jurisdictions.

The total tax credit/(charge) from continuing operations can be reconciled to the income statement as follows:

	2013 £m	2012 £m
(Loss)/profit before tax from continuing operations	(56.6)	18.8
Tax at the UK corporation tax rate of 23.4% (2012: 24.9%)	13.2	(4.7)
Expenses not deductible for tax purposes	(9.9)	(2.5)
Changes in tax rates	0.7	2.1
Research and development tax relief	0.5	1.3
Utilisation and recognition of tax losses	1.1	(3.0)
Non-taxable disposal of business	–	5.2
Prior period adjustments	0.4	3.5
Overseas profits taxed at rates different to the UK standard rate	3.1	(7.5)
Total tax credit/(charge) from continuing operations	9.1	(5.6)

In addition to the tax credit/(charge) in the income statement, a tax charge of £2.7 million (2012: £1.4 million credit) has been recognised in equity in the year.

The effective rate of tax on the profit/(loss) before tax of the Group is 16.1% (2012: 28.4%), and the effective rate of tax on the underlying profit before tax of the Group is 20.2% (2012: 21.5%). The decrease in the statutory effective rate is primarily as a result of the tax treatment of exceptional items and goodwill amortisation.

11. Dividends

	2013 £m	2012 £m
Dividends on ordinary shares of 1p each		
Final dividend for the year ended 31 October 2012: 4.2p (2011: 10.8p)	8.1	20.8
Interim dividend for the year ended 31 October 2013: 3.4p (2012: 5.3p)	6.6	10.3
Total dividends	14.7	31.1

The proposed final dividend in respect of the year ended 31 October 2013 of 3.8p per share will, if approved, have a total value of approximately £7.3 million of shareholders' funds. This proposed final 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.

	2013 £m	2012 £m
Dividends declared on ordinary shares of 1p each		
Interim dividend for the year ended 31 October 2013: 3.4p (2012: 5.3p)	6.6	10.3
Final dividend for the year ended 31 October 2013: 3.8p (2012: 4.2p)	7.3	8.1
Total dividends declared	13.9	18.4

12. Earnings per share

Earnings per share are based on the average number of shares in issue, excluding own shares held, of 193,292,820 (2012: 193,309,230) and the loss on continuing ordinary activities after tax of £47.5 million (2012: £13.2 million profit). Diluted earnings per share has been calculated using a diluted average number of shares in issue, excluding own shares held, of 193,292,820 (2012: 195,792,140) and the loss on continuing ordinary activities after tax of £47.5 million (2012: £13.2 million profit). For the year ended 31 October 2013, no dilution has been recognised for the purposes of basic earnings per share due to there being a loss per share. Dilution has however been recognised in the calculation of underlying earnings per share for the year ended 31 October 2013, using a diluted average number of shares in issue, excluding own shares held, of 196,854,505 (2012: 195,792,140).

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

	2013 Ordinary shares Number 000s	2012 Ordinary shares Number 000s
Weighted average number of shares used to calculate basic (loss)/earnings per share	193,293	193,309
Additional shares issuable other than at fair value in respect of options outstanding	–	2,483
Weighted average number of shares used to calculate diluted (loss)/earnings per share	193,293	195,792
Additional shares issuable other than at fair value in respect of options outstanding	3,562	–
Weighted average number of shares used to calculate diluted underlying earnings per share	196,855	195,792

Notes to the group financial statements

12. Earnings per share (continued)**Continuing operations**

	Basic £m	2013 Diluted £m	Basic £m	2012 Diluted £m
Total (loss)/profit after tax	(47.5)	(47.5)	13.2	13.2
Non-underlying items (see reconciliation below)	89.3	89.3	41.8	41.8
Underlying profit after tax	41.8	41.8	55.0	55.0

	Basic Pence	2013 Diluted Pence	Basic Pence	2012 Diluted Pence
(Loss)/earnings per share	(24.6)	(24.6)	6.8	6.7
Underlying earnings per share	21.6	21.2	28.5	28.1

Continuing and discontinued operations

	Basic £m	2013 Diluted £m	Basic £m	2012 Diluted £m
Total (loss)/profit after tax	(47.5)	(47.5)	15.3	15.3
Non-underlying items (see reconciliation below)	89.3	89.3	41.8	41.8
Underlying profit after tax	41.8	41.8	57.1	57.1

	Basic Pence	2013 Diluted Pence	Basic Pence	2012 Diluted Pence
(Loss)/earnings per share	(24.6)	(24.6)	7.9	7.8
Underlying earnings per share	21.6	21.2	29.6	29.2

Discontinued operations contributed earnings per share of 1.1p in the year ended 31 October 2012. There were no discontinued operations in the year ended 31 October 2013.

The number of shares in issue differs from the number held by third parties due to the fact that the Company holds its own shares in treasury. Further information on own shares held is given in note 29.

Reconciliation of basic profit after tax to underlying profit after tax

Underlying basic earnings are defined as earnings before costs relating to business acquisitions and disposals, business restructuring and incident costs, profit on disposal of businesses, items deemed to be of an exceptional nature, impairment of goodwill and acquired intangibles, impairment of assets held for sale, amortisation of acquired intangibles and gains/losses on the movement in the fair value of derivative financial instruments, net of related tax effects. The directors consider this measure of earnings allows a more meaningful comparison of earnings trends. A reconciliation of the total and adjusted measures of profit after tax is set out below:

	2013 £m	2012 £m
(Loss)/profit after tax	(47.5)	15.3
Exclude:		
Acquisition and disposal related costs	3.2	8.2
Business restructuring and incident costs	11.7	11.9
Profit on disposal of business	–	(10.3)
Impairment of goodwill	50.9	22.5
Impairment of acquired intangibles	15.7	–
Impairment of assets held for sale	8.8	–
Intangible amortisation arising from business combinations	18.8	20.9
Gain on the movement in the fair value of derivative financial instruments	(0.1)	(1.9)
Tax on non-underlying items	(19.7)	(9.5)
Non-underlying items	89.3	41.8
Underlying profit after tax	41.8	57.1

13. Goodwill

	£m
Cost	
At 1 November 2011	243.7
De-recognised on disposal of subsidiary undertakings (see note 33)	(3.7)
Foreign exchange adjustments	(2.7)
At 31 October 2012	237.3
At 1 November 2012	237.3
Foreign exchange adjustments	2.7
At 31 October 2013	240.0
Accumulated impairment losses	
At 1 November 2011	–
Impairment	(22.5)
At 31 October 2012	(22.5)
At 1 November 2012	(22.5)
Impairment	(50.9)
Foreign exchange adjustments	1.7
At 31 October 2013	(71.7)
Carrying amount	
At 31 October 2013	168.3
At 31 October 2012	214.8

Goodwill acquired in a business combination is allocated at acquisition to the cash-generating units ("CGUs") that are expected to benefit from that business combination. The carrying amount of the goodwill has been allocated to the Group's principal CGUs.

An analysis of the pre-tax discount rates used and the carrying value of goodwill as at 31 October 2013 by the principal CGUs is shown as follows:

Notes to the group financial statements

13. Goodwill (continued)

	2013 %	2012 %	2013 £m	2012 £m
Simmel Difesa S.p.A.	13.8	13.8	47.2	44.9
Roke Manor Research Limited	10.6	14.0	28.3	28.3
Chemring Energetics UK Limited	12.0	12.8	18.1	18.1
Non-Intrusive Inspection Technology, Inc.	12.4	15.7	15.5	15.5
Chemring Detection Systems, Inc.	13.8	16.0	13.7	13.7
Chemring Energetic Devices, Inc.	11.0	11.9	12.9	12.9
Hi-Shear Technology Corporation	13.9	14.5	–	49.0
Other			32.6	32.4
			168.3	214.8

The Group tests goodwill at least annually for impairment. Tests are conducted more frequently if there are indications that goodwill might be impaired.

The recoverable amounts of the CGUs are determined from value-in-use calculations. The key assumptions for the value-in-use calculations are those regarding the discount rates, growth rates and expected changes to cash flows during the period for which management has 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 each of the CGUs.

Pre-tax discount rates, derived from the Group's post-tax weighted average cost of capital of 7.4% (2012: 7.8%) which has adjusted for a premium specific to each of the CGUs to account for differences in currency risk, country risk and other factors affecting specific CGUs, have been used to discount projected cash flows. These premiums range from 1% to 3% (2012: 1% to 4%).

The calculation has used the Group's forecast figures for the next five years. At the end of five years, the calculations assume the performance of the CGUs will grow at a nominal annual rate of 0.5% in perpetuity. The growth rates are based on management's view of industry growth forecasts. Changes in selling prices and direct costs are based on past practices and expectations of future changes. The Group prepares cash flow forecasts derived from the most recent financial forecasts 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, impairment losses have been recognised in relation to Hi-Shear of £50.9 million as a consequence of lower expectations of future trading performance and cash inflows, which have been informed by the recent integration of Hi-Shear with Chemring Energetic Devices, which form part of the Energetic Sub-Systems segment. These lower expectations reflect the continuing challenging economic conditions facing the defence industry within the US and the operational issues that have been encountered at Hi-Shear. In the year ended 31 October 2012 an impairment of goodwill of £22.5 million was recognised in respect of Chemring Ordnance and Chemring Energetic Devices Clear Lake facility. The impairments recognised in the consolidated income statement, as part of non-underlying items within continuing operating profit, in respect of goodwill and acquired intangibles are as follows:

Goodwill impairments	2013 £m	2012 £m
Hi-Shear Technology Corporation	50.9	–
Chemring Ordnance, Inc.	–	6.8
Chemring Energetic Devices, Inc.	–	15.7
	50.9	22.5

In respect of acquired intangible assets, an impairment of £15.7 million has been made in the year ended 31 October 2013 in relation to Chemring Energetic Devices' Clear Lake facility, as a result of lower expected cash inflows at this business. This reflects the continuing challenging economic conditions facing the defence industry within the US, and the markets served by this facility in particular. The value of impairments of acquired intangible assets is as follows:

Acquired intangibles impairment	2013 £m	2012 £m
Chemring Energetic Devices, Inc.	15.7	–

The impairment charges were primarily driven by business valuations that were negatively impacted by lower cash flows within business plans, reflecting the challenging economic conditions facing the defence industry in the US in particular.

Stress testing was performed and indicated that where a 10% fall in the forecast cash flows of the CGUs was modelled Hi-Shear would require an additional impairment charge of up to £3.0 million against acquired intangibles, Simmel Difesa would require an impairment charge of up to £5.0 million against goodwill, Chemring Detection Systems would require an impairment charge of up to £5.0 million against goodwill and Chemring Energetics UK would require an impairment charge of approximately £3.0 million against goodwill in these circumstances, but no impairment would be required for any other CGU in this scenario.

A 1% addition to the discount rate for each CGU was also modelled, and under these circumstances Hi-Shear would require an additional impairment charge of up to £3.0 million against acquired intangibles, Simmel Difesa would require an impairment charge of up to £4.0 million against goodwill, Chemring Detection Systems would require an impairment charge of up to £4.0 million against goodwill and Chemring Energetics UK would require an impairment charge of approximately £3.0 million against goodwill. The remaining CGUs would not require any impairment.

Setting long-term growth rates beyond the five year forecast period to zero would result in Hi-Shear requiring an additional impairment charge of up to £1.0 million against acquired intangibles and Chemring Detection Systems requiring an impairment charge of approximately £1.0 million against goodwill. The remaining CGUs would not require any impairment.

As part of the business restructuring process, certain businesses are in the process of being combined. We continue to monitor CGUs for impairment in light of this, and expect fewer principal CGUs going forward.

14. Other intangible assets

	Development costs £m	Acquired order book £m	Acquired technology £m	Acquired customer relationships £m	Patents and licences £m	Total £m
Cost						
At 1 November 2011	30.2	62.8	61.3	131.5	1.7	257.3
Additions	12.3	–	–	–	0.6	0.6
Disposals	(1.2)	–	–	–	–	–
Transfers between categories	(0.4)	–	–	–	0.4	0.4
Impairment	–	–	(0.8)	–	–	(0.8)
Foreign exchange adjustments	0.4	(2.1)	0.4	(2.7)	0.1	(4.3)
At 1 November 2012	41.3	60.7	60.9	128.8	2.8	253.2
Additions	7.4	–	–	–	0.7	0.7
Disposals	(2.6)	–	–	–	(0.4)	(0.4)
Transfer between categories	0.2	–	–	–	(0.2)	(0.2)
Transfer to assets held for sale	(0.5)	–	–	–	(0.8)	(0.8)
Foreign exchange adjustments	0.3	1.9	0.4	2.2	0.1	4.6
At 31 October 2013	46.1	62.6	61.3	131.0	2.2	257.1
Amortisation						
At 1 November 2011	6.9	33.4	7.9	23.5	1.0	65.8
Charge	4.3	4.6	5.3	11.0	0.3	21.2
Disposals	(0.8)	–	–	–	–	–
Foreign exchange adjustments	(0.1)	(1.4)	(0.2)	0.2	0.2	(1.2)
At 1 November 2012	10.3	36.6	13.0	34.7	1.5	85.8
Charge	5.5	2.8	5.3	10.7	0.4	19.2
Disposals	(1.8)	–	–	–	(0.3)	(0.3)
Transfer to assets held for sale	(0.5)	–	–	–	(0.1)	(0.1)
Impairment (see note 13)	–	–	–	15.7	–	15.7
Foreign exchange adjustments	(0.1)	1.5	–	(0.2)	–	1.3
At 31 October 2013	13.4	40.9	18.3	60.9	1.5	121.6
Carrying amount						
At 31 October 2013	32.7	21.7	43.0	70.1	0.7	135.5
At 31 October 2012	31.0	24.1	47.9	94.1	1.3	167.4

Notes to the group financial statements

14. Other intangible assets (continued)

Acquired intangible assets are recognised at fair value on acquisition 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 intangible assets are recognised at cost and are amortised over their estimated useful lives (see note 3).

15. Property, plant and equipment

	Land and buildings £m	Plant and equipment £m	Total £m
Cost or valuation			
At 1 November 2011	118.4	186.4	304.8
Additions	10.7	23.2	33.9
Disposals	(5.0)	(9.6)	(14.6)
Transfer between categories	1.3	(1.3)	–
Foreign exchange adjustments	(3.0)	(4.3)	(7.3)
At 1 November 2012	122.4	194.4	316.8
Additions	4.8	9.4	14.2
Disposals	(0.4)	(14.3)	(14.7)
Transfer between categories	(0.6)	0.6	–
Transfer to assets held for sale (see note 34)	(3.3)	(11.9)	(15.2)
Foreign exchange adjustments	0.3	1.6	1.9
At 31 October 2013	123.2	179.8	303.0
Depreciation			
At 1 November 2011	13.3	60.4	73.7
Charge	2.7	13.2	15.9
Disposals	(2.7)	(6.4)	(9.1)
Foreign exchange adjustments	(0.9)	(2.8)	(3.7)
At 1 November 2012	12.4	64.4	76.8
Charge	3.4	16.7	20.1
Disposals	(0.1)	(13.3)	(13.4)
Transfer to assets held for sale (see note 34)	(0.3)	(13.8)	(14.1)
Impairment	–	8.8	8.8
Foreign exchange adjustments	0.5	2.0	2.5
At 31 October 2013	15.9	64.8	80.7
Carrying amount			
At 31 October 2013	107.3	115.0	222.3
At 31 October 2012	110.0	130.0	240.0

The carrying amount of the Group's plant and equipment includes £5.7 million (2012: £6.0 million) in respect of assets held under finance leases. During the year, £3.0 million (2012: £4.6 million) of interest was capitalised, as set out in note 9. In the year, £0.6 million (2012: £0.1 million) of capitalised interest was charged as depreciation on completion of the relevant projects. This results in a net book value for capitalised interest of £14.1 million (2012: £11.7 million).

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 two pyrotechnic sites and on open market for the remainder.

	2013 £m	2012 £m
30 September 1997 depreciated replacement cost	5.8	5.8
Freehold at cost	117.4	116.6
	123.2	122.4

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

	2013 £m	2012 £m
Cost	121.2	120.4
Accumulated depreciation	(15.2)	(11.7)
Historical cost value	106.0	108.7

All other tangible fixed assets are stated at historical cost.

The total additions during 2013 of £14.2 million is different to the figure of £12.3 million shown in the cash flow statement, due to the application of IAS 23 *Borrowing Costs* and the timing of payments.

At 31 October 2013, the Group had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £6.5 million (2012: £6.9 million).

16. Subsidiary undertakings

All subsidiary undertakings have been reflected in these financial statements. The undertakings held at 31 October 2013 which, in the opinion of the directors, principally affected the results for the year or the net assets of the Group, are shown below:

	Country of incorporation (or registration) and operation	% of issued ordinary share capital controlled by Chemring Group PLC	Segment
Subsidiary undertaking			
Chemring Countermeasures Limited	England	100	Countermeasures
Chemring Defence UK Limited	England	100	Pyrotechnics & Munitions
Chemring EOD Limited	England	100	Sensors & Electronics
Chemring Prime Contracts Limited	England	100	Pyrotechnics & Munitions
Roke Manor Research Limited	England	100	Sensors & Electronics
Chemring Energetics UK Limited	Scotland	100	Energetic Sub-Systems
Chemring Defence Germany GmbH	Germany	100	Pyrotechnics & Munitions
Alloy Surfaces Company, Inc.	USA	100	Countermeasures
Kilgore Flares Company LLC	USA	100	Countermeasures
Chemring Energetic Devices, Inc.	USA	100	Energetic Sub-Systems
Chemring Ordnance, Inc.	USA	100	Pyrotechnics & Munitions
Non-Intrusive Inspection Technology, Inc.	USA	100	Sensors & Electronics
Hi-Shear Technology Corporation	USA	100	Energetic Sub-Systems
Chemring Detection Systems, Inc.	USA	100	Sensors & Electronics
Chemring Australia Pty Limited	Australia	100	Countermeasures
Simmel Difesa S.p.A.	Italy	100	Pyrotechnics & Munitions
Chemring Nobel AS	Norway	100	Energetic Sub-Systems
Mecar S.A.	Belgium	100	Pyrotechnics & Munitions
Associated undertaking			
CIRRA S.A.	France	49	Countermeasures

Notes to the group financial statements

17. Interest in associate

	2013 £m	2012 £m
Interest in associate	1.5	1.4

Amounts relating to associate:

	2013 £m	2012 £m
Non-current assets	0.2	0.2
Current assets	1.6	1.3
Current liabilities	(0.6)	(0.5)
Net assets	1.2	1.0
Group's share of net assets of associate	0.6	0.5

	2013 £m	2012 £m
Revenue of associate	1.6	1.8
Profit after tax of associate	0.1	0.2
Group's share of profit after tax of associate	–	0.1

The results of the associate relate to the Group's share of CIRRA S.A. CIRRA S.A.'s financial year ended on 30 September 2013 and there is no material difference between the results as reported and those that would be obtained were CIRRA S.A. to have had a financial year ending on 31 October 2013.

18. Inventories

	2013 £m	2012 £m
Raw materials	37.9	44.1
Work in progress	60.9	49.1
Finished goods	14.9	20.6
	113.7	113.8

There are no significant differences between the replacement cost of inventory and the fair values shown above.

19. Trade and other receivables

	2013 £m	2012 £m
Trade receivables	77.8	92.7
Allowance for doubtful debts	(1.6)	(1.8)
	76.2	90.9
Contract receivables	104.8	87.6
Other debtors	7.1	6.1
Prepayments and accrued income	15.8	8.4
	203.9	193.0

All amounts shown above are due within one year.

The average credit period taken by customers on sales of goods, calculated using a countback basis, is 27 days (2012: 25 days). No interest is charged on receivables from the date of invoice to payment.

The Group's policy is to provide in full for trade receivables outstanding for more than 120 days beyond agreed terms, unless extenuating circumstances exist. Due to the nature of the customer base, the Group does not experience significant bad debt write-offs. The decrease in trade receivables is due to a lower level of revenue in the final month of the year compared to 2012. The increase in the average credit period was due to the timing of invoicing and cash receipts at the end of the year. An ageing analysis has not been shown, as all significant overdue receivables are covered by the allowance for doubtful debts. The vast majority of the trade receivables balance was not yet due at the year end based on the credit terms provided to customers.

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.

Included within cash is £0.8 million of restricted cash (2012: £4.5 million).

21. Borrowings

		2013 £m	2012 £m
Within current liabilities			
Bank loans and overdrafts	– Sterling denominated	0.3	31.2
	– Euro denominated	-	40.2
	– US dollar denominated	0.1	0.2
Other overseas loans	– Euro denominated	-	2.4
Finance leases	– Sterling denominated	1.6	1.7
Borrowings due within one year		2.0	75.7
Within non-current liabilities			
UK bank loans	– Sterling denominated	0.3	0.7
Overseas bank loans	– US dollar denominated	-	0.2
Loan notes	– Sterling denominated	12.5	12.5
	– US dollar denominated	246.6	248.7
Finance leases	– Sterling denominated	1.4	2.9
Preference shares		0.1	0.1
Borrowings due after more than one year		260.9	265.1
		262.9	340.8

Analysis of borrowings by currency:

	2013 £m	2012 £m
Sterling	16.2	49.1
US dollar	246.7	249.1
Euro	-	42.6
Total	262.9	340.8

Notes to the group financial statements

21. Borrowings (continued)

The weighted average interest rates paid were as follows:

		2013 %	2012 %
Bank overdrafts		2.7	2.5
UK bank loans	– Sterling denominated	3.3	3.2
	– Euro denominated	4.9	5.7
Overseas bank loans	– US dollar denominated	3.2	2.7
Other loans	– Euro denominated	2.9	2.9
Loan notes	– Sterling denominated	6.8	6.8
	– US dollar denominated	4.8–6.3	5.3–6.3

An analysis of total borrowings by maturity is as follows:

	Bank loans and overdrafts £m	Loan notes £m	Other borrowings £m	2013 Total £m	Bank loans and overdrafts £m	Loan notes £m	Other borrowings £m	2012 Total £m
Borrowings falling due within:								
One year	0.4	–	1.6	2.0	71.6	–	4.1	75.7
Borrowings falling due within:								
One to two years	0.3	–	1.4	1.7	0.6	–	1.6	2.2
Two to five years	–	134.6	–	134.6	0.3	47.4	1.3	49.0
After five years	–	124.5	0.1	124.6	–	213.8	0.1	213.9
	0.3	259.1	1.5	260.9	0.9	261.2	3.0	265.1
Total borrowings	0.7	259.1	3.1	262.9	72.5	261.2	7.1	340.8

Other borrowings comprises finance leases and preference shares.

In January 2011, the Group completed a refinancing of its bank facilities with a syndicate of five banks. The resulting revolving credit facility, which is unsecured and provides both finance and funds for general working capital purposes, totals £230.0 million. The term of the facility extends to April 2015, with an option to extend for a further twelve months. This revolving credit facility provides access to committed lending and bonding line support. None of the borrowings in the current or the prior year were secured.

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 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 have been met. These facilities are at floating interest rates.

	2013 £m	2012 £m
Total undrawn borrowings	126.8	143.9

The Group is subject to two key financial covenants which are tested quarterly, relating to the ratio between underlying earnings before interest, tax, depreciation and amortisation ("underlying EBITDA") and debt (the "debt ratio"), and the ratio between underlying EBITDA and finance costs ("interest cover"). The revolving credit facility and the loan note agreements have different covenant compliance calculations – the primary difference being that the revolving credit facility uses consolidated net debt in the debt ratio, whereas the loan note agreements require consolidated total debt to be used.

The Group complied with both these covenants throughout the year, and the position at the year end was as follows:

	2013	2012
Covenant ratios – revolving credit facility		
Maximum allowed ratio of net debt to underlying EBITDA	3.25x	3.00x
Actual ratio of net debt to underlying EBITDA	2.65x	2.14x
Minimum allowed ratio of underlying EBITDA to finance costs	4.00x	4.00x
Actual ratio of underlying EBITDA to finance costs	4.98x	6.71x
Covenant ratios – loan note agreements		
Maximum allowed ratio of consolidated total debt to underlying EBITDA	3.50x	3.00x
Actual ratio of consolidated total debt to underlying EBITDA	2.78x	2.79x
Minimum allowed ratio of underlying EBITDA to finance costs	3.50x	3.50x
Actual ratio of underlying EBITDA to finance costs	5.61x	6.86x

22. Obligations under finance leases

	2013 £m	Minimum lease payments 2012 £m	2013 £m	Present value of minimum lease payments 2012 £m
Amounts payable under finance leases:				
Within one year	1.7	1.9	1.6	1.7
In the second to fifth years	1.5	3.2	1.4	2.9
Less future finance charges	(0.2)	(0.5)	–	–
Present value of lease obligations	3.0	4.6	3.0	4.6
Less amounts due within one year shown within current liabilities			(1.6)	(1.7)
Amount due for settlement after one year			1.4	2.9

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

23. Trade and other payables

	2013 £m	2012 £m
Current		
Trade payables	62.8	100.2
Other payables	44.4	38.7
Other tax and social security	3.2	5.3
Advance payments	17.4	11.7
Accruals and deferred income	48.9	45.6
	176.7	201.5
Non-current		
Other payables	2.3	4.3

Trade payables and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. Advance payments are amounts received from customers on larger contracts to fund working capital. The directors consider that the carrying amount of payables approximates to their fair value.

The average credit period taken on purchases of goods is 50 days (2012: 40 days). No interest is charged on trade payables from the date of invoice to payment.

Notes to the group financial statements

24. Financial instruments and risk management

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

The Group's global 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 foreign currency and interest rate risk, including:

- forward foreign exchange contracts to manage the exchange risk arising from transactional foreign exchange exposures; and
- interest rate swaps to mitigate the risk of movement in interest rates.

Foreign currency risk management

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

Transactional risk: The Group's policy is to hedge transactional currency exposures via the use of forward foreign exchange contracts. The measurement and control of this risk is 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 sterling equivalents of the carrying amounts of the Group's foreign currency denominated monetary assets and liabilities at the year end were as follows:

	USD	EUR	NOK	2013 AUD	USD	EUR	NOK	2012 AUD
Monetary assets (£m)	22.8	43.1	5.4	3.3	64.8	64.3	5.8	1.7
Monetary liabilities (£m)	299.2	72.6	4.5	4.1	300.8	103.0	3.3	3.5

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

	USD	EUR	NOK	2013 AUD	USD	EUR	NOK	2012 AUD
Borrowings (£m)	252.1	—	—	—	251.4	40.2	—	—

The Group uses forward foreign exchange contracts to hedge its currency risk, most with a maturity of less than one year from inception. The exchange rates which have the most significant effect on the Group are those relating to the US dollar and the Euro.

The following table details the forward foreign exchange contracts outstanding:

	Average exchange rate		Expiring within one year	
	2013	2012	2013 £m	2012 £m
US dollar	1.56	1.54	32.5	12.2

The principal amounts of the Group's US dollar loan notes have been accounted for as a net investment hedge of the US businesses. This hedge was effective throughout the year and the losses arising on translation have been offset against the gains on retranslation of these businesses in reserves.

Foreign currency sensitivity analysis

The following table details the Group's sensitivity to a 10 cent movement in the relevant foreign currencies against sterling with regards to its income statement. This sensitivity represents management's assessment of a reasonably possible change in its foreign exchange rates. This sensitivity analysis only includes translation of the results of foreign currency denominated companies and so does not factor in the impact on the results of sterling or other currency companies that have transactions in US dollars or euros.

	+10 cents				- 10 cents			
	US dollar impact		Euro impact		US dollar impact		Euro impact	
	2013 £m	2012 £m	2013 £m	2012 £m	2013 £m	2012 £m	2013 £m	2012 £m
Revenue	(17.8)	(21.6)	(11.8)	(15.2)	20.2	24.5	14.0	17.9
Underlying operating profit	(2.7)	(2.7)	(0.9)	(1.9)	3.0	3.0	1.1	2.2
Interest	1.0	1.0	0.2	0.4	(0.9)	(0.9)	(0.2)	(0.3)
Profit before tax	(1.7)	(1.7)	(0.7)	(1.5)	2.1	2.1	0.9	1.9

Interest rate risk

The Group finances its operations through a mixture of retained profits, bank and loan note borrowings, and leasing. The Group's policy is that no more than 75% of gross debt should have fixed interest rates. During the year, the average fixed interest level was within this policy.

The UK borrowings are denominated in sterling and US dollar, and at the shorter end are subject to floating rates of interest. The Group has entered into a floating to fixed interest rate swap for €50.0 million of Euro borrowings at a weighted average rate of 3.77% and a fixed to floating interest rate swap for \$80.0 million of US dollar borrowings at a weighted average rate of 4.20%.

The Group has outstanding fixed interest loan notes in the US, repayable in November 2016 (\$80.0 million), November 2017 (£12.5 million and \$125.0 million) and November 2019 (\$200.0 million). This arrangement provides a natural hedge against the Group's investment in its US businesses.

As the Group has predominantly fixed interest rate debt, a change in interest rates would not have an immediate significant impact on the income statement. An increase/(decrease) in interest rates of 1% would cause the finance expense to increase/(decrease) by £0.7 million.

Liquidity risk

The table below details the maturity profile of the Group's derivative financial instruments and loans (excluding finance leases, preference shares and capitalised facility fees):

	2013			2012		
	Derivative payables £m	Loans and overdrafts £m	Total £m	Derivative payables £m	Loans and overdrafts £m	Total £m
Falling due within:						
One year	49.6	0.4	50.0	12.2	77.1	89.3
One to two years	11.1	0.3	11.4	11.5	0.6	12.1
Two to five years	–	140.1	140.1	9.9	49.9	59.8
After five years	–	124.5	124.5	–	214.2	214.2
	60.7	265.3	326.0	33.6	341.8	375.4

Notes to the group financial statements

24. Financial instruments and risk management (continued)

The profile of the Group's financial assets by underlying currency and balance sheet classification is as follows:

	2013 £m	2012 £m
Sterling	65.5	62.9
US dollar	43.6	106.6
Australian dollar	3.4	4.9
Euro	103.7	111.0
Other currencies	5.2	5.6
	221.4	291.0
Overdraft offset	(24.7)	(15.5)
	196.7	275.5

	2013 £m	2012 £m
Cash at bank and in hand	14.2	96.0
Trade receivables	76.2	90.9
Contract receivables	104.8	87.6
Derivative financial instruments	1.5	1.0
	196.7	275.5

Cash balances held in the UK have a right of interest offset against UK-based overdraft balances. Overseas cash balances have a weighted average interest rate of 0.1% (2012: 0.1%) and are at a floating rate.

The foreign currency balances are predominantly attributable to overseas business units and therefore do not result in significant exposure to transactional risks for the Group. Included within cash is £0.8 million of restricted cash (2012: £4.5 million) (see note 20).

The profile of the Group's financial liabilities by underlying currency and balance sheet classification is as follows:

	Floating rate £m	Fixed rate £m	2013 Total £m	Floating rate £m	Fixed rate £m	2012 Total £m
Sterling	–	(72.5)	(72.5)	(30.9)	(75.5)	(106.4)
US dollar	(49.8)	(222.2)	(272.0)	(49.9)	(248.6)	(298.5)
Euro	–	(54.1)	(54.1)	(2.4)	(100.3)	(102.7)
Other currencies	–	(6.8)	(6.8)	–	(5.9)	(5.9)
	(49.8)	(355.6)	(405.4)	(83.2)	(430.3)	(513.5)
Overdraft offset			24.7			15.5
			(380.7)			(498.0)

	2013 £m	2012 £m
Bank loans and overdrafts	(0.4)	(71.6)
UK loans	(0.3)	(0.7)
Loan notes	(259.1)	(261.2)
Overseas loans	–	(0.2)
Other loans	–	(2.4)
	(259.8)	(336.1)
Preference shares (see note 27)	(0.1)	(0.1)
Obligations under finance leases (see note 22)	(3.0)	(4.6)
	(262.9)	(340.8)
Trade payables due within one year	(62.8)	(100.2)
Accruals	(46.6)	(44.8)
Other tax and social security	(3.2)	(5.3)
Derivative financial instruments due within one year	(0.4)	(0.1)
Trade payables due after more than one year	(2.3)	(4.3)
Derivative financial instruments due after more than one year	(2.5)	(2.5)
	(380.7)	(498.0)

A right of offset exists for currency amounts held within the UK by Barclays Bank PLC. These are used to offset the interest charged on any UK overdraft.

The weighted average interest rate of fixed rate financial liabilities at 31 October 2013 was 5.8% (2012: 5.1%) and the weighted average period of funding was five years (2012: four years).

Derivative financial instruments

The Group has two interest rate structures, one from floating rate to fixed rate that expires in April 2015 at a rate of 3.77%, and one from fixed rate to floating rate that expires in May 2015 at a rate of 4.20%. The fair value of interest rate swaps recognised on the balance sheet at 31 October 2013 was a liability of £2.5 million (2012: £2.4 million). The Group also has forward foreign exchange contracts with fair values of £0.4 million liability (2012: £0.2 million liability) and £1.5 million asset (2012: £1.0 million asset). The net value of these derivative financial instruments is a liability of £1.4 million (2012: £1.6 million).

The following table details the fair value of derivative financial instruments recognised in the balance sheet:

	2013 £m	2012 £m
Interest rate swaps	(2.5)	(2.4)
Forward foreign exchange contracts	1.1	0.8
	(1.4)	(1.6)

These derivative financial instruments are classified on the balance sheet as follows:

	2013 £m	2012 £m
Included in current assets	1.5	1.0
Included in current liabilities	(0.4)	(0.1)
Included in non-current liabilities	(2.5)	(2.5)
	(1.4)	(1.6)

Notes to the group financial statements

24. Financial instruments and risk management (continued)

The following table details the gain on fair value movements on derivative financial instruments recognised in the income statement:

	2013 £m	2012 £m
Change in fair value of derivative financial instruments	0.1	1.9

Fair value hierarchy

IFRS 7 *Financial Instruments: Disclosures* requires companies that carry financial instruments at fair value in the balance sheet to disclose their level of visibility, determining into which category those financial instruments fall under the fair value hierarchy.

The fair value measurement hierarchy is as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 – Inputs for the asset or liability that are not based on observable market data (i.e. as unobservable inputs).

The following tables present the Group's assets and liabilities that are measured at fair value:

	Level 1 £m	Level 2 £m	2013 Total £m	Level 1 £m	Level 2 £m	2012 Total £m
Assets						
Forward foreign exchange contracts	–	1.5	1.5	–	1.0	1.0
Total assets	–	1.5	1.5	–	1.0	1.0

	Level 1 £m	Level 2 £m	2013 Total £m	Level 1 £m	Level 2 £m	2012 Total £m
Liabilities						
Borrowings	–	(259.1)	(259.1)	(71.4)	(261.2)	(332.6)
Interest rate swaps	–	(2.5)	(2.5)	–	(2.4)	(2.4)
Forward foreign exchange contracts	–	(0.4)	(0.4)	–	(0.2)	(0.2)
Total liabilities	–	(262.0)	(262.0)	(71.4)	(263.8)	(335.2)

There were no assets or liabilities that were classed under Level 3 on the fair value hierarchy.

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. Whilst 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 monitored on an ongoing basis using credit ratings assigned by international credit rating agencies, the credit default swap market and market capitalisation.

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 are attributable to a small number of customers spread across diverse geographical areas. Customers are mainly multinational organisations or government agencies with whom the Group has long-term business relationships. The Group's principal customers are government defence departments, such as the US Department of Defense, the UK Ministry of Defence and the Kingdom of Saudi Arabia Ministry of Defence and Aviation, as well as US and UK defence prime contractors such as Lockheed Martin, BAE Systems and General Dynamics.

Counterparties are monitored on an ongoing basis for credit risk, and as at the balance sheet date the risk was deemed to be low. Ongoing credit evaluation is performed on the financial condition of accounts receivable and action is taken to minimise the credit risk to the Group.

The Group's accounting policies and control procedures require letters of credit to be put in place for the majority of contracts with overseas customers. Any departures from this policy require approval by the Group finance function.

The Group's pricing risk is primarily in relation to the cost of raw materials and is not considered significant. Pricing 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. From time to time, the Group purchases its own shares on the market; the timing of these purchases depends on market prices. Primarily, such shares are intended to be used for satisfying awards under the Group's share-based incentive schemes. Buy and sell decisions are made on a specific transaction basis by the Board.

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

25. Provisions

	Legal provision £m	Environmental provision £m	Warranty provision £m	Restructuring provision £m	Other provision £m	Total £m
At 1 November 2012	1.4	1.5	2.0	1.4	1.4	7.7
Provided	3.4	1.2	1.0	1.6	–	7.2
Foreign exchange adjustments	–	(0.1)	0.1	–	–	–
Paid/released	(0.2)	–	–	(1.7)	–	(1.9)
At 31 October 2013	4.6	2.6	3.1	1.3	1.4	13.0

These provisions are classified on the balance sheet as follows:

	2013 £m	2012 £m
Included in current liabilities	2.7	2.8
Included in non-current liabilities	10.3	4.9
	13.0	7.7

It is not possible to estimate more accurately the expected timing of any resulting outflows of economic benefits.

The legal provision represents the estimated legal liabilities faced by the Group as at the balance sheet date. Further details of the Group's contingent liabilities can be found in note 39.

The environmental provision is held in respect of potential liabilities associated with the Group's facilities in Illinois, USA and Belgium.

The warranty provision at 31 October 2013 represents management's best estimate of the Group's liability, based on past experience for defective products.

The restructuring provision at 31 October 2013 relates to Chemring Countermeasures, Chemring Energetics UK, CHG Group, and Alloy Surfaces Company. The provision is associated with the Performance Recovery Programme, and represents management's best estimate of the costs to be incurred on restructuring programmes during 2014.

Notes to the group financial statements

26. Deferred tax

The following are the principal deferred tax liabilities/(assets) recognised by the Group and movements thereon:

	Accelerated tax depreciation £m	Retirement benefit obligations £m	Tax losses £m	Acquired intangibles £m	Other £m	Total £m
At 1 November 2011	18.9	(6.4)	(8.6)	23.5	9.9	37.3
(Credit)/charge to income	(0.9)	0.9	4.5	(5.9)	1.3	(0.1)
(Credit)/charge to equity	(0.3)	(0.7)	–	(0.7)	0.3	(1.4)
At 1 November 2012	17.7	(6.2)	(4.1)	16.9	11.5	35.8
Credit to income	(0.3)	–	(0.4)	(13.3)	(7.4)	(21.4)
Charge to equity	–	0.9	–	0.9	0.9	2.7
Reclassification	–	–	–	16.4	(16.4)	–
At 31 October 2013	17.4	(5.3)	(4.5)	20.9	(11.4)	17.1

Certain deferred tax balances have been reclassified between categories.

The Finance Act 2013, which provides for reductions in the main rate of corporation tax from 23% to 21% effective from 1 April 2014 and to 20% effective from 1 April 2015, was substantively enacted on 2 July 2013. These rate reductions have been reflected in the calculation of deferred tax at the balance sheet date.

The impact of any further changes in the main rate of corporation tax will be taken into account at subsequent reporting dates, once any such changes have been substantively enacted. 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:

	2013 £m	2012 £m
Non-current liabilities	38.8	52.7
Non-current assets	(21.7)	(16.9)
	17.1	35.8

At the balance sheet date, the Group had unrecognised tax losses of £48.2 million (2012: £43.1 million) potentially available for offset against future profits in certain circumstances, with the majority arising from recent acquisitions. No deferred tax asset has been recognised in respect of this amount because of the unpredictability of future taxable qualifying profit streams.

27. Share capital

	2013 £m	2012 £m
Issued and fully paid		
195,493,918 (2012: 195,491,341) ordinary shares of 1p each	2.0	2.0

2,577 ordinary shares (2012: 14,907) were issued under the Group's savings-related share schemes during the year.

The Company's 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. 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 a winding-up to receive, in priority to any other classes of shares, the sum of £1 per share together with any arrears of dividends.

28. Reserves

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

Included within retained earnings are £1.4 million of retained profits (2012: £1.3 million) relating to the associated undertaking, £0.9 million (2012: £0.1 million) relating to the share-based payment reserve and £0.8 million (2012: £0.8 million) of the Company's own shares held by the trustee of the Group's employee share ownership plan.

29. Own shares

	2013 £m	2012 £m
Balance at beginning of the year	9.6	6.6
Acquired	–	4.8
Issued to satisfy employee share awards	–	(1.8)
Balance at end of the year	9.6	9.6

The own shares reserve represents the cost of shares in Chemring Group PLC purchased in the market and held by the Group to satisfy awards under the Group's share-based incentive schemes, details of which are set out in note 31. Nil ordinary shares (2012: 1,215,000) were acquired during the year and nil (2012: 359,331) ordinary shares were distributed following the vesting of awards under the Chemring Group Performance Share Plan. The total number of ordinary shares held in treasury at 31 October 2013 was 2,198,814 (2012: 2,198,814), with an average cost of 439.0 pence (2012: 439.0 pence) per share. This represents 1.1% of the total issued and fully-paid ordinary share capital.

30. Obligations under non-cancellable operating leases

	2013 £m	2012 £m
Minimum lease payments under operating leases recognised in the income statement	3.5	1.9

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:

	2013 £m	2012 £m
Within one year	2.0	3.7
In the second to the fifth years	4.7	7.0
	6.7	10.7

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.

31. Share-based payments

The Group operates share-based compensation arrangements to provide incentives to the Group's senior management and other eligible employees. The Group recognised a net charge of £1.0 million (2012: £0.1 million credit) in respect of share-based payments during the year.

Details of the four schemes which operated during the year are set out below.

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

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

	Number of conditional shares	
	2013	2012
Outstanding at beginning of the year	2,231,393	1,792,977
Awarded	1,753,267	1,785,720
Vested	–	(359,331)
Lapsed	(1,054,985)	(987,973)
Outstanding at end of the year	2,929,675	2,231,393
Subject to vesting at end of the year	–	–

Notes to the group financial statements

31. Share-based payments (continued)

The following awards were outstanding at 31 October 2013:

Date of award	Number of ordinary shares under award	Vesting price per share Pence	Date when awards will vest
19 January 2011	318,710	Nil	19 January 2014
27 January 2012	938,266	Nil	27 January 2015
21 November 2012	413,412	Nil	21 November 2015
31 January 2013	1,179,491	Nil	31 January 2016
27 June 2013	79,796	Nil	27 June 2016

The Group has applied a discount to the share-based payment, to reflect the anticipated achievement of the stipulated targets for each PSP award, based on the predicted figures within the Group's financial projections and expected number of leavers over the life of the PSP awards.

The PSP awards made in the year ended 31 October 2013 contained performance conditions based on achievement of share price targets, as opposed to the targets based on earnings per share growth targets used in prior years. The PSP awards made in the year ended 31 October 2013 have therefore been valued using the Monte Carlo Simulation model. The inputs into the Monte Carlo Simulation model are as follows:

	Date of award		
	21 November 2012	31 January 2013	27 June 2013
Share price at valuation	217.0p	283.6p	282.0p
Exercise price	nil	nil	nil
Risk free rate	0.38%	0.43%	0.78%
Expected dividend yield	3.50%	3.50%	3.50%
Expected volatility	40%	40%	40%
Fair value	71.5p	108.8p	107.9p

The weighted average fair value of awards made during the year was 100.0p (2012: 332.6p).

No awards vested in the year ended 31 October 2013. In the year ended 31 October 2012, the closing share prices on the dates of vesting of awards were 368.5p, 274.4p and 289.3p. The charge recognised in respect of PSP awards is based on their fair value at the grant date.

The Chemring Group Restricted Share Plan (the "RSP")

Under the RSP, deferred awards of ordinary shares are made at nil cost. Awards ordinarily vest on the second anniversary of the award date. The first awards under the RSP were made in February 2013.

	Number of deferred shares awarded	
	2013	2012
Outstanding at beginning of the year	—	—
Awarded	542,032	—
Lapsed	(32,683)	—
Outstanding at end of the year	509,349	—
Subject to vesting at end of the year	—	—

The following awards were outstanding at 31 October 2013:

Date of award	Number of ordinary shares under award	Vesting price per share Pence	Date when awards will vest
15 February 2013	509,349	Nil	15 February 2015

The Group has applied a discount to the share-based payment relating to the RSP, to reflect the expected number of leavers over the life of the RSP awards.

For the purpose of calculating the value of share-based payments, the share price is discounted based on the following

assumptions:

- dividend growth at 1p per annum; and
- weighted average cost of capital of 7.7%.

The weighted average fair value of awards made during the year was 257.6p (2012: nil).

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

Options were granted during the year on 30 July 2013.

	2013		2012	
	Number of share options	Weighted average exercise price Pence	Number of share options	Weighted average exercise price Pence
Outstanding at beginning of the year	782,171	279.8	505,164	430.2
Granted	222,874	239.0	553,724	223.0
Exercised	(2,577)	223.0	(14,115)	370.7
Lapsed	(166,091)	316.4	(262,602)	444.6
Outstanding at end of the year	836,377	261.8	782,171	279.8
Subject to exercise at end of the year	71,035	393.8	33,150	344.4

The following options were outstanding at 31 October 2013:

Date of award	Number of ordinary shares under award	Exercise price per share Pence	Dates between which options may be exercised
1 August 2008	57,345	373.6	1 October 2013 – 1 April 2014
31 July 2009	33,545	344.4	1 October 2014 – 1 April 2015
30 July 2010	13,690	478.4	1 October 2013 – 1 April 2014
30 July 2010	11,215	478.4	1 October 2015 – 1 April 2016
29 July 2011	22,437	508.0	1 October 2014 – 1 April 2015
29 July 2011	12,014	508.0	1 October 2016 – 1 April 2017
30 July 2012	337,437	223.0	1 October 2015 – 1 April 2016
30 July 2012	126,573	223.0	1 October 2017 – 1 April 2018
30 July 2013	145,062	239.0	1 October 2016 – 1 April 2017
30 July 2013	77,059	239.0	1 October 2018 – 1 April 2019

The weighted average fair value of options granted in the year was 68.4p (2012: 101.4p).

The weighted average fair value of options exercised in the year was 101.4p (2012: 83.0p).

The weighted average share price on exercise of the options during the year was 274.0p (2012: 365.1p).

The fair values of the share options in the UK Sharesave Plan are based on the difference between the exercise price and the share price on the grant date of the option.

Notes to the group financial statements

31. Share-based payments (continued)

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

The US Stock Purchase Plan provides 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. Options were granted during the year on 30 July 2013.

	2013		2012	
	Number of share options	Weighted average exercise price Pence	Number of share options	Weighted average exercise price Pence
Outstanding at beginning of the year	115,606	311.4	92,790	491.0
Granted	55,997	262.0	82,738	244.0
Exercised	–	–	(792)	498.8
Lapsed	(65,515)	362.9	(59,130)	496.5
Outstanding at end of the year	106,088	253.5	115,606	311.4
Subject to exercise at end of the year	–	–	–	–

The following options were outstanding at 31 October 2013:

Date of award	Number of ordinary shares under award	Exercise price per share Pence	Dates between which options may be exercised
30 July 2012	50,091	244.0	30 July 2014 – 29 October 2014
30 July 2013	55,997	262.0	30 July 2015 – 29 October 2015

The weighted average fair value of options granted in the year was 45.1p (2012: 46.0p).

The weighted average fair value of options exercised in the year was nil (2012: 78.8p).

The weighted average share price on exercise of the options during the year was nil (2012: 365.1p).

The fair values of the share options in the US Stock Purchase Plan are based on the difference between the exercise price and the share price on the date of grant of the option.

32. Acquisitions

No acquisitions were made during the year but as a result of ongoing mergers, disposals and acquisitions activity and acquisitions in prior years, acquisition and disposal related costs of £3.2 million (2012: £8.2 million) have been recognised in the income statement as non-underlying items, in accordance with IFRS 3 (Revised) *Business Combinations*. For the year ended 31 October 2013, the costs include £2.1 million relating to an onerous lease in respect of premises formerly occupied by a business disposed of by the Group in 2003. As part of the disposal terms, the Group guaranteed future lease payments and this guarantee has been called upon.

Acquisition and disposal related costs	2013 £m	2012 £m
Onerous lease cost	2.1	–
Mecar S.A.	–	0.1
Chemring Detection Systems, Inc.	–	0.8
Aborted acquisitions	0.3	0.6
Fees related to a third party approach for the Group	0.2	3.7
Joint ventures and other acquisition related costs	0.6	3.0
	3.2	8.2

This figure differs from the cash outflow from acquisition related costs of £3.8 million due to a net decrease in acquisition related costs within creditors and provisions at the year end of £0.6 million.

33. Discontinued operations

No disposals were made during the year.

On 31 July 2012, the Group completed the disposal of its marine business to Drew Marine for £30.4 million.

The results of the discontinued operations to the date of disposal which have been included in the consolidated income statement and consolidated statement of cash flows, were as follows:

	2013 £m	2012 £m
Revenue	–	15.1
Operating profit	–	3.1
Finance expense	–	(0.5)
Tax	–	(0.5)
Profit after tax	–	2.1

	2013 £m	2012 £m
Net cash inflow from operating activities	–	3.3
Net cash outflow from financing activities	–	(0.5)
Net cash flow from discontinued operations	–	2.8

The net assets of the marine business at the date of disposal were as follows:

	£m
Property, plant and equipment	1.2
Inventories	4.5
Trade receivables	6.0
Cash and cash equivalents	3.5
Trade payables	(2.7)
Other payables	(1.7)
Provisions	(0.7)
Remove cash and cash equivalents	(3.5)
Attributable goodwill	3.7
Attributable disposal costs	9.8
	20.1
Profit on disposal	10.3
Total consideration	30.4
Satisfied by:	
Cash and cash equivalents	32.0
Deferred working capital adjustment	(1.6)
	30.4
Net cash inflow arising on disposal:	
Consideration received in cash and cash equivalents	32.0
Less cash and cash equivalents disposed of	(3.5)
Less payments for attributable disposal costs	(6.7)
	21.8

The deferred working capital adjustment was settled in cash by the Group in December 2012.

Notes to the group financial statements

34. Held for sale

Substantially all of the assets of Chemring Energetic Devices' business located in Clear Lake, South Dakota have been classified as held for sale at 31 October 2013.

The sale was agreed on 19 December 2013 and is expected to be completed in early 2014. Gross sale proceeds are \$10.0 million (£6.1 million), subject to a working capital adjustment.

The major classes of assets and liabilities classified as held for sale at 31 October 2013 were as follows:

	£m
Property, plant and equipment	1.1
Other intangible assets	0.7
Inventories	2.9
Trade and other receivables	2.0
Assets held for sale	6.7
Trade and other payables	(1.1)
Liabilities held for sale	(1.1)

The property, plant and equipment balance of £1.1 million is stated after an impairment charge of £8.8 million (see note 5).

35. Pensions

In the UK, the Group operates a defined benefit scheme (the "Chemring Group Staff Pension Scheme"). In Germany, Chemring Defence Germany GmbH operates a defined benefit scheme (the "Chemring Defence Germany Scheme") and in Norway, Chemring Nobel AS operates a defined benefit scheme (the "Chemring Nobel Scheme"). The other UK and overseas pension arrangements are all defined contribution schemes, with a combined cost of £6.3 million (2012: £6.6 million).

The Chemring Group Staff Pension Scheme is a funded scheme and the assets of the scheme are held in a separate trustee administered fund. The scheme was closed to future accrual on 6 April 2012. A full actuarial valuation of the Chemring Group Staff Pension Scheme as at 6 April 2012 has been completed and updated to 31 October 2013 by a qualified actuary, using the projected unit credit method. The main assumptions for the scheme are detailed below. The net deficit of the Chemring Group Staff Pension Scheme was £24.2 million at 31 October 2013 (2012: £25.9 million).

Under the funding plan agreed with the trustees following the 2012 actuarial valuation, the Company has agreed to eliminate the deficit calculated at that time over a period of seven years. This funding plan provides for contributions of £8.2 million to be paid by the Group in monthly instalments during the year ending 31 October 2014, and thereafter, £5.0 million per annum to be paid in monthly instalments until 2019. The Company and the trustees monitor funding levels annually, and a new funding plan is agreed with the trustees every three years, based on actuarial valuations. The Group considers that the current contribution rates agreed with the trustees are sufficient to eliminate the calculated deficit over the agreed period.

The Group has provided a bank guarantee and letters of credit totalling £27.2 million (2012: £27.2 million) to the Chemring Group Staff Pension Scheme, comprising a £20.0 million letter of credit and a £7.2 million bank guarantee, which may only be drawn upon certain events of default by the Company.

On 31 July 2012, the disposal of the marine business triggered a payment of £1.6 million falling due to the Chemring Group Staff Pension Scheme under Sections 75 and 75A of the Pensions Act 1995. This debt was settled in full by the Group on 22 August 2012.

The Chemring Defence Germany Scheme is an unfunded scheme. The actuarial liability has been calculated at 31 October 2013 by a qualified actuary using the projected unit credit method. The main assumptions used were a discount rate of 6.0%, inflation rate of 1.8% and rate of increase in deferred pensions of nil %. The net deficit of the Chemring Defence Germany Scheme was £0.9 million at 31 October 2013 (2012: £0.8 million).

The Chemring Nobel Scheme is an unfunded scheme. The actuarial liability has been calculated at 31 October 2013 by a qualified actuary using the projected unit credit method. The main assumptions used were a discount rate of 4.1% and rate of increase in deferred pensions of 0.6%. The net deficit of the Chemring Nobel Scheme was £nil at 31 October 2013 (2012: £0.3 million).

As principal employer on all schemes and due to the similarity of the schemes, the schemes have been netted-off in the table below.

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

	2013 £m	2012 £m	2011 £m
Present value of funded and unfunded obligations	(76.7)	(71.6)	(65.2)
Fair value of schemes' assets	51.6	44.6	40.0
Net retirement benefit obligation recognised in the balance sheet	(25.1)	(27.0)	(25.2)

An analysis of the retirement benefit obligation recognised in the balance sheet by scheme is as follows:

	2013 £m	2012 £m	2011 £m
Chemring Group Staff Pension Scheme	(24.2)	(25.9)	(23.7)
Chemring Defence Germany Scheme	(0.9)	(0.8)	(1.3)
Chemring Nobel Scheme	–	(0.3)	(0.2)
Net retirement benefit obligation recognised in the balance sheet	(25.1)	(27.0)	(25.2)

Amounts recognised in the income statement in respect of the Group's defined benefit schemes are as follows:

	2013 £m	2012 £m
Amounts included within operating profit		
Current service cost	(0.2)	(1.0)
Curtailment gain	–	1.4
	(0.2)	0.4
Amounts included within finance expense		
Expected return on scheme assets	2.5	2.4
Discount on scheme liabilities	(3.0)	(3.2)
	(0.5)	(0.8)
Net charge recognised in the income statement	(0.7)	(0.4)

Amounts recognised in the statement of comprehensive income are as follows:

	2013 £m	2012 £m
Actual return less expected return on pension scheme assets at the balance sheet date	5.1	3.0
Actuarial losses and changes in assumptions underlying the present value of the scheme liabilities at the balance sheet date	(4.4)	(5.7)
Actuarial gain/(loss) recognised in the statement of comprehensive income	0.7	(2.7)

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

	2013 £m	2012 £m
Opening defined benefit obligations	(71.6)	(65.2)
Service cost	(0.2)	(1.0)
Interest cost	(3.0)	(3.2)
Contributions from scheme members	–	(0.3)
Actuarial losses and changes in assumptions underlying the present value of the scheme liabilities	(4.4)	(5.7)
Benefits paid	2.5	2.4
Curtailment gain	–	1.4
Closing defined benefit obligations	(76.7)	(71.6)

Notes to the group financial statements

35. Pensions (continued)

Changes in the fair value of the schemes' assets were as follows:

	2013 £m	2012 £m
Opening fair value of schemes' assets	44.6	40.0
Expected return on scheme assets	2.5	2.4
Actuarial gains less expected return on pension scheme assets	5.1	1.4
Contributions from scheme members	–	0.3
Contributions from sponsoring companies	1.9	1.3
Additional contributions in respect of the Section 75 debt on the disposal of the marine business	–	1.6
Benefits paid	(2.5)	(2.4)
Closing fair value of schemes' assets	51.6	44.6

The schemes' assets and the long-term expected rates of return on assets were as follows:

	Long-term rate of return expected	2013 £m	Long-term rate of return expected	2012 £m	Long-term rate of return expected	2011 £m
Equities	7.0%	35.9	6.8%	31.2	6.8%	27.7
Bonds	3.1%	15.7	3.2%	13.4	3.4%	12.3
Total fair value of schemes' assets		51.6		44.6		40.0

The analysis of the pension schemes' assets at 31 October 2013 is as follows:

	2013 %	2012 %	2011 %
Equities	69.5	70.0	69.3
Bonds	30.5	30.0	30.7
	100.0	100.0	100.0

The expected rates of return on assets 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 investment portfolios.

History of experience gains and losses:

	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Present value of funded and unfunded obligations	(76.7)	(71.6)	(65.2)	(61.9)	(63.0)
Fair value of schemes' assets	51.6	44.6	40.0	38.9	34.9
Deficit in the schemes	(25.1)	(27.0)	(25.2)	(23.0)	(28.1)
Experience gains on scheme liabilities	1.3	–	–	3.8	–
Percentage of scheme liabilities	1.7%	–	–	6.1%	–
Experience gains/(losses) on scheme assets	5.1	1.4	(1.3)	1.4	4.2
Percentage of scheme assets	9.9%	3.1%	(3.3)%	3.6%	12.0%

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

	2013 £m	2012 £m
Opening deficit in schemes	(27.0)	(25.2)
Current service cost	(0.2)	(1.0)
Curtailement gain	–	1.4
Contributions	1.9	1.3
Other finance costs	(0.5)	(0.8)
Actuarial gain/(loss) and changes in assumptions underlying the present value of scheme liabilities	0.7	(2.7)
Closing deficit in the schemes	(25.1)	(27.0)

The principal assumptions used in the actuarial valuation of the Chemring Group Staff Pension Scheme were as follows:

	2013 %	2012 %
Discount rate	4.2	4.4
Rate of increase in salaries	n/a	n/a
Rate of increase in deferred pensions	3.3	2.8
Rate of increase in pensions in payment (where applicable)	3.3	2.8
Inflation – RPI	3.5	2.9
– CPI	2.5	2.2
Expected return on scheme assets	4.2	5.8

In determining defined benefit obligations, the Group uses mortality assumptions which are based on published mortality tables. For the Chemring Group Staff Pension Scheme, the actuarial table currently used is SAPS Year of Birth Tables with a medium cohort and 1% underpin.

This results in the following life expectancies at age 65:

	2013	2012
Future pensioners – male	88.6	88.2
– female	91.3	91.0
Current pensioners – male	86.3	86.3
– female	89.2	89.1

The assumption considered to be the most significant is the discount rate adopted. If the discount rate used in determining retirement benefit obligations were to change by 0.1% then it is predicted that the deficit in the scheme would change by approximately £1.4 million. A change in the rate of inflation by 0.1% is predicted to change the deficit by approximately £0.9 million and a one year change to the longevity assumption would change the deficit by approximately £2.5 million.

The Group anticipates contributions to the defined benefit schemes for the year ending 31 October 2014 will be £8.2 million (2013: £2.0 million).

Notes to the group financial statements

36. Cash generated from underlying operations

	2013 £m	2012 £m
Operating (loss)/profit from continuing operations	(36.9)	37.0
Operating profit from discontinued operations	–	3.1
	(36.9)	40.1
Impairment of goodwill	50.9	22.5
Impairment of acquired intangibles	15.7	–
Impairment of assets held for sale	8.8	–
Amortisation of development costs	5.5	4.3
Intangible amortisation arising from business combinations	18.8	20.9
Amortisation of patents and licences	0.4	0.3
Loss on disposal of non-current assets	2.2	3.4
Depreciation of property, plant and equipment	20.1	15.9
Gain on the movement in the fair value of derivative financial instruments	(0.1)	(1.9)
Share-based payment expense/(credit)	0.9	(0.1)
Employer contributions towards pension scheme deficit reduction plan	(1.0)	–
Difference between pension contributions paid and amount recognised in income statement	(0.3)	0.6
Operating cash flows before movements in working capital	85.0	106.0
Decrease in inventories	0.1	28.0
Increase in trade and other receivables	(15.9)	(8.2)
Decrease in trade and other payables	(21.0)	(20.2)
Increase in provisions	5.5	2.8
	53.7	108.4
Add back non-underlying items:		
Acquisition and disposal related costs	3.2	8.2
Business restructuring and incident costs	11.7	11.9
Profit on disposal of business	–	(10.3)
Cash generated from underlying operations	68.6	118.2
Analysed as:		
Continuing operations	68.6	114.9
Discontinued operations	–	3.3
	68.6	118.2

37. Reconciliation of net cash flow to movement in net debt

	2013 £m	2012 £m
(Decrease)/increase in cash and cash equivalents during the year	(81.9)	5.3
Decrease in debt and lease financing due to cash flows	82.5	12.3
Decrease in net debt resulting from cash flows	0.6	17.6
Effect of foreign exchanges rate changes	(2.5)	1.9
Amortisation of debt finance costs	(2.0)	(1.6)
Movement in net debt	(3.9)	17.9
Net debt at beginning of the year	(244.8)	(262.7)
Net debt at end of the year	(248.7)	(244.8)

38. Analysis of net debt

	At 1 Nov 2012 £m	Cash flows £m	Non-cash changes £m	Exchange rate effects £m	At 31 Oct 2013 £m
Cash at bank and in hand	96.0	(81.9)	–	0.1	14.2
Debt due within one year	(74.0)	79.1	(3.6)	(1.9)	(0.4)
Debt due after one year	(262.1)	1.7	1.6	(0.6)	(259.4)
Finance leases	(4.6)	1.7	–	(0.1)	(3.0)
Preference shares	(0.1)	–	–	–	(0.1)
	(244.8)	0.6	(2.0)	(2.5)	(248.7)

39. Contingent liabilities

The Group enters into contracts which have offset commitments. These requirements are valued at the time of the contract being awarded. The cost of the offsets are reviewed throughout the contract life and provided for within the contract costings to the extent of the potential liability.

At 31 October 2013, the Group had contingent liabilities in respect of bank and contractual performance guarantees and other matters arising in the ordinary course of business. Where it is expected that a material liability will arise in respect of these matters, appropriate provision is made within the financial statements. As the conditions of these guarantees are currently being met, no obligating event is foreseeable and therefore no provision has been made.

The Group is, from time to time, party to legal proceedings and claims, and is involved in correspondence relating to potential claims, which arise in the ordinary course of business. The Group is currently engaged in pre-action correspondence in relation to the manufacture of certain components for the NLAW combat weapon by Chemring Energetics UK. In addition, Simmel Difesa, may become indirectly involved in proceedings relating to environmental issues in the Colleferro region of Italy, where its principal manufacturing site is located.

In light of the current status of these matters, the directors do not consider the outcome of all the proceedings, actions and claims in which it is currently involved, either individually or in aggregate, will have a material adverse effect upon the Group's financial position. A provision of £4.6 million (2012: £1.4 million) exists to cover potential legal costs for the Group with regards to pending and probable legal actions. This provision is detailed in note 25.

The Group has a £2.5 million deductible under its material damage and business interruption insurance policy, subject to a maximum liability of £3.5 million in any one year.

Notes to the group financial statements

40. 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. Transactions with the Group's pension schemes are disclosed in note 35.

Trading transactions

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

Remuneration of key management personnel

The executive directors constitute the key management personnel of the Group. Their remuneration is set out below in aggregate for each of the categories specified in IAS 24 *Related Party Disclosures*. Further information on the remuneration of individual directors is provided in the audited part of the directors' remuneration report on pages 76 to 85.

The directors of the Company had no material transactions with the Company during the year, other than in connection with their service agreements. The remuneration of the executive directors is determined by the Remuneration Committee, having regard to the performance of the individuals and market trends. The remuneration of the non-executive directors is determined by the Board, having regard to the practice of other companies and the particular demands of the Group.

	2013 £m	2012 £m
Remuneration of key management personnel	1.5	2.5

Included within the 2012 charge is £1.1 million relating to compensation for loss of office for David Price and Paul Rayner. Further detail can be found in the directors' remuneration report.

41. Post balance sheet event

On 19 December 2013, the Group agreed the conditional sale of substantially all of the assets of Chemring Energetic Devices' business in Clear Lake, South Dakota. Gross sales proceeds are expected to be \$10.0 million (£6.1 million), subject to a working capital adjustment. This business has been classified as held for sale as at 31 October 2013.

Parent company balance sheet

as at 31 October 2013

	Note	£m	2013 £m	£m	2012 £m
Fixed assets					
Tangible assets	2		0.3		0.7
Investments	3		575.2		575.2
			575.5		575.9
Current assets					
Debtors - due within one year	5	12.9		12.7	
- due after more than one year	5	250.8		279.6	
Cash at bank and in hand		1.6		21.1	
		265.3		313.4	
Creditors due within one year	6	(23.1)		(122.7)	
Net current assets			242.2		190.7
Total assets less current liabilities			817.7		766.6
Creditors due after more than one year	7		(487.1)		(451.0)
			330.6		315.6
Capital and reserves					
Called-up share capital	8		2.0		2.0
Share premium account	9	230.7		230.7	
Special capital reserve	9	12.9		12.9	
Profit and loss account	9	94.6		79.6	
		338.2		323.2	
Own shares	10	(9.6)		(9.6)	
			328.6		313.6
Shareholders' funds			330.6		315.6

These financial statements were approved and authorised for issue by the Board of directors on 23 January 2014.

Signed on behalf of the Board of Chemring Group PLC (registered number 86662)

Mark Papworth
Director

Steve Bowers
Director

Parent company statement of total recognised gains and losses

for the year ended 31 October 2013

	Note	2013 £m	2012 £m
Profit for the year	9	28.8	6.9
Additional charge due to treasury shares		–	(0.5)
Total recognised gains and losses for the year		28.8	6.4

Parent company reconciliation of movements in shareholders' funds

for the year ended 31 October 2013

	Note	2013 £m	2012 £m
Profit for the year		28.8	6.9
Dividends		(14.7)	(31.1)
Profit/(loss) for the year		14.1	(24.2)
Other recognised losses		–	(0.5)
Ordinary shares issued	8	–	–
Share premium arising	9	–	0.1
Share-based payments (net of deferred tax)	9	0.9	(1.8)
Own shares	10	–	(3.0)
Net addition/(reduction) to shareholders' funds		15.0	(29.4)
Opening shareholders' funds		315.6	345.0
Closing shareholders' funds		330.6	315.6

Profit attributable to shareholders

In accordance with the concession granted under the Companies Act 2006, section 408, 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. The Company reported a profit for the financial year ended 31 October 2013 of £28.8 million (2012: £6.9 million).

The auditor's remuneration for audit and other services is disclosed in note 6 to the group financial statements.

Cash flow statement

In accordance with the exemption under FRS 1 (Revised) *Cash flow statements*, the Company's cash flow statement has not been presented separately in these financial statements.

Going concern

The directors have, at the time of approving the financial statements, a reasonable expectation that the Company has adequate resources to continue to adopt the going concern basis of accounting in preparing the financial statements. Further detail is contained in the financial review on page 32.

Notes to the parent company financial statements

for the year ended 31 October 2013

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 2006, applicable accounting standards and UK generally accepted accounting practice ("UK GAAP").

Related parties

The Company is exempt under FRS 8 *Related Party Disclosures* from disclosing transactions with other members of the Group.

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

Property, plant and equipment is 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:

Leasehold buildings	- the period of the lease
Plant and equipment	- up to ten 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 substantively 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, 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 prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at rates prevailing on the balance sheet date. These translation differences are included in the profit and loss account.

For a forward foreign exchange contract to be treated as a hedge the instrument must be related to actual foreign currency assets or liabilities, or to a probable commitment. It must involve the same currency or similar currencies as the hedged item and must also reduce the risk of foreign currency exchange movements on the Company's operations. Gains and losses arising on these contracts are deferred and recognised in the profit and loss account, or as adjustments to the carrying amount of fixed assets, only when the hedged transaction has itself been reflected in the Company's financial statements.

For an interest rate swap to be treated as a hedge the instrument must be related to actual assets or liabilities or a probable commitment, and must change the nature of the interest rate by converting a fixed rate to a variable rate or vice versa. Interest differentials under these swaps are recognised by adjusting interest payable over the periods of the contracts.

If an instrument ceases to be accounted for as a hedge, for example because the underlying hedged position is eliminated, the instrument is marked to market and any resulting profit or loss recognised at that time.

Notes to the parent company financial statements

for the year ended 31 October 2013

1. Chemring Group PLC accounting policies (continued)

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 profit and loss account, 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.

Pensions

The Company operates a defined benefit pension scheme. The defined benefit scheme is a multi-employer scheme including employees of other Group companies. It is not considered possible to allocate scheme assets and liabilities between the various companies and accordingly the scheme is accounted for as though it was a defined contribution scheme. The amount charged to the profit and loss account is the contribution payable in respect of the year. Differences between amounts payable and actually paid are shown as accruals or prepayments in the balance sheet.

The Company also operates a defined contribution pension scheme. The amount charged to the profit and loss account in respect of pension costs and other post-retirement benefits is the contributions payable in the year. Differences between contributions payable in respect of the year and contributions actually paid are shown as either accruals or prepayments in the balance sheet.

Share-based compensation

For grants made under the Company's share-based incentive schemes, amounts which reflect the fair value of options awarded at the time of grant are charged to the profit and loss account. Further details can be found within note 31 of the group financial statements.

2. Tangible assets

	Land and buildings £m	Plant and equipment £m	Total £m
Cost			
At 1 November 2012	0.5	1.6	2.1
Disposals	(0.3)	(0.1)	(0.4)
At 31 October 2013	0.2	1.5	1.7
Depreciation			
At 1 November 2012	0.2	1.2	1.4
Disposals	(0.1)	–	(0.1)
Charge for the year	–	0.1	0.1
At 31 October 2013	0.1	1.3	1.4
Net book value			
At 31 October 2013	0.1	0.2	0.3
At 31 October 2012	0.3	0.4	0.7

The Company had no capital commitments as at 31 October 2013 or 31 October 2012.

Land and buildings represent leasehold improvements.

3. Investments

	Shares in subsidiary undertakings £m	Loans to subsidiary undertakings £m	Total £m
Cost			
At 1 November 2012 and 31 October 2013	588.1	6.3	594.4
Impairment			
At 1 November 2012 and 31 October 2013	19.2	–	19.2
Net book value			
At 31 October 2013	568.9	6.3	575.2
At 31 October 2012	568.9	6.3	575.2

Notes to the parent company financial statements

for the year ended 31 October 2013

4. Investments in Group undertakings

The trading Group undertakings at 31 October 2013 were:

	Country of incorporation (or registration) and operation	% of issued ordinary share capital controlled by Chemring Group PLC	Segment
Trading Group undertaking			
Chemring Countermeasures Limited	England	100	Countermeasures
Chemring Defence UK Limited	England	100	Pyrotechnics & Munitions
*Chemring EOD Limited	England	100	Sensors & Electronics
Chemring Prime Contracts Limited	England	100	Pyrotechnics & Munitions
Roke Manor Research Limited	England	100	Sensors & Electronics
Chemring Energetics UK Limited	Scotland	100	Energetic Sub-Systems
*Chemring Defence Germany GmbH	Germany	100	Pyrotechnics & Munitions
*Alloy Surfaces Company, Inc.	USA	100	Countermeasures
*Kilgore Flares Company LLC	USA	100	Countermeasures
*Chemring Energetic Devices, Inc.	USA	100	Energetic Sub-Systems
*Chemring Ordnance, Inc.	USA	100	Pyrotechnics & Munitions
*Non-Intrusive Inspection Technology, Inc.	USA	100	Sensors & Electronics
*Hi-Shear Technology Corporation	USA	100	Energetic Sub-Systems
*Chemring Detection Systems, Inc.	USA	100	Sensors & Electronics
*Chemring Australia Pty Limited	Australia	100	Countermeasures
*Simmel Difesa S.p.A.	Italy	100	Pyrotechnics & Munitions
*Chemring Nobel AS	Norway	100	Energetic Sub-Systems
Mecar S.A.	Belgium	100	Pyrotechnics & Munitions
Associated undertaking			
CIRRA S.A.	France	49	Countermeasures

* Investments held by a subsidiary company

The directors consider that the carrying value of the investments does not exceed their fair value. Full details of the associated undertaking are disclosed in note 17 of the group financial statements.

5. Debtors

	2013 £m	2012 £m
Amounts due within one year		
Deferred tax asset (see note 11)	0.3	0.6
Other debtors	6.9	10.8
Corporation tax recoverable	5.0	–
Prepayments and accrued income	0.7	1.3
	12.9	12.7
Amounts due after more than one year		
Amounts owed by subsidiary undertakings	250.8	279.6

An asset of £1.5 million (2012: £1.0 million) is recognised within other debtors in respect of the fair value of derivative financial instruments (see note 24 of the group financial statements). The directors consider that the carrying value of the debtors approximates to their fair value.

6. Creditors due within one year

	2013 £m	2012 £m
Bank overdrafts	7.3	–
Bank loans	–	71.1
Trade creditors	1.3	0.5
Amounts owed to subsidiary undertakings	1.2	37.4
Other creditors	6.9	8.4
Other tax and social security	0.2	0.2
Accruals and deferred income	6.2	5.1
	23.1	122.7

A liability of £0.4 million (2012: £0.2 million) is recognised in other creditors in respect of the fair value of derivative financial instruments. Further details are shown in note 24 of the group financial statements.

7. Creditors due after more than one year

	2013 £m	2012 £m
Derivative financial instruments (see note 24 of the group financial statements)	2.5	2.5
Loan notes	259.1	261.2
Cumulative preference shares (62,500 shares of £1 each)	0.1	0.1
Amounts owed to subsidiary undertakings	225.4	187.2
	487.1	451.0

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 a winding-up to receive, in priority to any other classes of shares, the sum of £1 per share together with any arrears of dividends.

	2013 £m	2012 £m
Borrowings falling due within:		
Within one year	7.3	71.1
Between two and five years	134.6	47.4
After five years	124.5	213.8
	266.4	332.3

The interest incurred on the above borrowings is detailed within notes 9 and 21 of the group financial statements.

8. Called-up share capital

	2013 £m	2012 £m
Issued, allotted and fully paid		
195,493,918 (2012: 195,491,341) ordinary shares of 1p each	2.0	2.0

2,577 ordinary shares (2012: 14,907) were issued under the Group's savings-related share schemes during the year.

The preference shares are presented as a liability and accordingly are excluded from called-up share capital in the balance sheet.

Share-based incentive schemes

Full details of the schemes are disclosed in note 31 of the group financial statements.

Notes to the parent company financial statements

for the year ended 31 October 2013

9. Reserves

	Share premium account £m	Special capital reserve £m	Profit and loss account £m	Total £m
At 1 November 2012	230.7	12.9	79.6	323.2
Profit for the year	–	–	28.8	28.8
Ordinary shares issued	–	–	–	–
Dividends paid	–	–	(14.7)	(14.7)
Share-based payments (net of settlement)	–	–	0.9	0.9
At 31 October 2013	230.7	12.9	94.6	338.2

The share premium account and special capital reserve are not distributable. Of the £94.6 million in the profit and loss account, £31.1 million is distributable, with the remaining £63.5 million arising from the disposal of the investment in Simmel Difesa not being distributable.

The proposed final dividend in respect of the year ended 31 October 2013 of 3.8p per share will, if approved, absorb approximately £7.3 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.

10. Own shares

	2013 £m	2012 £m
Balance at beginning of the year	9.6	6.6
Acquired	–	4.8
Issued to satisfy employee share awards	–	(1.8)
Balance at end of the year	9.6	9.6

The own shares reserve represents the cost of shares in Chemring Group PLC purchased in the market and held by the Group to satisfy awards under the Group's share-based incentive schemes (see note 31 of the group financial statements). During the year, nil (2012: 1,215,000) ordinary shares were acquired and nil (2012: 359,331) ordinary shares were distributed following the vesting of awards under the Chemring Group Performance Share Plan. The total number of ordinary shares held in treasury at 31 October 2013 was 2,198,814 (2012: 2,198,814), with an average cost of £4.39 (2012: £4.39) per share. This represents 1.1% of the total issued and fully-paid ordinary share capital.

11. Deferred tax asset

	2013 £m	2012 £m
At beginning of the year	0.6	0.5
(Charge)/credit to profit and loss account	(0.3)	0.1
At end of the year	0.3	0.6
The amount provided represents:		
Other timing differences	0.3	0.6

The Company has considered the recoverability of the deferred tax asset and concluded that the expected future activities of the Company are sufficient to support this value.

12. Staff costs

	2013 Number	2012 Number
Average monthly number of total employees (including executive directors)	38	38

The costs incurred in respect of these employees (including share-based payments) were:

	2013 £m	2012 £m
Wages and salaries	5.3	4.8
Social security costs	0.7	0.6
Other pension costs	0.5	0.4
	6.5	5.8

Included within the 2012 charge is £1.1 million of wages and salaries, and £0.1 million of social security costs, relating to compensation for loss of office for David Price and Paul Rayner. Disclosures in respect of directors' emoluments can be found in the directors' remuneration report on pages 64 to 85.

Corporate Information

Headquarters and registered office

Chemring House
1500 Parkway
Whiteley
Fareham
Hampshire
PO15 7AF
England

Tel: +44 (0) 1489 881880
Fax: +44 (0) 1489 881123

Website: www.chemring.co.uk

Registration number

86662

Registrars

Computershare Investor Services PLC
The Pavilions
Bridgwater Road
Bristol
BS13 8AE

Find out more online

For more information about Chemring Group PLC, please visit www.chemring.co.uk where you can access the latest shareholder information:

- Current share price
- Key financial information
- Financial calendar
- Shareholder services and notices
- Corporate governance
- RSS news feeds
- Results and presentations
- Analysts' forecasts
- Regulatory news

Chemring Group PLC's Annual Report and Accounts 2013 can also be viewed online at www.chemring.co.uk/investors.

You can also view and download the Notice for our Annual General Meeting.

www.chemring.co.uk



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Chemring Group PLC

Chemring House

1500 Parkway

Whiteley

Fareham

Hampshire PO15 7AF

Tel: +44(0)1489 881880

Email: info@chemring.co.uk

www.chemring.co.uk