Defence Innovation Redefined!

TWENTY 16/17

INTEGRATED REPORT

DENEL

ABOUT THIS REPORT

REPORTING SCOPE AND BOUNDARY

This report provides information on Denel SOC Ltd's strategy and business model, financial information, operations and its ability to create value for the period 1 April 2016 to 31 March 2017. Financial information includes information regarding associated companies. All significant items are reported on a comparative basis.

ASSURANCE

Financial information

The financial information in this report has been prepared in accordance with International Financial Reporting Standards (IFRS) and has been independently audited by Denel's external auditors, SizweNtsalubaGobodo Incorporated. The report of the external auditors on our consolidated annual financial statements has been included on pages 110 to 114.

Non-financial information

The South African Companies Act no. 71 of 2008 (Companies Act), the King Code of Governance Principles and the King Report on Governance in South Africa 2009 (King III), Global Reporting Initiative (GRI) G4 guidelines and the International Integrated Reporting Council's (IIRC's) Integrated Reporting (IR) Framework have been considered in providing non-financial information.

Non-financial information presented in the report relates to Denel, its operating business entities, subsidiaries and associated companies, unless otherwise stated. Financial information includes information regarding associated companies. Most of the non-financial information presented in this integrated report was assured by a number of service providers through various processes, i.e. Broad-based black economic empowerment (B-BBEE) verification, International Standards Organisation (ISO) certification, organisational climate assessment, etc.

REPORT CONTENT

This report outlines the group's outlook and further aims to highlight opportunities and challenges, as well as planned actions to address these. The planned actions take into account business priorities, risks and recommendations made by stakeholders.

Denel is committed to sustainable development, and responds to the economic, social and natural environmental imperatives where it conducts business. These principles are embedded in the group's corporate strategy and values, and are reflected in the financial and economic decisions made by the group. Denel actively identifies material matters through engagements with internal and external stakeholders, and considers the group's risk management processes and feedback from sustainability indices. This process ensures that the group's corporate responsibility programmes remain relevant and meaningful to the group's stakeholders, and reflects the changing landscape of corporate responsibility.

APPROVAL OF THE REPORT

The Denel board, supported by the audit and risk committee, has taken an overall responsibility and accountability for this report. The board confirms that it has collectively reviewed the report's content and has concluded that the integrated report has been presented in accordance with the IR Framework. The board believes that this report is a balanced and appropriate presentation of the profile and performance of Denel. The board approved this report on 27 July 2017.

Lugisani Daniel Mantsha
Chairman

Mpho Kgomongoe
Acting Audit and Risk committee Chairperson

SPACE

CYBER

AIR

LAND

SEA

TWENTY 16/17

INTEGRATED REPORT

DENEL

CONTENTS

A list of abbreviations and acronyms is provided on pages 210 to 211.

PART 1

WHO WE ARE

VISION

The state-owned credible South African strategic partner for innovative defence, security and related technology solutions

VALUES

Performance	Integrity	Innovation	Caring	Accountability
We embrace operational excellence	We are honest, truthful and ethical	We create sustainable, innovative solutions	We care for people, customers, communities and the environment	We take responsibility for our actions

PERFORMANCE INDICATORS

Revenue
R8bn
2016 | R8.2bn

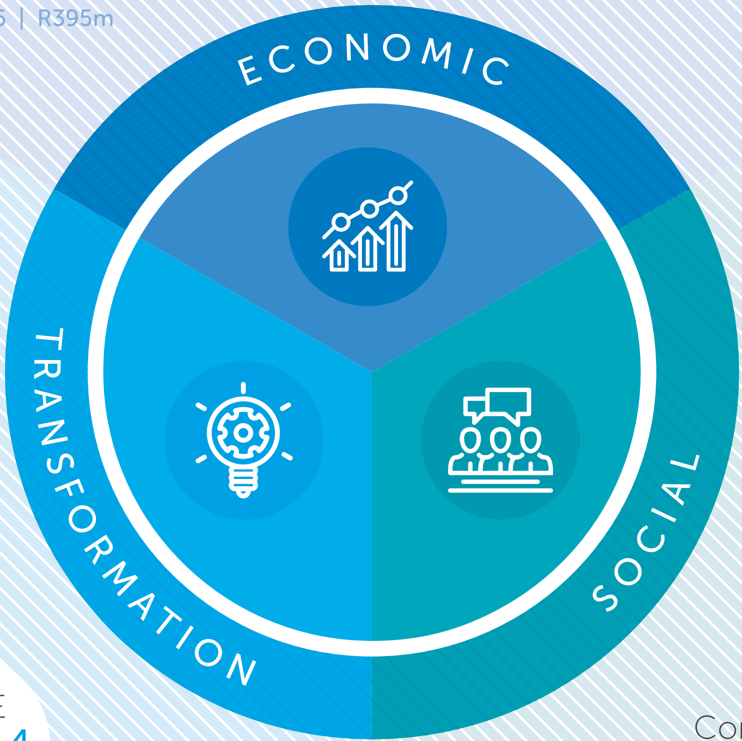
Cash
R2 021m
2016 | R2 003m

Borrowings
R3 265m
2016 | R3 717m

Debt to equity
1.2:1
2016 | 1.6:1

R&D
R609m
2016 | R550m

Net profit
R333m
2016 | R395m



Employee numbers
4 941
2016 | 5 114

B-BBEE
Level 4
2016 | Level 5

Corporate social investment
R7.2m
2016 | R7.6m

Female appointments
51%
2016 | 35%

Black-owned * spend
R816m
2016 | R873m

ACI * appointments
84%
2016 | 83%

Skills development
R68m
2016 | R65m

* *"Black"/ACI means African, Coloured or Indian persons as defined by the B-BBEE Act.*

WHO WE ARE

ONE DENEL. ONE VISION. ONE PURPOSE!

Denel is a state-owned commercially-driven company and a strategic partner for innovative defence, security, aerospace and related technology solutions. Denel provides turnkey solutions of defence equipment to its clients by designing, developing, integrating and supporting artillery, munitions, missiles, aerostructures, aircraft maintenance, unmanned aerial vehicle systems and optical payloads based on high-end technology.

Our business capabilities are as follows:

AEROSPACE

- Aircraft MRO
- Aircraft OEM and upgrade solutions
- Design and manufacture of aerostructure components
- Design and manufacture of air-to-air, air-to-surface and air defence missiles
- Design and manufacture of gas turbine engines for small and medium helicopters as well as turbo-shaft engines through Turbomeca Africa (Pty) Ltd [1]
- Manufacturer of aircraft bombs
- Manufacturer of ejection cartridges
- Conduct in-flight testing
- Manufacturer of precision-guided weapons
- Development and manufacture of satellites
- Manufacture of UAVS
- Manufacture of warheads
- Manufacturer of stabilised gimbals through Hensoldt Optronics (Pty) Ltd [1 and 2]

ARTILLERY

- Design and manufacture of:
  - » 105mm LEO guns
  - » 155mm G5 towed gun-howitsers
  - » 155 G6 self-propelled gun-howitsers
  - » Propellant charges
  - » Laser rangefinders

INFANTRY

- Design, manufacture and support of armoured combat and other vehicles
- Land systems equipment and systems integrator
- Manufacture of ammunition, machine guns, anti-materiel rifles and laser rangefinders
- Design and manufacture of automatic grenade launchers
- Design and manufacture of vehicle turrets
- Design and manufacture of surface-to-air missiles
- Design and manufacture of active missile protection, air defence systems and anti-armour missiles

NAVAL

- Design and manufacture of:
  - » 20mm guns
  - » Ammunition
  - » DPS-35 guns
  - » Periscope through Hensoldt Optronics (Pty) Ltd [1 and 2]
  - » Umkhonto missiles

SECURITY AND BORDER CONTROL

- Design and manufacture of:
  - » Ammunition
  - » Light weapons
  - » MEDDS
  - » Demining
  - » Seeker UAVS (200 and 400 variants)
  - » Surveillance equipment
  - » Risk control and police patrol vehicles

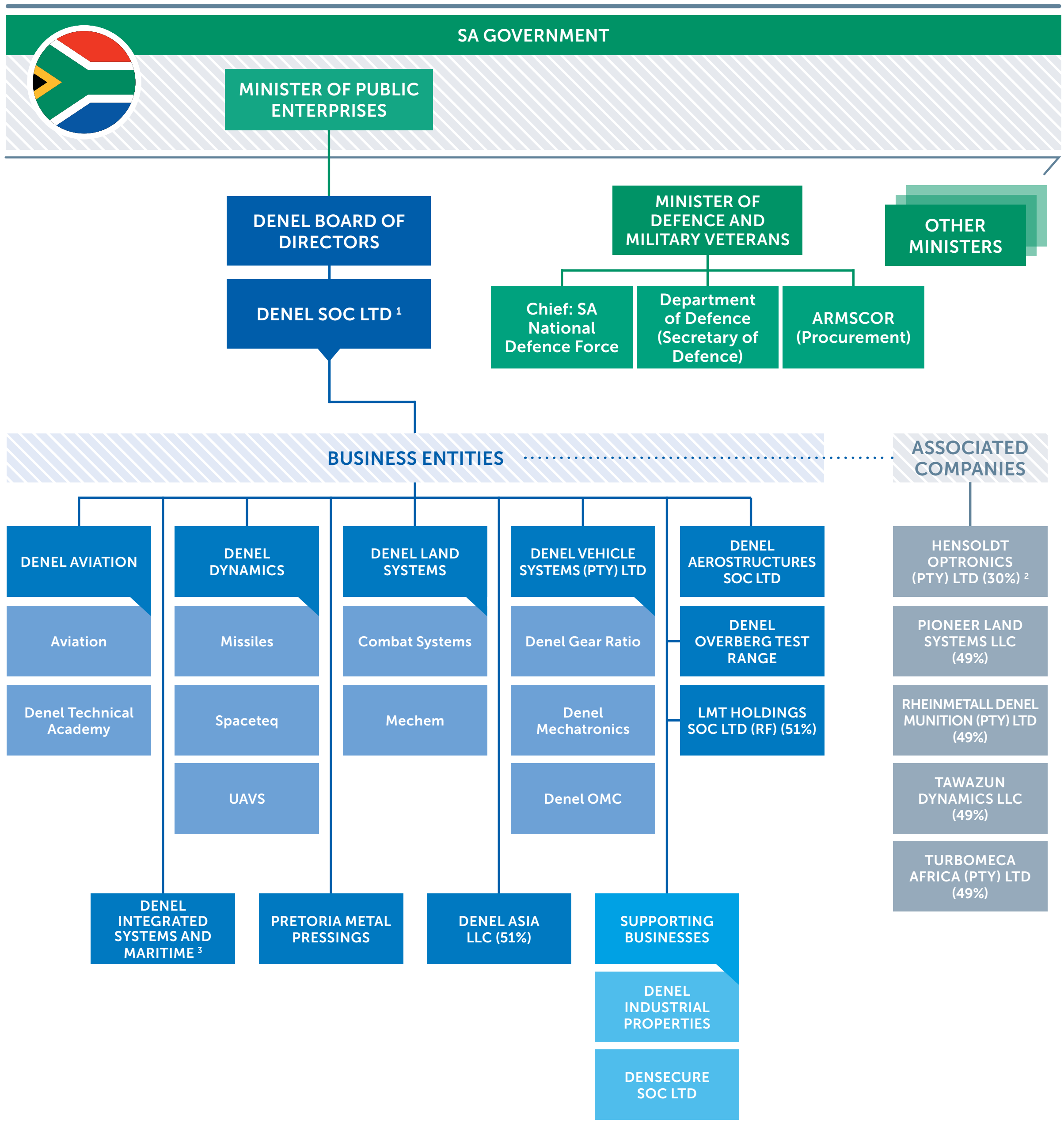
TRAINING AND OTHER

- Artisan qualification
- Commercial brass strip
- Energetic material
- Engineering training
- Rocket motors through Rheinmetall Denel Munition (Pty) Ltd [1]
- Humanitarian services including demining
- Mine clearance training
- Manufacturing of mining drill bits

A list of abbreviations and acronyms is provided on pages 210 to 211.

1. *Associated companies. Refer page 09.*
2. *Refer footnote 2, page 201.*

ORGANISATIONAL STRUCTURE

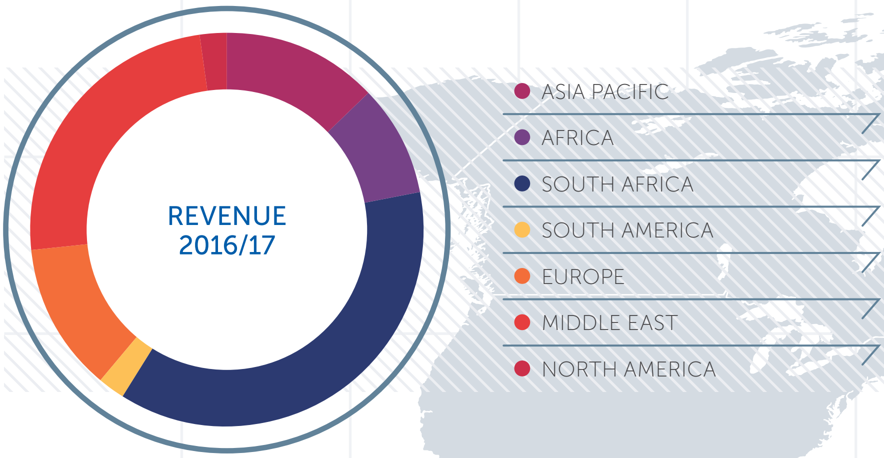


STRATEGIC EQUITY PARTNERSHIPS

HENSOLDT	INTERNATIONAL GOLDEN GROUP	RHEINMETALL DEFENCE	PAMODZI	SAFRAN	TAWAZUN	VR LASER ASIA LTD

1. Denel's shareholding is 100%, unless stated otherwise.
2. Refer footnote 2, page 201.
3. Denel Integrated Systems and Maritime (Denel ISM), has been split into two business entities: Denel Maritime and Denel Sovereign Security Solutions (Denel S3) as of 1 July 2017.

OUR GLOBAL PRESENCE



1. Algeria
2. Brazil
3. Kenya
4. Malaysia
5. Mozambique
6. Oman
7. Pakistan
8. South Africa
9. Turkey
10. United Arab Emirates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CHAIRMAN'S REPORT

Denel is a valuable national asset that contributes to the sovereignty of South Africa and the safety of its citizens – but also creates considerable long-term value for our shareholder, the state.

We are keenly aware of the responsibilities incumbent on public sector companies such as Denel to improve our outcomes with the same or reduced resources and to report back to our stakeholders on how the organisation creates value.

As a state-owned company in the defence and high-technology environment Denel is committed to the government's vision to create a developmental state. Thus, our responsibilities and mandate stretch beyond the mere requirements to ensure good returns on investment, but also to contribute to the economic transformation of South Africa and addressing the challenges of job creation, skills development and a reduction in inequalities in society.

As an enterprise we can again report on a very successful year in which we focused on our objectives to achieve financial sustainability, improve productivity and increase operational efficiencies. Moreover, we conclude the year with a healthy long-term order book which positions Denel well for the future.

GOVERNANCE AND LEADERSHIP

The board is committed to provide strategic direction to the organisation according to the highest standards of corporate governance. We appreciate the support we receive from our stakeholder, the Department of Public Enterprises, as well as the various ministries, departments and agencies who work with Denel to meet its mandate and create long-term value for the country.

We have concluded the process in which we parted ways with the former Group Chief Executive Officer (GCEO) and other senior officials. That chapter belongs to our past. We are firmly focused on the future to grow the business of Denel, expand the range of our products, move into new markets with new products and provide our primary client, the South African National Defence Force, with the equipment, services and systems that will enable it to perform its missions.

The appointment of a new GCEO is imminent. We want to thank the Acting GCEO, Mr Zwelakhe Ntshepe for his leadership and unstinting devotion to Denel over many years and in many capacities. We also welcome the appointment of a new Group Chief Financial Officer, Mr Odwa Mhlwana and a new Group Company Secretary, Ms Vuyokazi Xaxa.

The board and its committees met on a regular basis throughout the year and I want to thank my fellow board members for their constructive contributions.

Denel's long-term rating is closely linked to South Africa's sovereign rating. We are pleased to report that Fitch Ratings has affirmed both Denel's National Long-Term Rating and the National Short-Term Rating, despite its decision to downgrade the sovereign status. This is testimony to the confidence that our business partners and stakeholders – both local and international – have in the future sustainability of Denel and in our capacity to deliver on key contracts and partnerships.

We are proud of the results we have achieved, especially the growth in export revenue despite the negative impacts of the deteriorating exchange rates. Our sustained financial recovery will depend on our ability to increase market share, manage cost and achieving our revenue targets, as well as the continued support and guarantees we receive from the sole shareholder.

The board is addressing some of the key challenges faced by Denel, most notably in the critical areas of funding and contract delays resulting in liquidity problems. Some of these issues have also impacted on our supply chains. We are confident that the executive management team, with the help of the board and support from the shareholder will be able to resolve these issues in the near future.

BUSINESS GROWTH

The results underline the urgency of the board's approach to pursue new market opportunities, especially in geographic regions that have the potential for future growth. We continue to build on our strong research and development partnerships in the Middle East and with countries in the BRICS alliance.

Denel still sees massive potential for growth in the Asia-Pacific region which will soon command more than half of global defence procurement outside of the United States. At a time when defence budgets are contracting in many countries, Asia-Pacific is expanding and opportunities are opening up for Denel to find new markets for our world-class products, especially in the fields of artillery, armoured vehicles, missiles and unmanned aerial vehicles. The establishment of Denel Asia as a joint venture in Hong Kong was done to create a stronger foothold in this region. We are currently looking at various options to address this market.

We are proud of the results we have achieved, especially the growth in export revenue, despite the negative impacts of the deteriorating exchange rates. Our sustained financial recovery will depend on our ability to increase market share, manage cost and achieving our revenue targets, as well as the continued support and guarantees we receive from government.

FUTURE DIRECTION

Denel will continue to build on its traditional strengths in landward defence, aviation and aerostructures, missile technology and munitions. The establishment of Denel Maritime has given us a strong presence in the maritime environment and we are well-placed to support government's objectives to expand the oceans economy through Operation Phakisa.

The Defence Review 2015 has defined Denel's role as a national security asset with the primary mandate to define, develop, manufacture and sustain such defence material that government prefers to source locally for security or economic reasons, as well as products that are not commercially viable propositions for the private industry.

Denel has the potential to provide South Africa with sovereign capabilities in a number of areas that are of vital strategic importance – most notably cybersecurity, command and control and electronic warfare. In the past year we have built a successful partnership with another state-owned entity, the CSIR, to develop platforms for maritime surveillance and situational awareness that adds value to the country's broader security framework.

Modern threats against the security of the country also include elements of violent and organised crime, illegal immigration, environmental insecurity and the poaching of our natural resources. In all of these fields Denel is developing sovereign capabilities that will improve South Africa's capacity to counter such threats. To strengthen cybersecurity we have established a Denel Tactical Cyber Command Centre (DTC^3) and we intend to increase our investments in research and development and strategic partnerships with other agencies and entities.

We are excited by government's stated intention to grow the South African defence industry. The launch of the National Defence Industry Council by the Minister of Defence and Military Veterans was a pivotal event and is sustained by a clear strategy for the future trajectory of the broader defence industry in which Denel will play a leading role.

Similarly, government's implementation of the Industrial Policy Action Plan (IPAP) will open new opportunities for Denel. The strategy notes that future defence procurement programmes will contribute to the growth of the country's advanced manufacturing sector and have a knock-on effect on employment. This will accelerate South Africa's move away from being heavily dependent on commodity exports to having a diversified knowledge economy.

The defence industry is well-suited to support the growth of small, medium and micro-enterprises and Denel remains committed to bring sectors that were excluded in the past – most notably black-owned businesses and enterprises owned by women, the youth, the disabled and military veterans – into our supply chains.

CONTRIBUTION TO THE DEVELOPMENTAL STATE

South Africa's national security is centered on its political and economic independence and its ability to protect the democratic system and the freedoms enjoyed by its citizens. As a developmental state these freedoms are inextricably linked to our ability to address challenges relating to poverty, unemployment and inequality.

During the past year Denel has taken a concerted decision to increase its spending on socio-economic development, especially through the educational initiatives we support. Our Schools Outreach Programme provides extra tuition in mathematics and physical science to learners in six provinces and we are extending our partnerships with education departments to sponsor educational camps and teacher support programmes.

APPRECIATION

On behalf of the board I want to extend my appreciation to our stakeholders, partners and suppliers for their continued support to Denel during the past financial year. Your support and trust will enable Denel to grow its business in the years to come and add value to the South African economy and society.

We value the continued interest shown in Denel by the Minister of Public Enterprises, Lynne Brown, Deputy Minister Ben Martins, Director General Mogokare Richard Seleke and officials of the department. The Minister of Defence and Military Veterans, Nosiviwe Mapisa-Nqakula and her team, have been a champion of the defence industry in general. We further wish to thank the chairman of ARMSCOR, Vice Admiral (Rtd) RJ Mudimu and his board for their continued support. As an organisation Denel interacts with government departments and agencies on a regular basis and I want to thank key role players.

Through the year we have had constructive engagements with Parliament and I want to thank the chairpersons and members of the Portfolio Committee on Public Enterprises and the Select Committee on Communications and Public Enterprises for their oversight role and support to Denel.

Finally, I wish to extend my gratitude to all the employees of Denel who have contributed to building a successful organisation and who remain committed to its future.

Lugisani Daniel Mantsha
Chairman of the Denel board

PART

2

CREATING VALUE FOR OUR STAKEHOLDERS

BUSINESS MODEL

CAPITAL INPUTS

INTELLECTUAL
- Internally developed systems
- R&D
- Unique customer solutions

HUMAN
- Effective and responsible leadership
- Developing skills
- Transformed skills workforce
- Retaining key talent

FINANCIAL
- Profitability
- Order book quality and growth
- Source appropriate funding
- Access to funding
- Cash flow efficiency and working capital management

NATURAL
- Energy needs for manufacturing

SOCIAL AND STAKEHOLDER ENGAGEMENTS
Effective engagements to:
- Employees and trade unions
- Shareholder and funders
- Customers and suppliers
- Government and regulators

ACTIVITIES

CONCEPTUALIS-ATION	RESEARCH AND DEVELOPMENT	BIDDING AND CONTRACTING	DESIGN AND DEVELOPMENT	MANUFACTURING, AND INTEGRATION	SERVICES,SUPPORT AND UPGRADE
Identifying customer needs	Innovative technological advancements	Scoping, planning and contracting	Programme management and system engineering	Manufacturing, maintenance, assembling, integration and testing	Delivery, product support and warranty

OUTPUTS

PRODUCTS | SERVICES | SOLUTIONS

OUTCOMES

Innovation and positive contribution to **technology advancements**

R2.3bn paid remuneration

Skills development R68m

Level 4 B-BBEE

R&D spend R609m

4 941 employees

Responsible leadership

Corporate social investment R7.2m

Sustained strategic capabilities

R8bn revenue

Cash R2 021m

8% EBIT

330 Learnerships, **sponsorships** and other **training**

R333m net profit

Order pipeline <R40bn

Positive relationship with **organised labour**

EXTERNAL ENVIRONMENT
- Global demand for defence and security products
- Shareholder's Compact demands







STAKEHOLDER ENGAGEMENT

As a company wholly owned by the South African government, Denel reports to the Minister of Public Enterprises as the shareholder representative, with its stakeholders reflecting both the developmental and commercial mandate of the group. Denel contributes to industrial development towards the building of a dynamic defence and related industry cluster.

The group is a catalyst for advanced manufacturing in the country. Equally important, Denel contributes to the country's socio-economic objectives, which include skills development and the transformation of the industry starting at school level through tertiary education to on-the-job training.

Therefore, Denel's stakeholder engagement programme covers the entire spectrum of stakeholder groups, and is premised on building, strengthening and maintaining strong mutually beneficial relationships with them all, including customers and communities. Our stakeholder engagement plan is a critical component of the group's Communication and Public Affairs programme with the key focus area deriving from the integration of all of the entities' stakeholders.

A detailed mapping process was undertaken to identify and prioritise engagement levels with each of the group's stakeholders. That process led to the integrated stakeholder engagement plan that guides our interactions with stakeholders and is centrally coordinated between the Communication and Public Affairs and Business Development departments, as well as and the various business entities. In this manner, Denel aims to engage with all stakeholders through appropriate engagement platforms.

Formal engagements through meetings, roadshows and forums with stakeholders are conducted on a regular basis. Futhermore Denel uses sponsorship opportunities to achieve the following specific objectives:

- Interact closely with political and industry stakeholders including the head of state, premiers, ministers, executive mayors, and senior government officials and other key decision-makers;
- Highlight the Denel brand as driving good corporate governance in SA; and
- Strategic engagements with new and existing customers.

Given the high-level interaction envisaged for such opportunities, most of these events were attended by the chairman of the Denel board, the Acting GCEO and members of the exco. Although informal in nature, however, some of the most important issues for the business would get deliberated and sometimes resolved at these events. GCEO roadshows to employees and frequent interaction with clients, suppliers and other social partners were also prioritised.

KEY STAKEHOLDERS

SHAREHOLDER, PARLIAMENT AND GOVERNMENT DEPARTMENTS

Ensures fulfilment of dual mandate of commercial performance and national socio-economic imperatives

CLIENTS AND CUSTOMERS

Allow Denel to be innovative and provide technologically advanced solutions

EMPLOYEES AND ORGANISED LABOUR

Provide skills to deliver on strategy and facilitate debate on issues facing the business and employees

FINANCIAL INSTITUTIONS AND INVESTORS

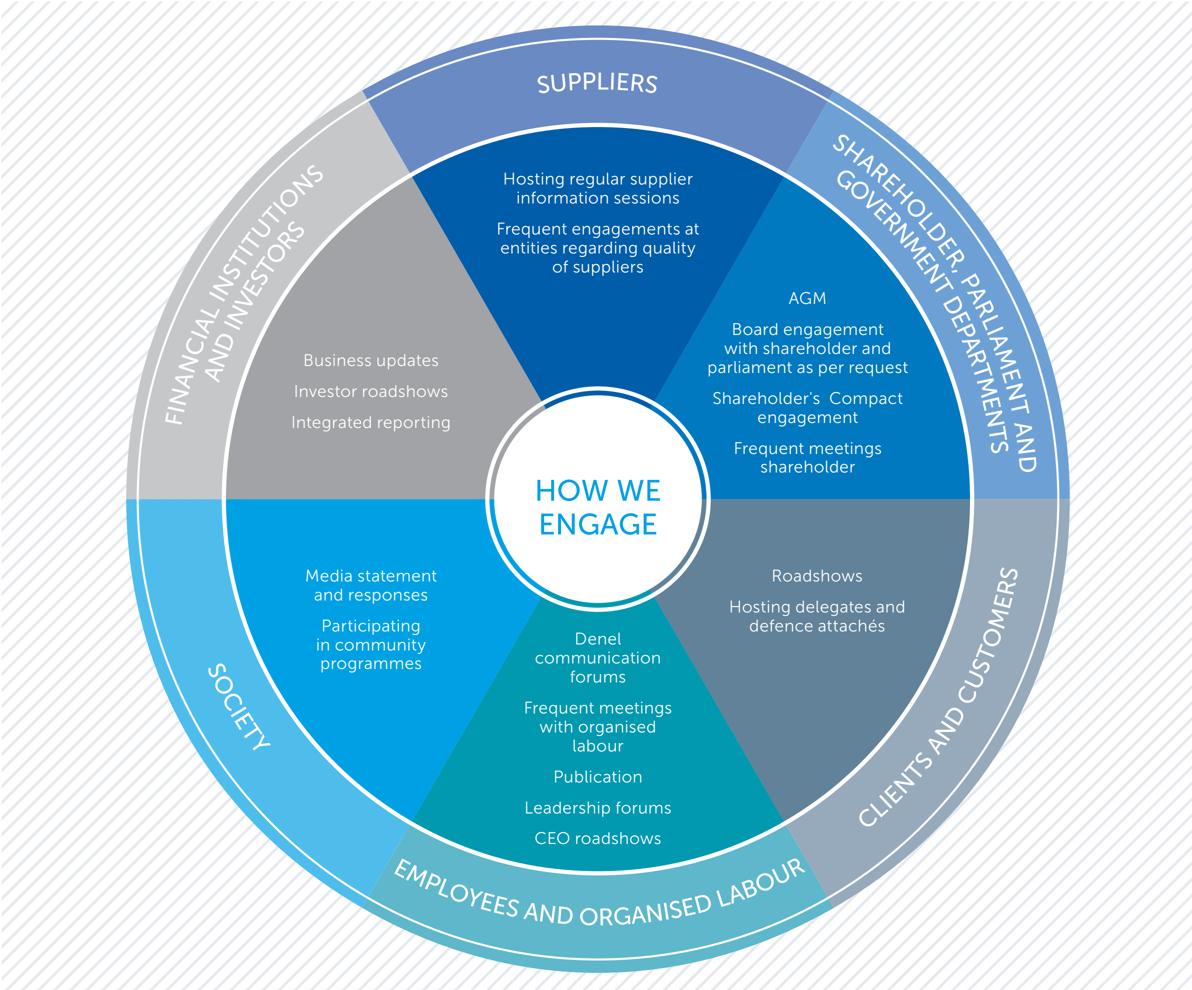
Provide financial assistance to enable sustainable growth

SOCIETY

Holds Denel accountable to remain a credible corporate citizen

SUPPLIERS

Supply quality material and services



Among the key engagements that have taken place within the group, we can highlight the following:

SHAREHOLDER, PARLIAMENT AND GOVERNMENT DEPARTMENTS
DOD&MV, DPE, DIRCO, dti, NATIONAL TREASURY, PORTFOLIO COMMITTEE

KEY ISSUES	OUTCOMES
» Review of performance measures as detailed in the Shareholder's Compact (refer page 80); » Government support for export opportunities and industry participation; » Transformation and advances in EE, B-BBEE, diversity management and skills and enterprise development; and » Engagements on the Denel Asia joint venture.	» Received oversight support from DPE on implementing in key areas such as: • Contract management • Socio-economic imperatives • Corporate governance » Support for marketing activities » Ongoing oversight support from Parliamentary portfolio committees and Select Committee » Positioning Denel as a global leader in the design, development and manufacturing of top quality products, solutions and services » Visible contributions by Denel towards national priorities » Ongoing engagements regarding Denel Asia joint venture

CLIENTS AND CUSTOMERS
AMD, ARMSCOR, DOD&MV, INTERNATIONAL CLIENTS, LOCAL COMMERCIAL CLIENTS, SANDF, SAPS

KEY ISSUES	OUTCOMES
» Denel as a custodian of core strategic and sovereign capabilities; » Elevate product ranges, services, solutions and new capabilities; » Performance and programme delivery; and » Research and development.	» Stronger order pipeline in excess of R40m » Maintain all strategic capabilities for the SANDF » R&D investment R609m » Export revenue improved by 6% » Promote marketing activities » Better understanding of Denel values, business objectives and challenges

EMPLOYEES AND ORGANISED LABOUR

KEY ISSUES	OUTCOMES
» Fostering integration across the group; » Living the Denel values (refer page 06) and strategic objectives (refer page 53); » Continuation of sound labour relations; and » Delayed variable pay remuneration payment.	» Embrace the Denel group brand » Continued engagement around negative media coverage » Synchronised communication activities among the entities » Placed employees through various development programmes » Continuous engagements and payment of variable pay remuneration » Unlocked employee volunteer programmes

SOCIETY

KEY ISSUES	OUTCOMES
» Improve the lives of communities in which we operate; » Contribution to national government imperatives; » Acknowledge Denel as a strategic national asset; and » Position Denel as employer of choice.	» Spent R7.2m to improve Science, Technology, Engineering and Mathematics (STEM) education » Provided 421 bursaries and learnerships » Improved understanding of Denel to national and international audiences » Positioned itself as a responsible corporate citizen committed to the advancement of rural community development » Extended Schools Outreach Programme to include the Eastern Cape, Limpopo and KwaZulu-Natal » To encourage STEM as a career of choice, Denel showcased its young innovators to society through various media platforms

FINANCIAL INSTITUTIONS AND INVESTORS

KEY ISSUES	OUTCOMES
» Financial performance and prospects; » Transparency of general information about key business developments; and » Business focus and strategy updates.	» Cognisance of decisions taken by management » Improved understanding of Denel's business model » Continued financial assistance

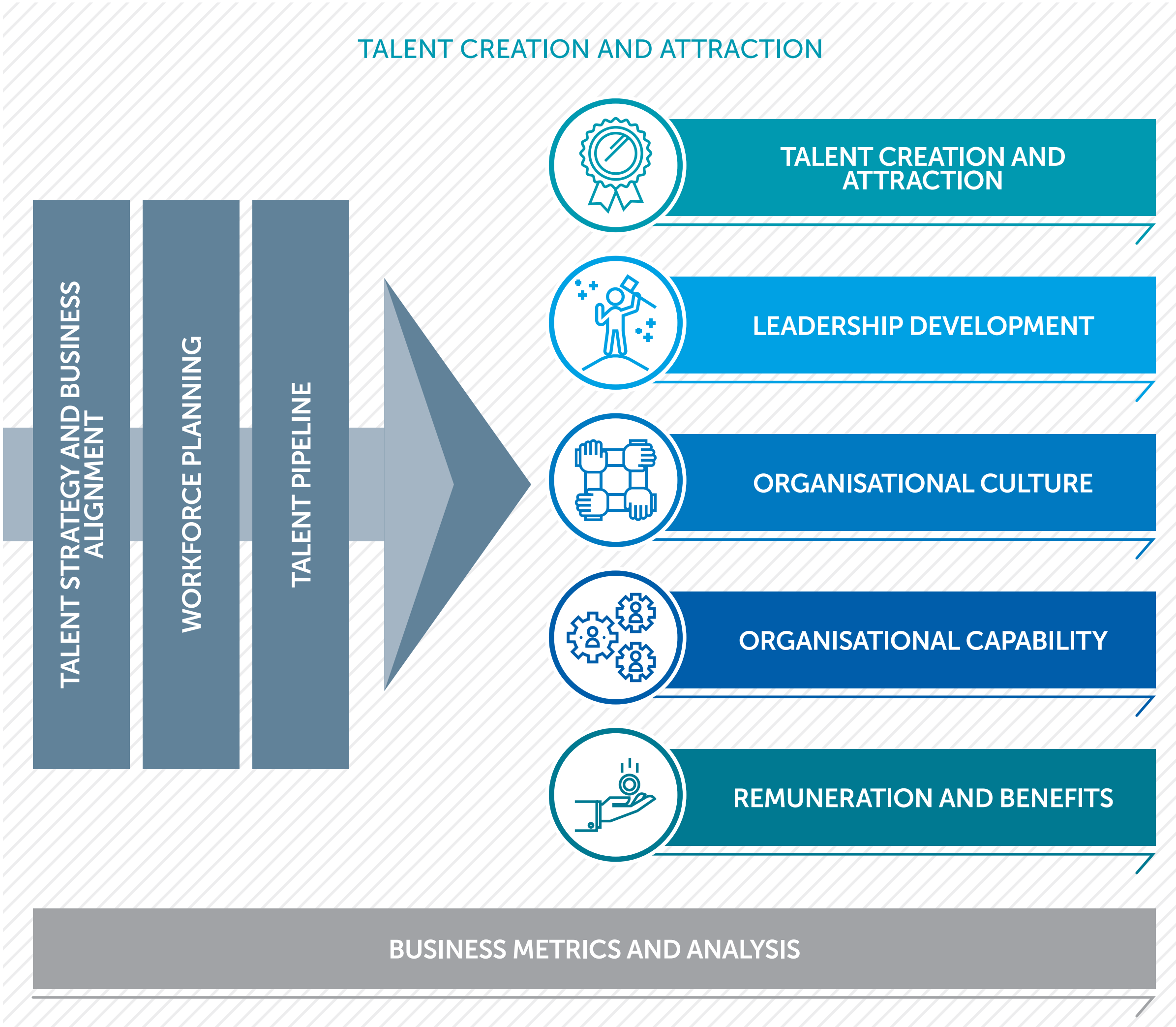
SUPPLIERS

KEY ISSUES	OUTCOMES
» Meet B-BBEE procurement targets; » Ensure consistent supply of quality materials; » Improvement on enterprise development; » Transparency of general information about key business developments; and » Payment of suppliers.	» Achieved level 4 B-BBEE rating » Focused on identifying further B-BBEE suppliers and enterprise development » Improved understanding of Denel's business » Continuous engagements with suppliers regarding payment terms

HUMAN CAPITAL

Globally companies place great emphasis on talent, engagement and retention. Numerous studies are conducted annually to determine the oracle of ever-changing employee expectations. Evidence clearly outlines that there is an ever-growing gap in expectations between millennials and other generations within the workforce. Employers are often not attuned to the vast implications for the workplace. Literature also suggests that there are common requirements for employees which, if addressed appropriately, can lead to an engaged, dynamic workforce. Denel's talent management strategy is aligned to the business strategy. This ensures that workforce planning guides the talent pipeline. These strategies are underpinned by business metrics and analysis.

At Denel these talent dimensions are managed as follows:



TALENT CREATION AND ATTRACTION

Denel invests heavily in skills development amongst the youth. Our programme commences at secondary school level as outlined in our social capital section, pages 38 to 40, with these learners then accessing bursaries at Denel after matriculation. In order to create a healthy skills pipeline Denel sponsored tertiary education for 421 learners in various technical fields. This pipeline is shaped towards increasing diversity with 52% of bursary holders being female.

BURSARIES

The purpose of the bursary scheme is to have a readily available pipeline of qualified engineering students who (post-matric) can apply for engineering degrees in the following disciplines:

- Electronic
- Mechanical
- Industrial
- Software/Computer
- Mechatronic

Bursaries cover tuition; accommodation; books; a computer allowance, as well as a stipend. Denel's hands-on approach ensures bursars are fully supported so that they obtain their qualifications and join the group. During the 2016/17 financial year, Denel sponsored 85 bursary students in various years of study towards obtaining degrees in the technical disciplines mentioned above.

ARTISAN TRAINING

The Denel Technical Academy (DTA) remains an artisan training "hub" that develops skills, particularly for the aerospace and engineering industry. DTA has been purposely structured and resourced to deliver technical training, and is not currently geared to deliver other skills development programs e.g. management training. The academy creates a foundation for future employability of young apprentices. DTA also offers short courses for qualified artisans as part of their continuous professional development.

INTERNSHIPS

Graduates, mostly from technical disciplines, are employed on internship programmes by various entities. This allows the graduates to acquire critical workplace skills, whilst simultaneously affording entities the opportunity to assess the graduates' employability, although they are not bound to employ these graduates on a full-time basis.

LEARNERSHIPS

Entities have embarked on learnership programmes in various fields to enhance the EE profile. Opportunities are targeted for ACI females and where possible, with disabilities. Should they excel during the learnership period, permanent employment is offered.

VACATION WORK

Denel offers vacation work opportunities for engineering students who are required to gain workplace experience in order to complete their qualification.

PERFORMANCE OVERVIEW

Skills development of scarce and critical skills particularly in the ACI			
Description	**Target**	**Achievement**	**2016/17 Outcomes and 2017/18 Outlook**
Total number of engineering trainees (bursaries and internships)	50	85	Whilst target is not met on DTA first-year apprentices 2017, Denel has sponsored 330 youth in various technical fields, thereby making significant contributions towards the development of critical and scarce engineering skills for the country.
Total number artisan trainees	100	177	
Total number of DTA artisan (enrolments during the year Denel sponsored only)	85	66	

LEADERSHIP DEVELOPMENT

DENEL TRAILBLAZERS

Leadership effectiveness remains one of the key success factors in any organisation. Leader and leadership development is a critical pillar in the human capital trajectory. Leadership development is critical to ensuring that Denel's leaders are adequately equipped to lead change within an ever-changing business landscape. Within this transforming context, leadership development therefore needs to focus on the development of broad skills and competencies, including flexibility, team building, change management, self-awareness and interpersonal skills.

Leadership competencies have been determined based on the different levels of work. It starts with junior management where the focus is on managing the present through middle and senior management where the focus is on planning the future and ultimately to executive level where the focus is on shaping the future.

Leaders within the organisation undergo a battery of psychometric assessments to determine strengths and developmental areas. Development comprises a blended approach as determined by the individual's results. The Denel leadership and management development programme does not only entail formal training courses, but various exposures, including coaching and mentoring. All persons designated as management including those in supervisory roles qualify to participate in leadership and management development programmes. Priority on leadership and management development programmes is given to women, youth and people with disabilities. Denel has re-aligned its learning and development strategy and processes to encourage development and create a learning organisation. The learning and development strategy ensures that training interventions are aligned and ultimately supports the Corporate strategy. Special emphasis is placed on the growth and development of younger employees and historically disadvantaged people.

A formal leadership development programme called "The Trailblazers" is executed by Henley Business School. The programme has four levels, from Junior to Executive programmes. Delegates are from all entities across the group and as part of the learning process delegates have to complete action learning projects which find solutions to actual business challenges. Groups are measured on scalability of these solutions to ensure return on investment for the organisation.

During the year under review 84 (2015/16: 81) delegates participated in the programme.

EXECUTIVE COACHING

Denel has established executive coaching relationships for executives and managers as part of the leadership and management development programmes. The choice of coaching initiatives are informed by developmental needs of managers and executives. The group identifies coaching programmes to ensure alignment and standardisation of training.

ORGANISATIONAL CULTURE

Values ensure the strength of Denel's culture, by focusing employees on the best ways to serve the organisation's needs. Values are particularly important in facilitating the effective transformation of Denel in that they promote a common behavioural philosophy which results in effective workplace relationships.

Annually the GCEO hosts a gala dinner for employees and their spouses who have been nominated to receive the prestigious Group CEO Awards. Entities nominate their best contenders per value who are then considered and one winner per values category is selected.

The third Annual Group CEO Awards comprise eight categories which are based on the iconic Denel products. These are as follows:

MUNITIONS PERFORMANCE AWARD

This award is given to an employee or team that embraces operational excellence and has demonstrated this by working efficiently, effectively and with high quality standards.

UMKHONTO INTEGRITY AWARD

This award is given to an employee or team that has exhibited honesty, truthfulness and ethical conduct by doing the right thing even when no-one is watching.

AIRBUS INNOVATION AWARD

This award is given to an employee or team that has created a sustainable innovative solution that advances business objectives.

CASSPIR CARING AWARD

This award is given to an employee or team that has demonstrated caring for fellow employees, customers, communities or the environment.

Zwelakhe Ntshepe, Acting Group Chief Executive Officer

G6 ACCOUNTABILITY AWARD

This award is given to an employee or team that has demonstrated an exceptional sense of responsibility for their actions, and behaved in a manner that showed they regard Denel as if it were their own company.

RG31 INCLUSIVITY AWARD

The award is given to an employee or team for promoting and championing inclusivity by acknowledging the value which all employees bring to the organisation, regardless of their age, race, culture and gender, making Denel the best company to work for.

BADGER TRANSFORMATION AWARD

The award is given to a division for demonstrating outstanding contribution and impact to the group's transformation agenda as it relates to climate improvement (values; talent management; inclusivity and leadership development) and B-BBEE score (management control; skills development; enterprise and supplier development; as well as socio-economic development).

ROOIVALK GCEO EXCELLENCE AWARD

This award is given to an employee or team that has excelled in terms of performance, by executing tasks with passion, striving for zero-defect and getting things right the first time.

AND THE WINNERS WERE:

MUNITIONS PERFORMANCE AWARD

Kenya Puma 406 Servicing Team, Denel Aviation

The team was tasked to carry out a 4P2 servicing for the Kenyan Air Force in order to save on costs and ensure that the target date was brought forward as per customer request. This was ground-breaking as it would be the first time that servicing of this scale had to be performed at the client's base and as a joint technical effort with the customer.

Phaladi Petje, CEO PMP; Kenny Molepo, Gerson Lambani, Forward Gumbanjera and Dean Louw, award winners and Zwelakhe Ntshepe, Acting GCEO.

UMKHONTO INTEGRITY AWARD

Shipment Team, Denel Dynamics

The Shipment Team ensures at all times that shipping related documentation is handled with the utmost sensitivity, thus ensuring validity and coherence with the rules and regulations for local and international arms control authorities. Their integrity goes above and beyond what is required of them to ensure that Denel Dynamics remains within the set parameters.

Tsepo Monaheng, CEO Denel Dynamics; Cindy Khutlisi and Riette van Biljon, award winners and Zwelakhe Ntshepe, Acting GCEO.

AIRBUS INNOVATION AWARD

DMG-5 Team, Denel Land Systems

The DMG-5 Team responded to the need from the market for a lighter general-purpose machine gun. The DMG-5 Team made various design changes to the SS77, resulting in the reduction in mass from 10.3kg to 8.4kg, making this the lightest 7.62x51mm machine gun currently available on the market. This innovative initiative by the three young engineers has gained international recognition.

Marumo Talane, Phindile Mashaba and Dakalo Nekhumbe, awards winners and Zwelakhe Ntshepe, Acting GCEO.

CASSPIR CARING AWARD

PMP Employees Team

On their way to work, the team recognised a colleague who had been involved in an accident and immediately stopped to assist. They called for help from PMP when private medical assistance took time to get to the scene. Some of the team members are PMP first-aiders and put their skills to action by keeping the colleague awake and warm while awaiting medical help.

Left to right: Resemate Mathye, Ezra Ryce, Jenny Horing, Berta Fourie, Desiree Fynn, Jurie Labuschagne, Kehwile Rammaru, Zwelake Ntshepe (Acting GCEO), Daphne Haas, John Ross Petrie, Thulani Mahlinza.

G6 ACCOUNTABILITY AWARD

Takalani Mandiwana, Denel Aviation

Takalani was sent to the war-torn Goma region of the Democratic Republic of the Congo (DRC) to service the Rooivalk combat helicopter that the SAAF was using in the fight against rebel forces. He worked with limited resources while under pressure to get the aircraft back in the air to resume military missions. Takalani went beyond the call of duty by delivering the required technical support services to the best of his ability in trying circumstances. His dedication strengthened relations with the client who was unable to get the aircraft to South Africa for maintenance.

Stephan Burger, CEO Denel Land Systems; Takalani Mandiwana, award winner and Zwelakhe Ntshepe, Acting GCEO.

RG31 INCLUSIVITY AWARD

Software Development Team, Denel Overberg Test Range

The team has demonstrated that by working collaboratively the objectives of the section can be achieved in an environment where people of all backgrounds, individualities, cultures, and perspectives can feel valued in achieving the goals of the organisation. This has made success at the workplace possible through inclusivity on various technical fronts through innovatively developing software applications and test client interfaces.

Team members that remained after retirements, promotions and termination of contract posts have embraced the transformation ideals of the Denel group through participation in the recruitment process of young software developers. This has resulted in a diverse working group that is currently in place at Denel Overberg Test Range. Mentorship and training of young and new team members continues through the different activities undertaken by the team, which has ensured the smooth running of the various services offered by the Software Development section.

Vuyelwa Qinga, Group Executive Communication and Public Affairs; Henry van Wyk representing the team and Zwelakhe Ntshepe, Acting GCEO.

BADGER TRANSFORMATION AWARD

Denel Industrial Properties

All entities were nominated for this award and Denel Industrial Properties was the entity that ultimately received the award.

Natasha Davies, Group Executive HR and Transformation; Rentia Geldenhuys, General Manager Industrial Properties and Zwelakhe Ntshepe, Acting GCEO

Marumo Talane, Phindile Mashaba and Dakalo Nekhumbe, award winners and Zwelakhe Ntshepe, Acting GCEO.

ROOIVALK GCEO EXCELLENCE AWARD

DMG-5 TEAM, Denel Land Systems

The DMG-5 Team responded to the need from the market for a lighter general-purpose machine gun. The DMG-5 Team made various design changes to the SS77, resulting in the reduction in mass from 10.3kg to 8.4kg, making this the lightest 7.62x51mm machine gun currently available on the market. This innovative initiative by the three young engineers has gained international recognition.

ORGANISATIONAL CAPABILITY

This area refers to your organisation's ability to accomplish its work processes through the knowledge, skills, abilities, and competencies of its people. This ensures that current and future skills requirements are identified and developed. Denel provides 3% of its personell costs for learning and development for the entire workforce, however, there is targeted spending on employees with critical and core skills, young employees with potential, as well as on black people. During the period under review, Denel spent R68m (2015/16: R65m) on learning and development for employees.

Each employee has a personal development plan to target learning interventions. Many of the Denel entities require advanced technical skills to conduct their business. Accordingly, processes are required to ensure that highly skilled technical employees stays abreast of advances in technology. Bursaries are also offered to employees to assist their long-term development and enable them to make a stronger contribution in their current and future roles.

The following key transformation measures exist within the group:

MENTORSHIP

Each Denel entity has a mentorship plan that is constantly tracked and evaluated by the entity Training and Transformation committee. These programmes assist in the identification of future technical and managerial leaders and on the development of technical competence and productivity. All mentee and mentor programmes have pre-determined targets and goals that must continuously be assessed as part of the group's performance assessments.

WORKPLACE SKILLS PLANS

Entities, as part of their skills development processes, develop workplace skills plans which deal with training that is core or statutory for that specific business. Entities are registered with their respective SETAs, which ensures that training obligations are managed appropriately and aligned to the SETA requirements.

SUCCESSION PLANNING

Denel has acknowledged that succession planning is a business imperative to ensure survival, growth and profitability of a company. The objective of succession planning is to create a pool of quality successors for critical and strategic positions to serve a purpose of immediate availability when a position becomes vacant, eliminating a strategic void and to purposefully develop individuals in preparation for future strategic positions. All the positions earmarked to be filled through succession plan are pre-identified and approved by the relevant authority. Minimum requirements for the positions are pre-determined before succession planning candidates are identified In the event where there is a shortfall on minimum requirements, the identified candidate must be given support to achieve the deficit.

CAREER PATHING

Career paths have been developed to encourage younger employees to choose the paths that would best contribute to the success of the group and best suits the individual. There are both technical and management career paths available. All employees considered as management and specialised or technical paths follow pre-defined career paths, which are detailed in their Personal Development Plans.

Career pathing is a key contributor to the implementation of the succession plan across the group.

TRAINING AND DEVELOPMENT INITIATIVES

Training and development is a key lever in motivating and retaining skilled employees within Denel. The group has developed and implemented programmes to reach out to, up-skill and retain young technical skills within the group. The training and development programmes also serve as a pool from which Denel recruits its future employees. Entry level jobs are preferably offered first to Denel bursary holders, interns and those on its learnership programme. Denel requires advanced technical skills to conduct its business. Accordingly, processes are required to ensure that highly skilled technical employees stays abreast of advances in technology. The two projects listed below illustrate how younger employees are given the opportunity to design and develop new products.

PROJECT SARA

The SARA (Small African Regional Aircraft) project is based on collaboration between young engineers at Denel Aeronautics and academics along with post-graduate students at local universities. SARA is an initiative to develop a passenger aircraft to serve regional destinations that are not served by existing airlines. The programme is creating new horizons for young engineers such as Preshni Govender, Puseletso Matlala and Naadira Hassim, as well as artisans entering the industry.

DMG-5

The challenge given to three young engineers at the Engineering Academy at DLS was to redesign an infantry soldier's most trusted ally, the machine gun, making it lighter and easier to handle without compromising its firepower and reliability. Three young mechanical engineering graduates, Dakalo Nekhumbe, Phindile Mashaba and Marumo Talane, a trained electro-mechanical engineer, took to the challenge with enthusiastic "out-of-the-box" thinking. The result was the development of a new generation light-weight machine gun with excellent export potential.

PERFORMANCE OVERVIEW

Developing a skilled and highly innovative workforce		
Target	**Achievement**	**2016/17 Outcomes and 2017/18 Outlook**
Training spend: 3% of personnel cost	3% of the personnel cost was spent on employee skills development (R68m)	3% of the personnel cost to be spent on employee skills development

REMUNERATION AND BENEFITS

The Denel human capital strategy is designed to attract and retain employees of the right calibre and competence, and to motivate employees to perform in line with our business and operational objectives and goals. To ensure internal equity, Denel evaluates and grades jobs to provide equitable remuneration to employees in accordance with their assigned duties and responsibilities, while differentials will be based on fair practices.

Denel pays fixed remuneration on a total guaranteed package (TGP) basis. This value is used for the development of pay ranges and for benchmarking purposes. It includes all contributions to the company's benefit structures and consists of the following:

» Cash component;
» Retirement fund contribution;
» Travel allowance (only if the employee qualifies);
» Medical aid contribution; and
» Thirteenth cheque may be structured.

Denel has its own retirement fund called Denret, which is a defined contribution fund to provide members and their dependants with reasonable and competitive retirement and risk benefits such as death and disability benefits.

Short-term incentives are also available, which are dependent on company and individual performance and are paid annually.

EMPLOYEE WELLNESS

A correctly designed wellness programme can increase productivity, boost morale and reduce stress. Wellness programmes help employees make smart and healthy choices that can reduce healthcare costs, increase vitality and diminish absenteeism. All Denel entities ensure they have a wellness programme that addresses physical, mental and social health needs. The corporate medical aid, namely Discovery Health, also conducts health days to assess employees' physical health as early detection is key to treatment of any medical condition. Throughout Denel we ensure compliance with occupational health and safety (OHS) regulations by appointing health and safety committees.

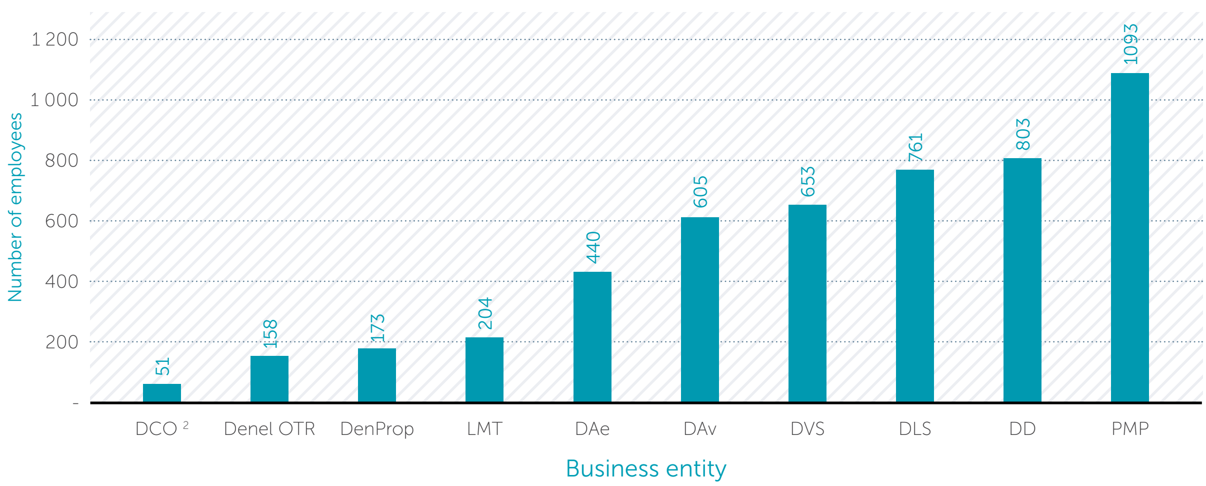
HUMAN CAPITAL REPORT

WORKFORCE PROFILE

Talent management strategically focuses on ensuring that Denel's skills needs will be adequately met in the short-, medium- and long-term. Effective talent management is of critical importance for transformation in that initiatives are put in place to ensure that there are sufficient skills from the designated groups (black [1] people, women and people with disabilities (PWDs) to ensure that Denel's workforce is fully representative in meeting current and future organisational needs.

Denel currently employs 4 941 (2015/16: 5 114) employees at the various majority owned entities. The graph below indicates the employees per entity:

EMPLOYEES PER BUSINESS ENTITY



1 Refer footnote 1, page 07.
2 Denel Integrated Solutions and Maritime (Denl ISM) is included within the DCO headcount.

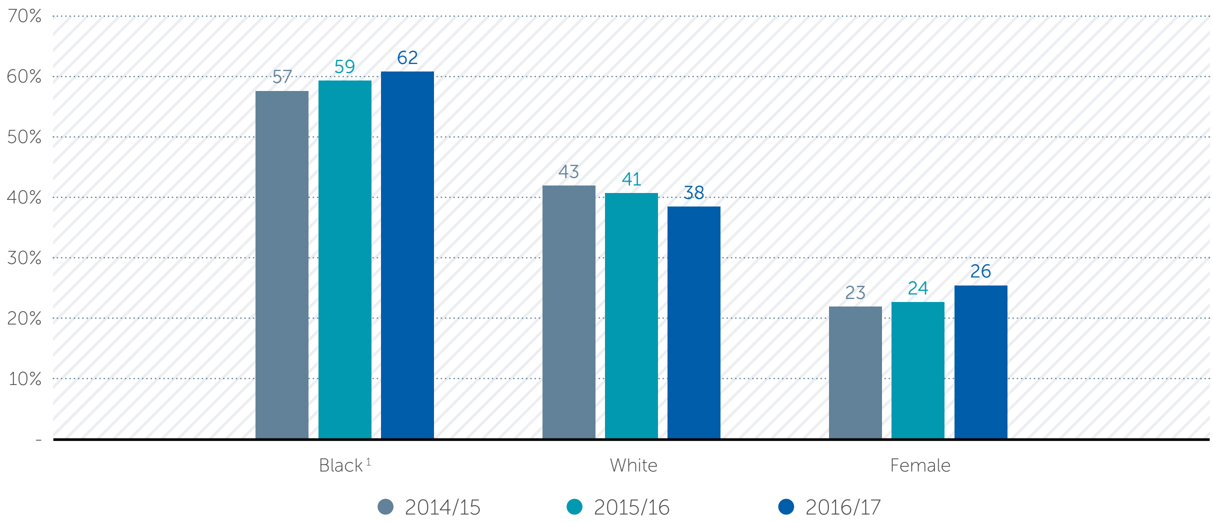
The workforce has contracted slightly due to economic conditions which resulted in a moratorium being placed on the appointment of external candidates, as well as restructuring at Denel Aviation and Denel Dynamics.

DIVERSITY AND INCLUSION

Inclusivity is integral to Denel's transformation process in that it promotes effective workplace relationships amongst colleagues from diverse backgrounds, which in turn facilitates inclusivity, innovation and productivity for business benefit. The focus is to improve the level of diversity and inclusivity within the existing workforce, while creating an environment that promotes engagement and satisfaction of a diverse workforce profile.

The graph below outlines the demographics of the workforce. As indicated below, black [1] employees comprise 62% (2015/16: 59%) of the workforce and females comprise 26% (2015/16: 24%).

DEMOGRAPHIC OF WORKFORCE



OCCUPATIONAL BAND CATEGORIES

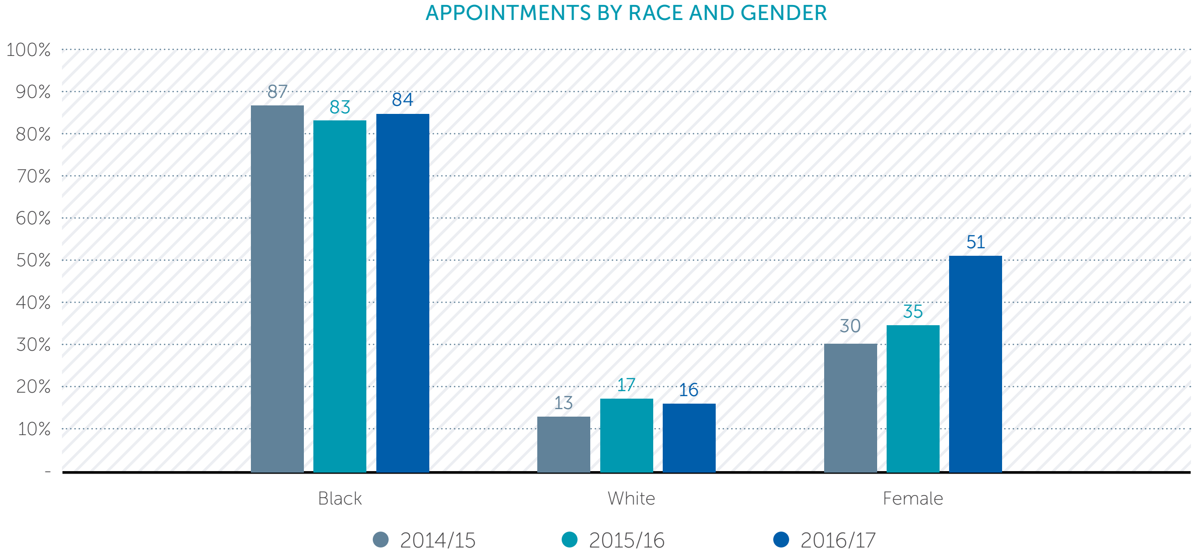
The table below indicates how diversity within the workforce has increased across all occupational band categories:

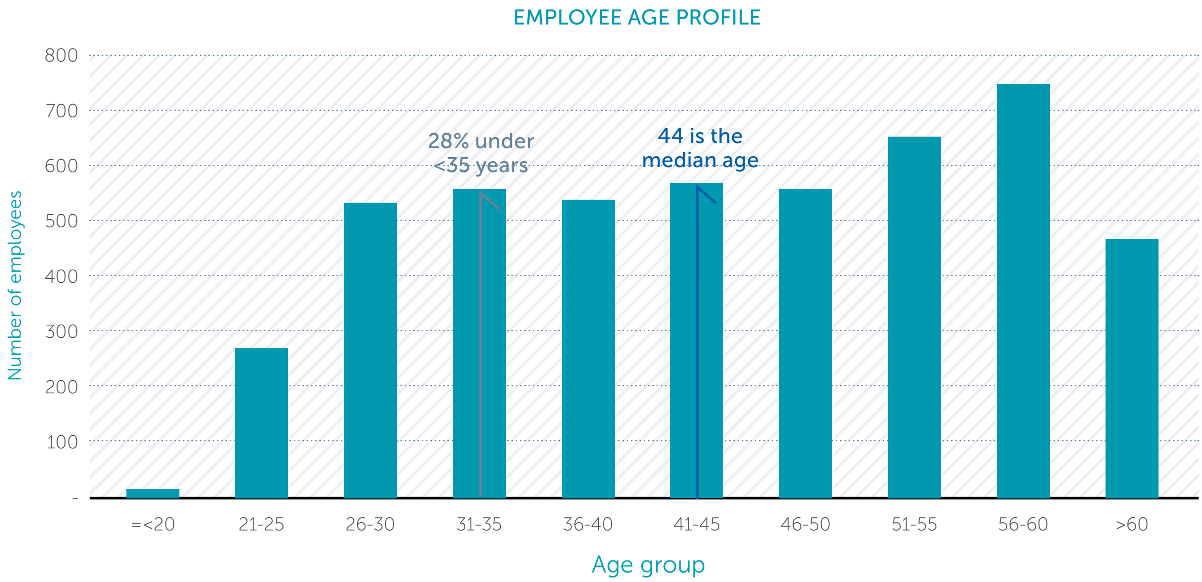
OCCUPATIONAL BAND CATEGORIES	2016/17		2015/16		2014/15	
	BLACK	WHITE	BLACK	WHITE	BLACK	WHITE
Executive management	8	4	8	4	8	3
Senior management	25	25	28	28	22	28
Management	119	195	116	228	109	227
Professional	1 928	1 318	1 885	1 451	1 639	1 364
Administrative	266	169	294	193	264	177
Support	195	110	194	107	158	98
Trainees	204	13	193	25	164	25
General workers	307	55	303	57	246	27
Sub-total	**3 052**	**1 889**	**3 021**	**2 093**	**2 610**	**1 949**
Total	**4 941**		**5 114**		**4 559**	

1 *"Black" means African, Coloured or Indian persons as defined by the B-BBEE Act.*

ATTRACTION

In order to improve diversity within the workplace, Denel utilises new appointments to improve equity. During the period under review, Denel appointed **416** new employees, with **84**% of new recruits being ACIs (Africans, Coloureds and Indians), and **51%** being female.





The median age of Denel employees is **44** years. For Denel this signifies a good balance between younger inexperienced employees and more mature seasoned professionals. Horizontal succession planning ensures that employees nearing their retirement age have competent successors to ensure business continuity. **28%** of our employees are below 35 years of age.

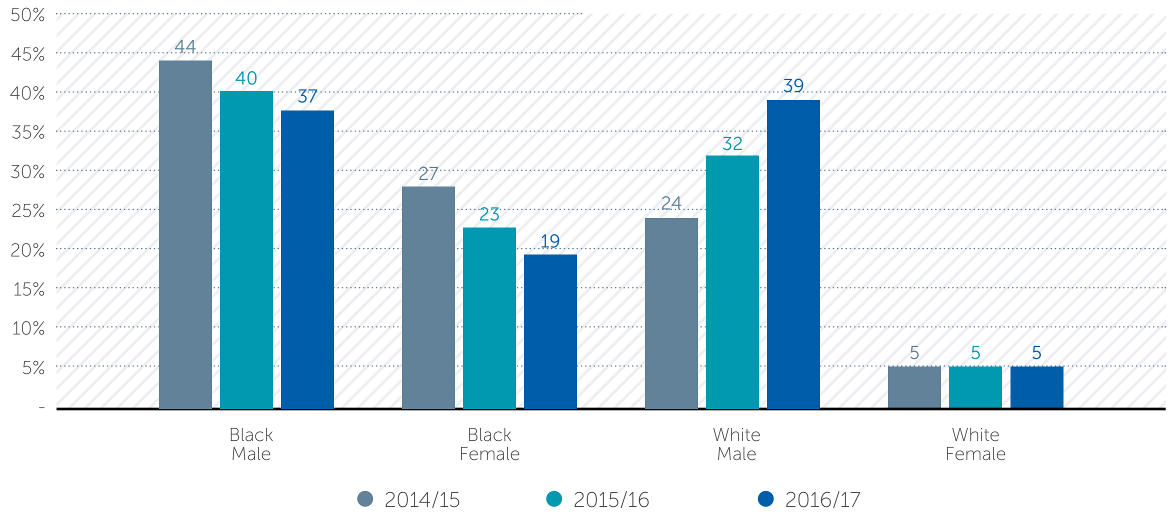
INDUSTRIAL RELATIONS

Labour relations within Denel remain positive and constructive. Of the total workforce, 51.6% (2015/16: 51%) is affiliated to one of the recognised unions. The labour environment is considered stable. Various platforms within the group have been established to regularly interact with unions.

TERMINATIONS

During the period under review regretted loss terminations (resignations) increased marginally to **4.7%** from **3.2%** during the previous financial year. The graph below indicates terminations by race and gender. Retention of key skills is essential within the context of global skills shortages. Various retention mechanisms exist within the group, which are constantly reviewed to ensure relevance.

TERMINATIONS BY RACE AND GENDER



PERFORMANCE OVERVIEW

Retention of labour force and maximised employment in designated groups			
Description	Target	Achievement	2016/17 Outcomes and 2017/18 Outlook
ACI as % of total appointments	80%	84%	Continue to create an environment that cultivates transformation for all designated groups with an increase in representation of women in leadership.
Women as % of total appointments	40%	51%	
Maintain employee numbers	5 114	4 941	

SOCIAL CAPITAL

Denel recognises that the manner in which it engages with its employees, suppliers and broader society is important. This will affirm Denel as a responsible corporate citizen and further meet its strategic objective to entrench a culture of transformation in the broader sense of the society.

We define social capital to include the internal relationships as well as external stakeholders. Denel has deliberately chosen to use CSI as a strategic lever to eliminate the persisting social ills of poverty, unemployment and inequality, in partnership with the government. Our CSI interventions seek to fulfil our societal obligations as a state-owned company, by delivering on our Shareholder's Compact (refer page 80) with the shareholder and, beyond that, living up to one of our core values: **CARING**. The approach to CSI is one of efficient delivery of strategic interventions in an integrated manner that consolidates funds across all the entities in the group into a single source for more meaningful projects with greater impacts.

CORPORATE SOCIAL INVESTMENTS

Denel has positioned itself as a responsible corporate citizen committed to the advancement of previously excluded communities, particularly those from rural areas. In order to achieve this objective and through the visionary leadership of the current Denel board, the organisation has moved away from spending the mandatory 1% for socio-economic development. This has led to the extension of the Denel group flagship CSI project, Schools Outreach Programme (SOP), which offers extra tuition in Mathematics and Physical Science.

This programme was previously run in only three provinces, Gauteng, Mpumalanga and North West. It has now been extended to include the Eastern Cape, Limpopo and KwaZulu-Natal. In addition, we introduced a bursary programme targeting learners from rural communities to train as commercial pilots.

EDUCATION INITIATIVES

Maths and Science Schools Outreach Programme	**R4.9m - impacting 455 learners across provinces**

» The programme is aimed at addressing the technical skills shortage due to non-participation and poor performance by learners in Mathematics and Physical Science, especially in the previously disadvantaged communities. In partnership with the Department of Basic Education, learners are offered extra tuition in Mathematics, Physical Science, English, Life Science and Engineering Graphic Design on Saturdays and during school holidays . The programme is run in six provinces. This contributed to the improved success rate in the Free State for achieving top matric result status in 2016.

Employee volunteerism	**R95k - Free State Department of Education Matric Winter School impacting over 1 000 learners**

» In partnership with the Department of Basic Education, Denel engineers offer extra tuition to learners in rural communities.

Denel Winter Camp	**R470k - 200 learners from various school in Gauteng, Limpopo and the North West**

Telematics	**R60k - impacting 1 500 learners in Tsakane High School**

» Interactive learner support system from the University of Stellenbosch which offers revision sessions to learners in Grades 10 - 12.

Teacher support	**R104.4k - impacting 130 Grade 0-7 learners at schools in the Western Cape**

» Denel pays the salary for extra teachers so that the school can accommodate more learners from the area. These learners would have to commute extensively if they were not accommodated in these local schools.

HUMANITARIAN OUTREACH

Mandela day	**R91k - impacting over 600 individuals**

» Denel donates sanitary protection/dignity packs and various hygiene products to learners in disadvantaged communities to reduce absenteeism due to lack of sanitary protection.

» Employees donated funds and manpower to the Zodwa school for learners with special needs. The kitchen provides meals daily to 200 physically challenged learners from disadvantaged communities.

» Employees donated books for a library in Ekurhuleni as part of "Read a Book" drive.

INFRASTRUCTURE DEVELOPMENT

School facilities upgrade — R100k - impacting 40 children - Mooiplaas informal settlement

- Welding, upgrade and repair of school chairs and desks by artisans.
- Disposal and replacement of old chemicals for school science laboratories in Tshwane.
- Donations of office furniture for use in schools.

AWARENESS INITIATIVES

Career exhibitions — R634k - impacting 35 000 Grade 10-12 learners

- Denel participates in various career expos nationally in order to expose learners to the various careers available for science engineering and technology. These include visits to universities in a drive to recruit learners for bursaries and internships.

Air shows — R798k - impacting 5 000 Grade 10-12 learners

- Learners from disadvantaged communities get exposed to the world of aviation through air shows. The events ensure that learners are provided with information about the company and possible future careers and they also get to do aviation-related activities.

SUPPLY CHAIN

Denel is committed to using supply chain initiatives or programmes to pursue value for the business and to support the government in its drive to transform the economic landscape and create employment. This economic transformation entails a targeted approach to develop eligible black-owned companies that will supply into the core business of Denel. Secondly, it entails a constant scanning of the supplier base to identify black-owned companies with potential or capable of supplying into both the core and the non-core part of the business. The third intervention is a systematic intervention to support the Black Industrialist (BI) programme by creating access to opportunities for identified BI candidates.

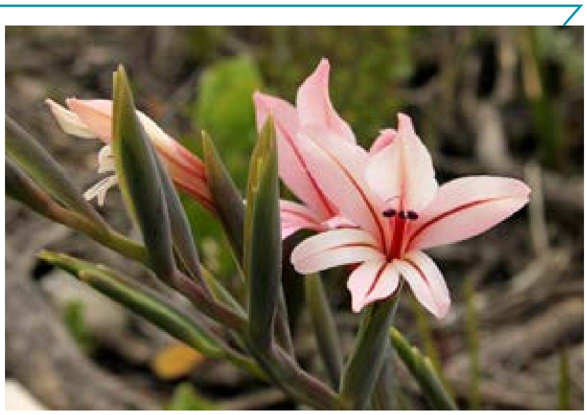
The Denel group has reviewed its approach to Enterprise and Supplier Development (ESD) with a view to achieving a high success rate whilst shortening the development cycle. That has necessitated a re-evaluation of ESD beneficiaries that there is focus primarily on those companies that will lessen dependence on untransformed companies and in the process increase the pool of strategic black suppliers.

Apart from continuing to conduct an assessment of potential candidates for development prior to approving them based on Denel's criteria, there is an additional focus to track and report on the business opportunities that are extended to the said companies. This approach not only improves the probability of success in developing a sustainable and growing business but also increases Denel's spend on black-owned companies, as well as targeted designated group companies.

PERFORMANCE OVERVIEW

Contribute to transformation and socio-economic objectives			
Description	**Target**	**Achievement**	**2016/17 Outcomes and 2017/18 Outlook**
Procurement from black-owned suppliers as % of local spend	25%	27%	The group is pleased with achievements on the spend on black-owned companies and especially within the youth space. The supplier development programme strategy implemented will improve not only the number of businesses that have access to Denel but also the level of business that they receive. The focus in the 2017/18 financial year will be smart procurements wherein Denel looks to: » Improve planning and developing a procurement strategy for high value and critical transactions; » Exploiting the group purchasing power; and » Improving spend on B-BBEE and in particular companies owned by military veterans.
Black woman-owned as a % of total local spend	5%	9%	
Black youth-owned as a % of total local spend	1%	1.6%	
Spend on companies with ownership by persons with disabilities	0.2%	0%	
Small and emerging enterprises suppliers developed	20	73	
Corporate social investment spend	R3.5m	R7.2m	Continued focus on spend on advancement of skills in science, maths and the defence industry.

ENVIRONMENTAL CAPITAL



The group's business delivers a positive impact on the country's economic and social development. At the same time, such industrial activities in areas where Denel operates might have inherent negative effects on the environment. Therefore, we see it as a strategic objective to manage, protect and rehabilitate the environment in conformance with our environmental management policy.

Whilst the policy is based on the principles of ISO14001, providing guidelines and minimum requirements applicable to each core entity, we are committed to continuously improve environmental management activities and operations to meet the environmental objectives. As outlined below, we constantly strive to minimise waste and prevent pollution; in essence caring for our precious environment.

MANAGING MATERIAL ENVIRONMENTAL IMPACTS

As a group, we address environmental responsibilities in the design, manufacture, packaging and transportation processes of the value chain as part of an integrated environmental management process. Environmental impact studies and environmental risk assessments are included as key operational and strategic imperatives in the entities' processes.

KEY ENVIRONMENTAL GOALS

Protection of species and habitats, and the conservation of biodiversity and natural resources.

Mitigation of environmental disturbances, deterioration, contamination and/or destruction as a result of human activity and structures.

Providing a remediation plan for all entities.

CEOs appointed to execute environmental responsibility S&E committee provides oversight

Denel screens suppliers using environmental criteria at most of its business entities and will extend these screenings to all campuses. The group is not aware of any potential or actual negative environmental impacts that could arise from its supply chain environment.

The environmental aspects discussed below have been identified as material for the Denel group and we manage, monitor and report these on a regular basis.

Denel subscribes to ISO and requires all its entities to be ISO certifies

ENERGY AND CARBON EMISSIONS

Our continued commitment to reducing energy consumption and carbon footprint is evidenced by continuous investment in mitigation strategies. This is further evidenced by the objective to improve energy efficiency and reduce our direct greenhouse gas emission by at least 20% by 2020.

The table below breaks down Denel's identified and quantified carbon sources at the various campuses and entities:

ENERGY CONSUMPTION

	ELECTRICITY	LIQUID PETROLEUM GAS	COAL	HEAVY FUEL OIL	AVIATION TURBINE FUEL	PETROL	DIESEL	PARAFFIN
CAMPUS	kWh	kg	kg	litres	litres	litres	litres	litres
Kempton Park	29 989 656	80 866	-	290 143	90 370	6 865	11 317	-
PMP	24 833 937	49 699	1 717 890	-	-	73 472	51 516	51 640
Irene	18 760 350	-	-	-	-	25 000	17 440	-
Lyttelton	9 696 033	-	-	-	-	28 950	34 816	-
DVS	10 061 242	84 458	-	-	-	-	41 977	-
Denel OTR	5 857 032	-	-	-	-	107 387	137 000	-
LMT	723 320	-	-	-	-	-	18 779	-
Houwteq	1 656 391	-	-	-	-	-	-	-
Total	**101 577 961**	**215 053**	**1 717 890**	**290 143**	**90 370**	**241 674**	**312 845**	**51 640**

Carbon sources reflected in tonnes CO_2 equivalent emissions on the various campuses are tabulated below:

CAMPUS	ELECTRICITY	LIQUID PETROLEUM GAS	COAL	HEAVY FUEL OIL	AVIATION TURBINE FUEL	PETROL	DIESEL	PARAFFIN
Kempton Park	29 990	238	-	923	229	16	30	-
PMP	24 834	146	4 153	-	-	169	138	131
Irene	18 760	-	-	-	-	58	47	-
Lyttelton	9 696	-	-	-	-	67	93	-
DVS	10 061	249	-	-	-	-	112	-
Denel OTR	5 857	-	-	-	-	247	367	-
LMT	723	-	-	-	-	-	50	-
Houwteq	1 656	-	-	-	-	-	-	-
Total	**101 578**	**633**	**4 153**	**923**	**229**	**556**	**837**	**131**

Scope 1 and 2 emissions based on DEFRA CO_2 equivalent emissions

With a view to further reduce carbon footprint, Denel is constantly assessing its operations and develop specific objectives and measures to be implemented. As electricity remains the main source of carbon, Denel has implemented an energy management policy that supplements the environmental management programme in order to address energy efficiency and reduce consumption.

ENERGY EFFICIENCY PROGRAMME

Denel's manufacturing plants require stable and affordable energy in an uninterrupted manner to operate efficiently. Denel's comprehensive energy efficiency programme was rolled out for the first time in 2012/13, making this its fourth year of implementation. Across the group the company continues to pursue in Eskom's energy conservation project of reduction in electricity consumption by 10% through deliberate measures to be more energy efficient.

Measures taken to maintain energy savings include instilling responsible energy consumption behaviour in the workplace through ongoing roadshows throughout the year. Building on the significant advancements in the energy efficiency improvement programme over recent years, we implemented a three-tier plan which is reviewed and updated annually.

DENEL ENERGY EFFICIENCY PROGRAMME

1 PHASE ONE	Switch to energy efficient lighting in all Denel offices and manufacturing facilities.
2 PHASE TWO	Optimising boiler systems, hot water systems, compressed air systems, waste heat recovery systems and heating, ventilation and air-conditioning (HVAC) systems, LED lighting systems, smart switch technology.
3 PHASE THREE	Renewable energy generation.

EMPLOYEE AWARENESS BEHAVIOURAL CHANGE

BEHAVIOURAL CHANGE

WATER

Denel's entities have water management plans in place to manage and promote the efficient use of this resource. It remains a challenge to reduce while at the same time maintaining our operations and facilities at optimal capacity. Denel is implementing a grey water system and by harvesting rainwater we create significant value. Rainwater collected from roof surfaces is stored, filtered and piped to processes where water is required, i.e. evaporative coolers, cooling towers, gardens, etc. Rainwater harvesting reduces dependence on water supplied by the local municipalities, which adds value downstream in the towns and cities where Denel operates. In addition, discussions with suppliers are under way to improve water leak detection and further reduce water wastage.

Water consumption (kl) per campus are tabulated below:

DVS	Houwteq	Irene	Kempton Park	LMT	Lyttelton	Denel OTR	PMP	Total
17	11	73	351	461	47	79	274	**1 313**

LAND STEWARDSHIP AND NATURE CONSERVATION

Denel's operations that involve explosive and chemical related activities increase the risk of contamination and pollution of the environment. Denel has put in place systems to detect and mitigate the adverse effects on the environment of our operations. The system includes procedures to handle or prevent major spillages that may contaminate land. These procedures are part of the emergency response plans in the SHE management system. During the year under review no material incidents were recorded.

Nature conservation plans are in place with the objective to protect, conserve and manage protected areas and species involving fauna and flora. These plans are aligned with the objectives of National Electrical Manufacturers Association (NEMA).

During the year Denel collaborated with government and other stakeholders, specifically the Overberg district municipality and marine and coastal management on the draft situation analysis report of the Overberg Coastal Management Programme.

VARIETY OF SPECIES AT DENEL OTR

FLORA	FAUNA
Cera Argenteum (Ceratocaryum argenteum)	Bontebok (Damaliscus pygargus)
Leuca Decorum Star (Leucadendron laureolum)	Eland (Taurotragus oryx)
Leuca Tortum Female (Luecadendron linfolium)	Kudu (Tragelaphus strepsiceros)
Pro. Red (Protea obtusifolia)	Red Hartebeest (Alcelaphus buselaphus)
Pro. Red Repens (Protea Repens)	Springbok (Antidorcas marsupialis)
Pro. Susannea (Protea Susannae)	
Sta. Glass-eyes (Staavia radiate)	

LAND CONSERVATION

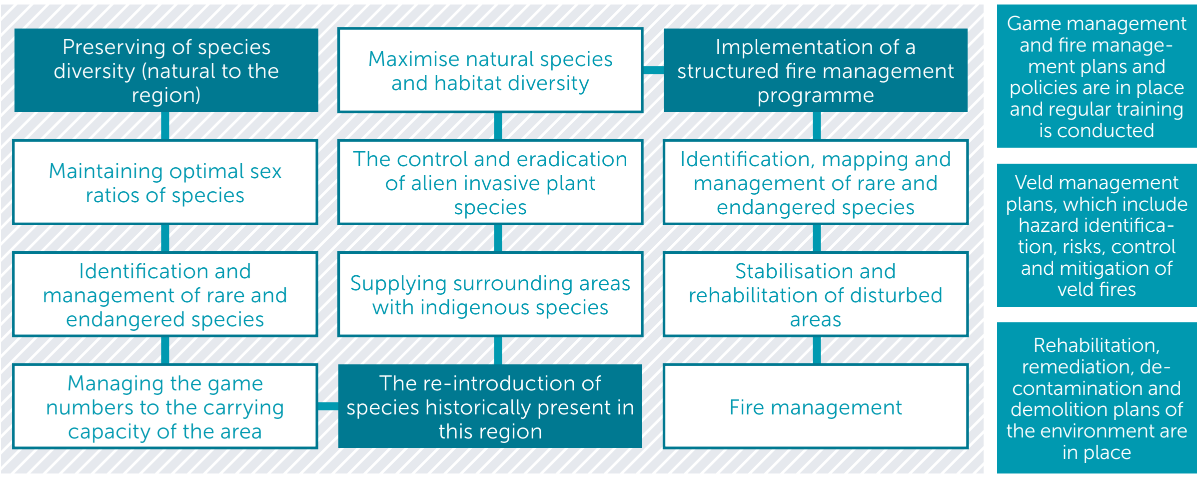
The Denel OTR weapons testing facility is situated on 43 000ha of land in a sensitive conservation area. It is located near the southernmost tip of Africa, between Waenhuiskrans and Cape Infanta, where it forms part of the De Hoop conservation area. Approximately 60 000ha in extent, it is one of the few relatively untouched nature areas remaining along SA's southern coast. Apart from its scenic beauty, Denel OTR harbours a unique diversity of ecosystems with its greatest value being its extensive stretches of unspoilt coastal vegetation and the exceptionally rich and varied marine life along the coastline.

The environmental management system at Denel OTR responds to the unique ecological management requirements applicable on the test range and the adjacent De Hoop Nature Reserve, the De Hoop Marine Protected Area, as well as Air Force Base Overberg. The environmental management process includes identifying indigenous species and alien plants to mitigate adverse environmental effects. The single largest threat to the natural vegetation and ecosystems at the range is posed by alien invasive plant species, such as the Rooikrans. The mechanical eradication of these adult trees coupled with the biological control of the seed of these trees, constitutes a holistic approach to effectively manage and control the alien plants.

Over the past eight years, the mechanical control of Rooikrans in collaboration with the Department of Environmental Affairs, resulted in 5 000ha of land being successfully cleared. Denel OTR continuously monitors previously cleared areas. Biological control of Rooikrans by means of the gall-fly introduced at the range during the year 2000 continues to show signs of success. This has resulted in lesser seed formation and a lower rate of new Rooikrans trees flowering.

Through a comprehensive campaign to ensure that the indigenous game and wildlife of the area are preserved, Denel OTR continues to promote conservation in the area. Considerable success has been achieved with the re-introduction of the Cape Mountain Zebra into the region with a herd of over 90 of this species located there. Various other game, such as the Bontebok and Eland have also managed to thrive in this region due to Denel OTR's intensive interventions supported by CapeNature.

The primary goal for game conservation are to manage and maximise species natural to this region according to ecological sustainable methods, through:



In addition, a rich legacy of prehistoric remains and historical sites and buildings are found along the range's coastal area. Although there are no proclaimed national monuments on Denel OTR terrain, all historical buildings of architectural merit, the 'visvywers' (stone fish traps) and other important archaeological sites like Strandloper shell middens, have been charted and are conserved. The striking Melkkamer homestead situated on the bank of the De Hoop Vlei was transferred to CapeNature and was restored to its original splendour.

WASTE PRACTICES AND RECYCLING

Denel's manufacturing processes include a significant amount of waste being generated, some which is hazardous waste. Management of waste is key for the group as part of the standard operating procedures of all hazardous substances to be stored and handled safely. Recycling or disposal of hazardous substances, as well as segregation and separation of hazardous substances, are addressed in these procedures that are reviewed on a regular basis. Denel has valid permits from local authorities for the storage and handling of these hazardous substances. The management of the use and safe disposal of chemical substances, domestic and hazardous waste, as well as recyclable waste in a responsible manner is key to how waste is handled. Denel uses reputable waste removal suppliers as part of its waste management value chain.

Details of hazardous and general waste disposed and recycled are indicated in the table below:

TYPE OF WASTE	DISPOSAL/RECYCLING METHOD AND COMMENTS
Hazardous waste disposed (tons)	Disposed of 120tons (2015/16: 332tons) at special landfills, where waste is treated in an environmentally friendly manner. Safe disposal certificates are received.
Hazardous waste disposed (kl)	Disposed of 1 505kl (soluble cutting oil and water) (2015/16: 611kl) at special landfills where the waste is treated in an environmentally friendly manner. Safe disposal certificates are received from waste contractors.
Hazardous waste recycled (tons)	Recycled 244tons (2015/16: 370tons) as part of environmental management.
Non-hazardous disposed (tons)/(m^3)	Disposed of 772tons (2015/16: 224tons) at normal landfills by waste removal companies or own transport.
Non-hazardous waste recycled (tons)	Recycled 619tons (2015/16: 537tons) of paper, plastics, tins and metal shavings which are sold to recycling companies or dealers.

INTELLECTUAL CAPITAL

Denel is continuously keeping abreast with new technologies as well as maintaining the internal knowledge learnt over time. As such, R&D investment and intellectual property development are critical to maintain and expand the technologies, capabilities and products, in keeping with Denel's mandate as a key strategic organ of the state.

The intellectual properties that Denel holds, together with the skilled, experienced and technically qualified employees, are the key inputs in the intellectual capital. Partnering with academic institutions, research bodies and industry peers to develop, pilot and implement new technologies remains key in advancing in new technologies. Collaboration with clients on new technology is another platform in which Denel investigates and develops new technologies. This is based on specific or broad client needs and in which Denel would develop solutions to best suit the client.

Key organisational intangibles also include the know-how, management systems and company culture. Intellectual capital is relevant particularly in the implementation of large-scale projects. Project management skills and structures need to be in place. The challenges faced within the development stages are that the project lifecycles are sometimes underestimated at conceptualisation leading to delays in project deliveries. The transfer of past experience knowledge becomes important for future projects. The implementation of the Centre of Innovation and Learning (CIL) at DD and at DLS assist in bridging the knowledge gap between mature engineers and the young engineers entering Denel. The technical mentorship programme is project-driven and the mentor and protégé relationship can formally run for either one or two years depending on the needs of the protégé.

PERFORMANCE REVIEW

Contribute to development in support of national key requirements			
Description	**Target**	**Achievement**	**2016/17 Outcomes and 2017/18 Outlook**
R&D spend 8.5% of revenue limited to R740m	R685m	R609m	R&D investment in 2016/17 of R609m has increased by 10.7% and includes both self- and client-funded investments. The focus for 2017/18 will be designing and developing services in line with market demand, i.e. cyber- and naval security.

DENEL SOVEREIGN SECURITY SOLUTIONS

To contribute to the promotion of **peace, safety and security** by delivering and supporting **complex, multidisciplinary systems in partnership with local and international defence, security and maritime players and stakeholders.**

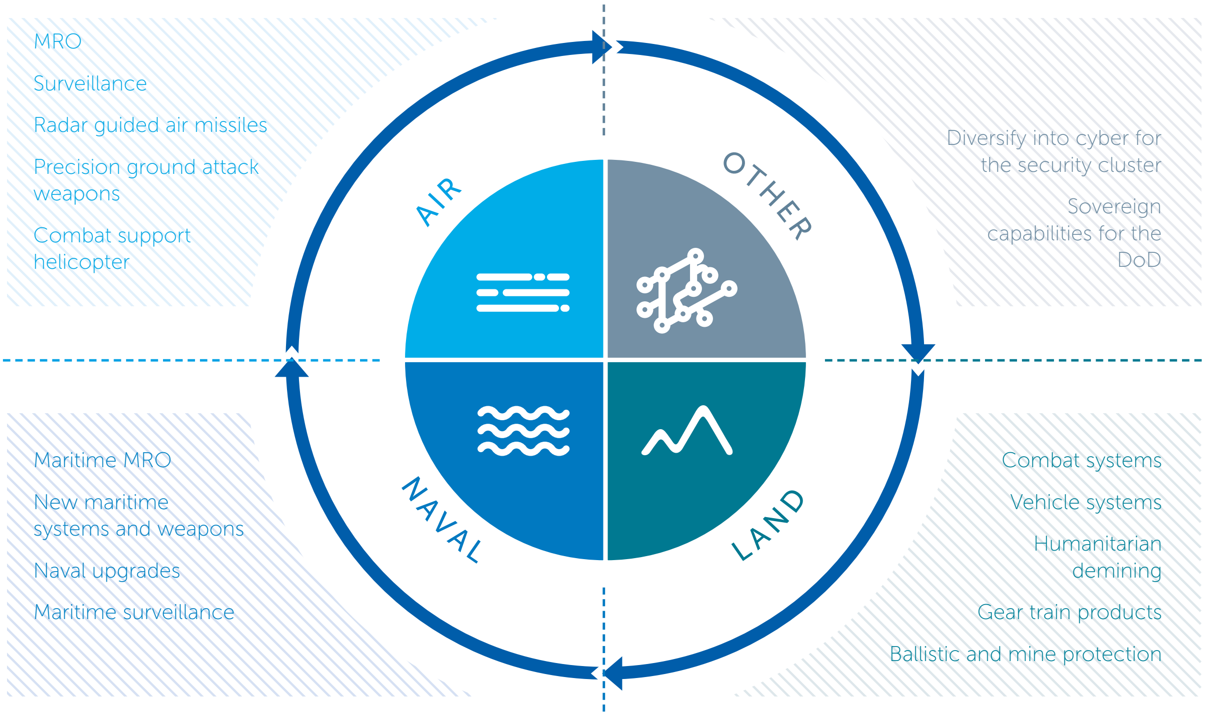
The primary focus of Denel Sovereign Security Solutions (Denel S3) will be to establish the DTC³, starting with a basic cybersecurity operations centre to provide Denel with protection against cyber threats. Ultimately, DTC³ will provide accredited cybersecurity services for the protection of sovereign defence and security interests aligned to the National Cybersecurity Policy Framework (NCPF), the Defence Review 2015 and the National Security Strategy.

KEY DENEL CAPABILITIES

- Model, simulate, design, develop, qualify and clarify complex systems
- Ammunition, munitions, propellant and pyrotechnics
- Broad advanced specialised manufacturing capability
- Manage turn-key systems acquisition, commissioning and support guided missile

- MRO capability for transport aircraft and helicopters
- Landward mobility, ballistic and mine protection technologies
- MRO capability for landward defence systems
- Armoured vehicle systems capability
- Combat helicopter and utility helicopter
- Electro-optics, optronics and photonics

- Missile radar technology capabilities
- Scientific test range capability
- Ballistic and mine protection
- Rapid firing cannon and gun
- Ground-based air defence
- UAV systems capability
- Satellite technologies
- Canine technologies
- Artillery system



CAPABILITY DEVELOPMENT

- C4ISR systems capability (land, sea, air, joint ops) to act as prime contractor for future programmes
- Military, paramilitary and homeland security capability (incl. border control, law enforcement and disaster management).

- Maritime systems integration capability
- Niche unmanned systems solutions (incl. armed, ship-launched and civilian UAV satellite surveillance and communications systems capability
- New generation artillery systems
- New generation missile systems

- Cybersecurity and encryption capability to support national programmes
- MRO capability for maritime systems
- MRO capability and fleet management of B-vehicle fleet
- MRO capability for combat and non-EC helicopters

FINANCIAL CAPITAL

Denel's strategic relevance for value creation for the shareholder is to stimulate and support South Africa's economic growth. This is enabled by sustainable and bankable profits. Apart from creating value through business activities, Denel's mandate is also to reinvest the financial capital created in each of the other capital areas in a manner that is most efficient and sustainable for the business.

The financial inputs in creating value have been:

Equity	Borrowings	Cash and cash equivalents
R2.7bn	**R3.3bn**	**R2bn**

The inputs to the financial capital are under pinned by access to capital funding. In order to achieve the strategic objective the focus in 2016/17 has been:

- Optimise cash conservation and unlock pre-payments;
- Obtain funding and maintain credit ratings;
- Normalise debt/equity ratio – drive profitability targets and deliver on bankable profits;
- Optimise scarce resource with the view to improve cost management;
- Exercise resilience in working capital management; and
- Adopt an aggressive and focused centralised cardinal campaign capture with the view to increase the order book.

VALUE ADDED STATEMENT

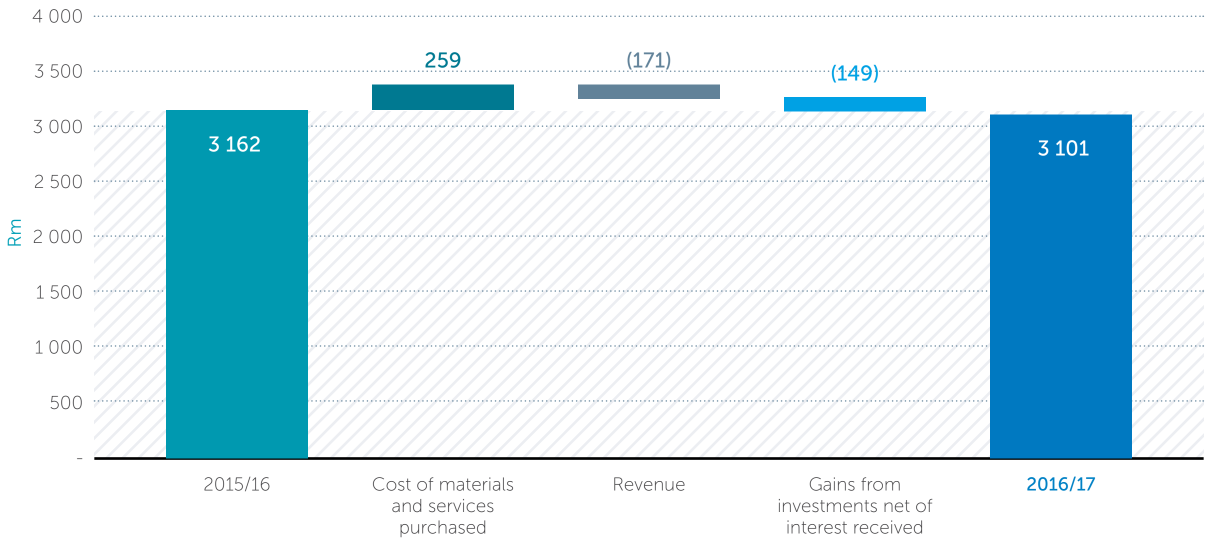
YEAR ENDED 31 MARCH 2017

	Notes [1]	GROUP			
		2016/17		2015/16	
		Rm	%	Rm	%
Revenue	2	8 057		8 228	
Less: Cost of materials and services purchased		(5 172)		(5 431)	
Value added by operations		2 885		2 797	
Gains from investments net of interest received		216		365	
Wealth created		3 101		3 162	
Distributed as follows:					
Salaries and relevant costs [2]	3	2 275	73.3	2 278	72.1
Providers of capital		340	11.0	297	9.4
Government		11	0.4	61	1.9
Re-invested in the group for continuation and expansion		475	15.3	526	16.6
Wealth distributed		3 101	100.0	3 162	100.0

The total amount reflected above excludes R601m (2015/16: R294m) collected by the group on behalf of governement.

1. *Refer to the notes to the consolidated annual financial statements.*
2. *Directors' remuneration is excluded from Employees: Salaries and relevant costs. Directors' remuneration are disclosed in detail on pages 101 to 103.*

VALUE ADDED



Whilst there has been improvements in wealth created by operations, gains from investments have decreased due to a drop in other income. In 2016/17, the outcomes of the value created has been:

- EBIT – **R628m**
- Net profit – **R333m**
- Cash from operations – **R376m**
- Fitch Ratings – **AAA long-term and F1+ short-term**
- Cash and cash equivalents – **R2bn**
- Share capital and reserves – **R2.7bn**
- EBIT – **8%**
- Debt to Equity – **1:1.2**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PART

3

STRATEGY AND
OPERATING CONTEXT

EXTERNAL ENVIRONMENT

LOCAL ENVIRONMENT

Our local customers are our most important partner and comprises 37% (2015/16: 42%) of Denel's current revenue stream. The local client base assists in key product developments which Denel leverages when pursuing foreign business initiatives. The current defence and security budget is 1.1% of GDP, which is low compared to international norms. Whilst the relatively low defence spend places pressure on Denel to find export clients to maintain capability and be sustainable, it provides a base load together with investment in new technologies. The technology is important when pursuing export business. The export business provides critical mass to sustain strategic and sovereign defence capabilities. The strategic alignment between the DoD, SANDF and Denel ensures that the recently approved Defence Review policy implementation does achieve its stated objectives.

EXPORT ENVIRONMENT

Stronger competition with the European and USA companies are to be expected in markets traditionally serviced by Denel due to contraction in defence spending in their home markets. It is further expected that customers will shift their focus from procuring systems with the highest possible performance to ones that are more affordable. In addition, lower oil prices are likely to affect the cash reserves of some countries and their spending patterns on defence going forward.

Despite the above, Denel is experiencing a strong demand for its products in the growth markets of Asia-Pacific and the Middle East. These markets are currently the main export customers for Denel products. There are a number of new business opportunities expected to be concluded and executed in the short- to medium-term. South Africa is well positioned through its foreign policies in these regions. The existing political support enjoyed by Denel from government and its agencies facilitates the business development in said markets.

Business opportunities in the African continent remain largely untapped due to ill-defined user requirements, funding constraints and other hindering dynamics, most of which are political. There is, however a gap to fill and opportunities to pursue specifically in the West African region.

Denel is in good standing with the United Nations which provides access to humanitarian and peacekeeping initiatives with some contracts currently being executed. The Latin American region is still heavily invested in acquisitions of weapon systems and despite defence cuts still offers opportunities for Denel. The poor economic outlook for this region, however, is expected to further erode market opportunities.

The global supplier base became an important value creation element to secure export business. To be successful in international markets requires localisation of capability and technology. Denel is well positioned with its networks through equity and strategic partnerships to take advantage of this trend.

Active participation in the IBSA and BRICS initiatives is expected to unlock better funding possibilities for the defence related projects and to further enhance collaboration within the BRICS countries in the near future.

STRATEGY

VISION	STRATEGIC DRIVERS	KEY OBJECTIVES	TO BE STATE
The state-owned credible South African strategic partner for innovative defence, security and related technology solutions	**Improve** customer and other stakeholder relationships in **support** of a strong, long-term order book	» Significant increase in the order book that can be converted into cash generated revenue » Strong relationship with customers and stakeholders » Leverage smart partnerships	**A dynamic, vibrant, financially sustainable, transformed and profitable organisation**
	Increase **productivity, efficiency** and **profitability**	» Focused managing of working capital » Operational excellence in contract execution » Optimise cost structure » Lucrative contracting » Profitable cash returns » Restructuring debt profile » Strong balance sheet	
	Enhance capabilities and foster **innovation**	» Deliver differentiated and sustainable value » Leveraging current product lines » Meeting customers' requirements » Selective and focused R&D investment particularly in areas of expertise and core strengths	
	Create a **dynamic** and **vibrant** organisation	» An entrenched culture driving a transformed, high performance and innovative organisation » Attract, develop and retain talent » Good governance	

Denel is a catalyst to transform the SA society which also deepens the industrial knowledge base

↓ ↓ ↓

PROGRESS ON THE STRATEGY

CUSTOMER RELATIONS AND STRONG ORDER BOOK

- Sound strategic stakeholder alignment with DoD
- Stable and comprehensible order book: R18bn
- Effective collaborations with strategic partners e.g. Technologies Poly Inc. on the maritime business

PRODUCTIVITY, EFFICIENCY AND PROFITABILITY

- Enhanced governance across entities
- Peer reviews to improve productivity and efficiencies
- Improved profitability, however with further improvements required

ENHANCED CAPABILITIES AND INNOVATION

- Capability expansion in cyberspace and maritime
- Improved R&D alignment with customer customisation demand

ORGANISATION CULTURE

- Improvements in female representation and ACI
- Sound governance process to ensure value creation and compliance to regulations

MATERIAL ISSUES

The material issues are those with the potential to affect Denel's ability to deliver on the strategy, create value and sustain the group in the short-, medium- and long-term.

MATERIAL ISSUES

IDENTIFY	PRIORITISE	RESPOND	REPORT AND MONITOR
» Issues at entity exco » Group board meetings » Stakeholder engagements » Media coverage	» Based on risk and opportunities » Impact issue will have on Denel	» Identify and implement mitigation actions	» Report at regular board meetings » Provide regular feedback to employees » Monitor against Shareholder's Compact » Monitor against performance targets

LIQUIDITY AND FUNDING

Material issue

Exponential growth in revenue has placed significant strain on cash resources and the Denel business model. This impacts on growth opportunities, reputation and operations due to sub-optimal cash to fund working capital and new business opportunities, as well as for R&D investment in new products. In addition, the group remains highly geared with debt of R3.3bn, of which about R2.4bn is due and planned to be rolled over with the renewal of the government guarantee.

Strategic response

- Unlocking significant amounts of cash currently trapped in working capital is a key priority to support further growth in the group by:
  - » re-engineering our working capital processes, including aspects of supply chain; and
  - » monitoring and evaluating working capital management mechanisms currently in place.
- Reposition ailing/non-core business areas and improve integration;
- Restructuring the cost base with the view to its improvement;
- Secure favourable pre-payments from key programmes; and
- Convert bank guarantees to Denel corporate guarantees in order to free up bank facilities.

CAPACITY CONSTRAINTS ON MAJOR PROGRAMMES DELIVERY

Material issues

The demands of South African programmes necessitate that the availability of project management resources be reviewed to address skills requirements, transfer of skills, succession planning and overall group alignment.

Strategic response

- Adaptation of programme management procedures to be in line with group project lifecycle management (PLCM) framework;
- Implementation of Programme Management Development initiative;
- Determine the capacity and requirements for new and current programmes and adjust as required; and
- Execute succession planning for programme management function.

PEOPLE – TRANSFORMATION, RETENTION AND ATTRACTING CORE SKILLS

Material issues

Denel as a state-owned enterprise and a major defence industry player needs to take a lead in the transformation of this sector by facilitating the inclusion and development of black people and women to be full participants.

Activity growth in Denel drives the need for experienced and skilled resources.

Strategic response

- Changing the employee profile by ensuring that women are adequately represented in all occupational levels;
- Shaping bursary intake to have increased ACI representation;
- Seeking ways to retain employees from the ACI group;
- Ensuring that promotions to senior levels give preference to employees from the ACI group, especially women;
- Establishing support mechanisms such as coaching and mentoring for ACI employees;
- Creating an organisational climate wherein ACI employees are respected and treated equitably; and
- Value add for our employees and creating a vibrant culture.

SUPPLY CHAIN

Material issues

As a group, the external supply chain forms more than 50% of our input costs. The supply chain function is therefore instrumental to the achievement of the corporate plan. To this end, Denel supply chain needs to be more effective, efficient and value adding thereby ensuring that Denel:

- Achieves strategic objectives;
- Complies with regulatory framework; and
- Delivers the best value for money.

Strategic response

- Ensure that the supply chain function is aligned to the corporate strategy in order to address business needs on time and in accordance with shareholder expectations;
- This strategy provides strategic framework within which Denel will pursue supply chain excellence. It supports the delivery of Denel's priorities and strategies in areas including transformation;
- Implement control systems that will strengthen governance and compliance in order to eliminate irregular expenditure and fruitless and wasteful expenditure;
- Re-organisation of the supply chain function to execute the mandate as expected. The emphasis is to recruit supply chain management (SCM) professionals with the correct mind and skills set and capacitating the current employees; and
- Denel to instil a culture of collaboration between its entities to leverage on economies of scale.

STAKEHOLDER ENGAGEMENTS

Material issues

The Denel group became the subject of a fair degree of negative media coverage, which had an adverse impact on the image and reputation of the group.

The key issues that resulted in most of the negative reporting emanated broadly from the following:

- Executives who were suspended by the board;
- Denel Asia and VR Laser Asia;
- Relationship with the National Treasury; and
- Fireblade Aviation matter.

This negative media coverage had the following impact:

- Influenced investor perceptions;
- Employee uncertainty and mistrust; and
- Customer and supplier perceptions of the group.

Strategic response

- Targeted stakeholder engagements in order to restore image and reputation by correcting perceptions;
- Embarked on investor roadshows with the purpose to provide clarity on investor concerns;
- Heightened focus on brand management to restore public trust, repair and strengthen the Denel brand in both local and global markets; and
- Concluded on the suspended executives matter, appointed the GCFO and Group Company Secretary and recommended a candidate for the GCEO position to the shareholder.

RISK MANAGEMENT

Denel is a strategic enterprise, offering defence equipment to the country's military and law enforcement agencies. Our shareholder places a high premium on protecting the business. The governance of risk in whichever form it presents, is a key strategic driver. Denel's risk governance process emphasises continuous anticipation and identification of risks. Importantly, in the process the executive management allocates significant resources to implement measures to respond to risks and opportunities in order to create value for the shareholder.

RISK GOVERNANCE PROCESS

Denel's enterprise-wide risk management system is a combination of Committee of Sponsoring Organisations of the Treadway Commission (COSO) and ISO31000 principles. Risk assessment is embedded in the strategy process, the execution of significant transactions, as well as the delivery of products and services from conception to delivery. The risk management process entails continuous identification, evaluation, mitigation and monitoring of risk, using robust intelligence processes and structures. As a result, it informs strategic and operational decisions and is underpinned by an effective system of internal control. The system of internal control ensures delegations of authority, regulation of significant transactions, compliance processes and good governance. The various levels of the organisation play specific roles in the governance of risk. The board is ultimately responsible for risk governance and has assigned risk oversight to the A&R committee, which is supported by the S&E and PR&T committees on pertinent issues.

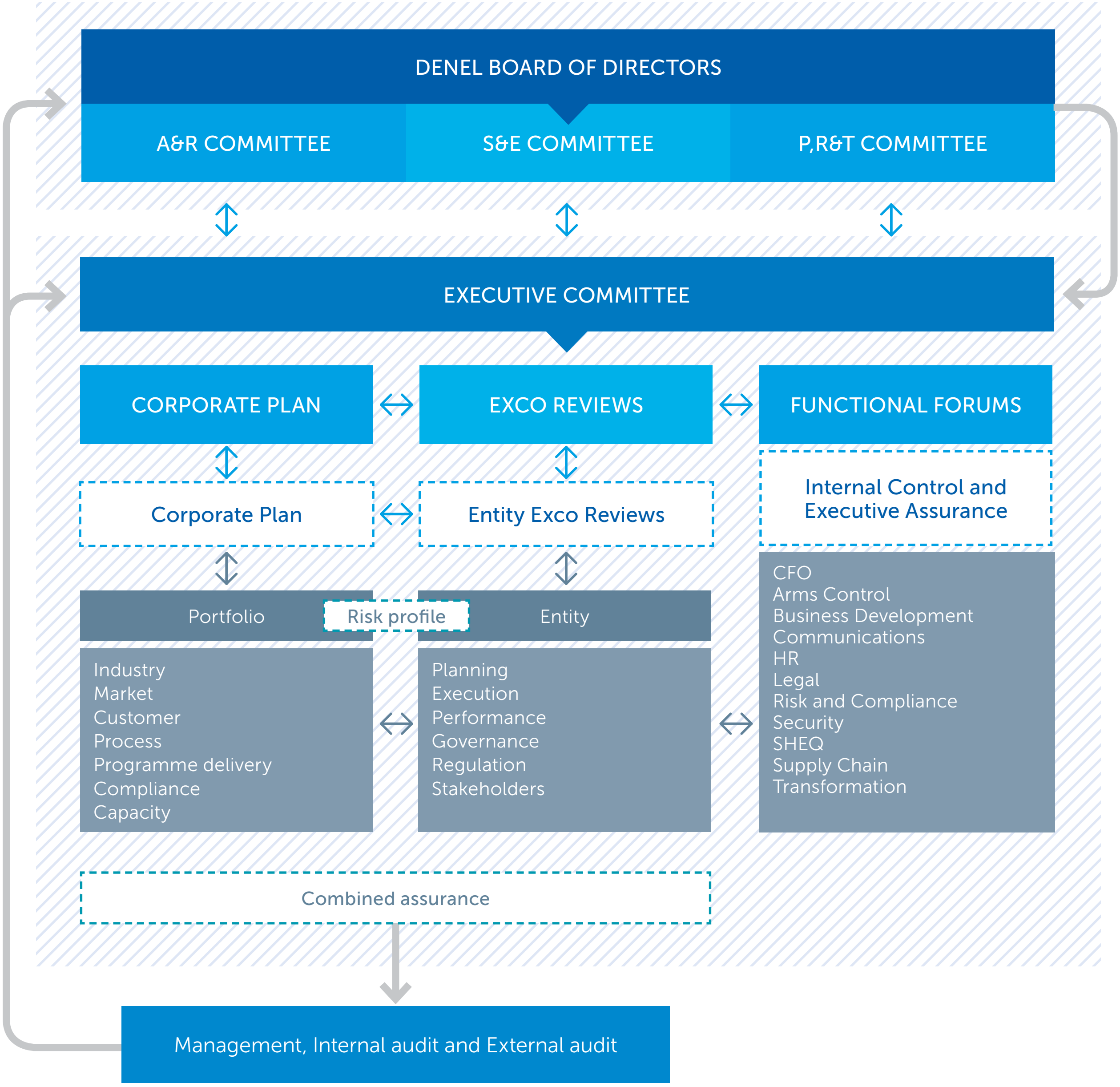
The exco is guided by the delegation of authority in implementing systems of risk management. Denel has put in place a system of internal control which includes financial and operational processes to manage and monitor risk. The exco is responsible to the board regarding the implementation of a robust system of risk management and internal control.

Denel adopted a combination of a top-down and bottom-up approach to risk assessment and uses entities and group exco's risk assessments in developing the group risk profile. Each entity addresses internal control issues as they arise and also dedicates (at least twice a year) to formally assess the internal control environment and risks. This ensures risks are mitigated at the appropriate levels of management throughout the group.

At least twice a year, executive management undertakes a rigorous strategic planning process, which includes the identification of risks and opportunities, as well as assigning responsibilities for mitigation, reporting and monitoring of risks. Risk mitigation strategies are integrated into strategic and operational activities, processes and policies of the group. Denel recognises the complexities of operating in a contract environment and has therefore implemented processes to manage programme risks throughout the contract lifecycle of pre-proposal, proposal, design, development and execution at each entity under the oversight of executive management. The programme manager's process is driven by high levels of project risk management.

The broad risk categories include financial, programme management, safety and environmental management and IT. An update is tabled at the A&R committee for discussion and review.

The integrated risk management model is illustrated below:



The board approves the group treasury and financial policies, as well as directives that govern financial risk management. Risks related to programme and contract execution are monitored and managed continuously by management through various forums at entity level, including formal programme review meetings. Risks related to human capital retention, development and transformation are managed through HR and Transformation forums at entities and group level.

Denel has adopted various management systems, ISO9001, ISO14001 and OHSAS18001, on which workplace, environmental management and product safety processes are based. IT risk is managed by means of the IT governance framework and policy, and managed at entity level and by the IT steering committee.

Denel continues to monitor macro-economic trends and specifically the movement of oil prices. The diversified markets have proven to be an effective mitigation strategy to falling oil prices.

The group's top risks that could have a material impact on Denel's business are detailed below, including the relevant key success factors, impact, affected stakeholders, opportunities and mitigations. The mitigations have been implemented and are duly monitored by both the board and the exco.

RISK DESCRIPTION	KEY SUCCESS FACTORS	IMPACT(S)	AFFECTED STAKEHOLDERS	OPPORTUNITIES	MITIGATIONS
Slippages in programme delivery time-lines resulting in cost overruns and negative cash flows	» Improved project management capacity » Optimal inventory management » Effective, quality and timeous sub-contractor delivery » Effective contracts management	» Working capital » Penalties » Cost overruns » Customer reaction	» Customers » Sub-contractors » Material suppliers » Employees	» Streamlining project management and product development processes » Strengthening collaborations between sub-contractors, suppliers and programme management. » Improving working capital management » Leveraging procurement to improve supply chain efficiencies	» Prioritising high risk programmes for evaluation and monitoring of project specific risk » Increased monitoring of subcontractor and suppliers performance and quality » Inculcating effective project management culture of effective procurement and management of inventory » Improving feedback loop and close cooperation with customers
Solvency and liquidity (funding for new large contracts, cash flow	» Positive cash from operations » Optimal working capital » Optimal debt levels	» Funding for large contracts » Working capital requirements » Debt levels	» Customers » Sub-contractors » Material suppliers » Funders	» Seek alternative sources of funding » Improve programme deliveries to improve cash positions contracting » Debt restructuring to improve solvency	» Rationalisation of the organisation to improve profitability » Improving programme management to ensure optimal working capital. » Investing appropriate funding model for programme
Order cover trend: Order book growth falling behind growing revenue	» Order book growth consistent with revenue growth » Strong order book across the portfolio » Strong and effective marketing strategy	» Growth and profitability » Cost structure	» Sub-contractors » Material suppliers	» Reviewing business model for profitability	» Implementation and monitoring of marketing campaigns » Increased coordination of marketing efforts » Continuous improvement of competitiveness across the organisation
Supply chain management processes and practices impacting delivery and efficiency	» Sourcing » Execution » Transportation » Storage	» Schedule » Quality and cost » Reputation » Business interruption » Transformation	» Customer » Programme office » Regulators	» Improve organisational performance across the value chain » Reducing supply chain cost » Optimal allocation of risk along the value chain	» Implementing a supply chain strategy that entails optimal sourcing, value for money, transformation and ethics » Creating awareness among supply chain professionals across the organisation

RISK DESCRIPTION	KEY SUCCESS FACTORS	IMPACT(S)	AFFECTED STAKEHOLDERS	OPPORTUNITIES	MITIGATIONS
Legal and regulatory developments Not complying with legal, regulatory requirements, codes and standards	» Litigations » Penalties » Prosecution » Reputation	Compliance: » Trading licenses » Regulations and permit requirements » Statutory obligations » Company policies	» Suppliers » Customers » Regulators » Shareholder	» Strengthen relations with regulators	» Implementing Ethics and Business Conduct policy across the group » Continuous review of new and updated laws/ regulations and standards » Reviewing, updating and communication of policies to ensure compliance » Constant liaison with specific regulators
Onerous conditions on contracts (tight delivery time-lines, high risk, late placement)	» Mutually beneficiary contract » Optimal risk allocation	» Working capital » Penalties » Cost overruns » Customer reaction	» Suppliers » Customers » Regulators	» Improve contracting and contract management » Optimal allocation of risk along the value chain	» Rigorous monitoring of contracts » Prioritising high risk programmes for evaluation and monitoring of project specific risk
Prospecting / exploration for minerals, gas and oil on Denel facilities impacting Denel capacity to meet its mandate	» Facility availability	» Production » Testing » Qualification	» Suppliers » Customers » Employees		» Opposing the action in terms of the applicable law
Reducing defence budget attracting more competitors in Denel's traditional markets	» >1% of GDP expenditure in defence locally	» Order cover » Competition	» Suppliers » Customers » Employees	» Improve competitiveness » Diversification of the portfolio » Diversification of markets	» Improving efficiencies for competitiveness » Diversification outside the traditional defence markets and products
Critical skills attraction and retention	» Skilled and motivated employees » Critical skills and talent retention » Transformed work environment	» Quality of workforce » Nature and level of skills and climate » EE » Labour turnover	» Employees » Organised labour » Shareholder	» Transformed workforce and climate	» Implementing transformation programme which includes improving organisational climate and retention » Regularly assessing effectiveness of plans to determine impact

PART 4

PERFORMANCE REVIEW

GROUP CHIEF EXECUTIVE OFFICER'S REPORT

Denel continues to perform well in a challenging period for the global defence and technology sectors. We remain committed to our primary mandate to serve the South African defence and security forces while playing an ever-increasing role in support of government's transformation and developmental priorities.

The past year has seen much progress in the restructuring of Denel's business through the consolidation of our aerospace entities and the extension of our capabilities. This also applies to areas that represent the future of defence technology – most notably cybersecurity, command and control and such areas as defined by the Defence Review 2015 where South Africa requires sovereign security capabilities.

Thus, while we maintain – and strengthen – our traditional capabilities in artillery, motorised infantry, munitions and precision-guided weapons, Denel is increasingly expanding its horizons into areas that require the utilisation of 21st century technology and solutions to meet the demands of a modern defence force.

Throughout our history, Denel has demonstrated that it has the agility to identify trends and to position itself to respond to opportunities that might arise. We will increasingly look for partnerships within the local defence and research communities, but also internationally where we can benefit from global expertise to penetrate new markets.

More than 60% of our revenue is already derived from exports and our future business outlook is bolstered by a strong order pipeline in excess of R40m.

Going forward our strategy to create value for our shareholder and the people of South Africa who regard Denel as a valuable asset will be guided by:

- Improved customer and stakeholder relationships in support of strong long-term business prospects;
- Efficiency, productivity and profitability;
- Enhanced capabilities and innovation; and
- The creation of a dynamic and vibrant organisation.

GROWING THE BUSINESS AND ORDER PIPELINE

The successful hosting of the Africa Aerospace and Defence exhibition AAD2016 once again demonstrated the vibrancy of the South African defence industry. Denel was a major exhibitor at the two-day trade show and also attracted significant numbers of visitors during the open days.

During AAD2016 Denel announced a new collaboration with China's leading state-owned defence supplier, Poly Technologies Inc., to collaborate in the local maritime sector. The agreements cover areas such as ship repairs, ship building, naval systems and maritime services.

Prior to the start of AAD2016 the Minister of Defence and Military Veterans, Ms Nosiviwe Mapisa-Nqakula, announced that Denel Maritime will take over the management of the naval dockyards in Simon's Town and Durban. This gives Denel a strong foothold in the naval environment and I am confident that it will become a catalyst for our participation in a number of maritime acquisition programmes that are currently in the pipeline.

The launch of the Africa Truck at AAD2016 emphasised Denel's ability to deliver products that are designed to meet the unique requirements of the SANDF in its deployment during peacekeeping operations on the continent. This is a uniquely South African product where the entire truck and all its components will eventually be designed, industrialised, manufactured and rolled out from local facilities using local expertise, local technology, local material and local labour.

The Africa Truck is a truly national project around which South Africans can unite and be proud of and which can contribute to our strategic national objectives of job creation, industrialisation, localisation and transformation.

Denel Land Systems also unveiled a collection of new infantry weapons that have been added to its range of products. This includes a light-weight machine gun and infantry mortar that meet the specialised needs of quick-reaction forces.

During the year Denel also maintained a strong presence at a number of international and regional exhibitions, most notably IDEX2017 in Abu Dhabi and the Defence Services Asia exhibition in Malaysia.

The Middle East and Asia-Pacific regions are key export targets for Denel and we are making great progress to extend our footprint in these vital markets. Denel Vehicle Systems (Pty) Ltd has successfully delivered N34 4x4 vehicles to a customer in the United Arab Emirates and received further orders for RG12 and RG31 mine-resistant vehicles.

Moreover, LMT Holdings SOC Ltd (RF) will complete delivery of its LM13 multi-purpose combat vehicle to clients in the Middle East and Asia, and received an order from a client in Africa to supply LM5 armoured personnel carriers.

The Badger infantry combat vehicle is one of Denel's flagship projects and we remain on track to start with full-scale production before the end of the 2017 calendar year.

The new generation Casspir vehicle continues to generate great interest and Mechem has successfully executed the delivery of 25 mine protected vehicles to the Angolan armed forces.

> Throughout our history, Denel has demonstrated that it has the agility to identify trends and to position itself to respond to opportunities that might arise. We will increasingly look for partnerships within the local defence and research communities, but also internationally where we can benefit from global expertise to penetrate new markets.

EFFICIENCY, PRODUCTIVITY AND PROFITABILITY

During the past year we completed the consolidation of all Denel's aviation-related businesses at the Kempton Park campus. The establishment of Denel Aeronautics as a new entity demonstrates our commitment to improve efficiency and productivity and to optimise our cost structures through operational excellence.

Denel Aeronautics is, without a doubt, the leading aerospace company in Africa and is a powerhouse in design, manufacturing and MRO solutions – maintenance, repair and overhaul – to both the military and commercial sectors on the continent. We continue to deliver on our commitments to the A400M programme and we recently completed the 67th consecutive on-time completion of the top shells that are fitted on to the world's most advanced military airlifter.

While our relationship with Airbus remains strong on both the manufacturing and MRO sides of the business we are also building strategic relationships with other global aerospace companies. We are confident that this will lead to new business opportunities and revenue diversification.

Denel has also grown its footprint in the aviation sector with the full acquisition of Turbomeca Africa (TMA). The Competition Commission has given its approval for this transaction subject to certain human capital conditions. TMA manufactures engine components – including gears, gearbox casings, shafts and couplings – for Safran Helicopter Engines. The company supports 40 customers in 20 countries, including the SA Air Force, the SA Police Services and a number of civilian air operators.

ENHANCED CAPABILITIES AND INNOVATION

Denel welcomes the challenge to be at the cutting edge of innovation in the defence and technology sectors. Already we can meet many of South Africa's defence requirements in land, sea and air, and in the past year we have expanded our capabilities into the cyberspace environment. Cyber terrorism is the fastest growing threat to our national security and economic interests. More than 60 countries around the world have already developed cyber-weapons for offensive or defensive purposes.

Denel S3 represents a major advance to combine the capabilities, skills and research accumulated within Denel into a comprehensive solution that is available to the state. Through Denel S3 we will expand our capabilities as the preferred and trusted sovereign technology partner and make significant contributions to the promotion of peace and safety and the protection of South Africa's territorial integrity and constitutional order.

The establishment of the DTC[3] was an important step to strengthen South Africa's sovereign capabilities in critical areas and stimulate the growth of research and development in highly-specialised sectors.

We have signed a ground-breaking agreement with the CSIR to conduct joint research and development, share our intellectual property and pool our marketing skills in the defence and technology arenas. The joint steering committee established by this agreement will identify specific projects for collaboration in fields as diverse as cybersecurity, command and control, laser technology, advanced manufacturing and space engineering.

Our partnership with the CSIR have already resulted in the development of local technology to detect illegal fishing in South Africa's coastal waters and the unauthorised dumping of waste oil into the ocean. The SeaFAR technology is a major contribution to the broader national objectives to grow the country's ocean economy through Operation Phakisa. Similar collaboration with the CSIR and ARMSCOR has produced the C-more system, a new software platform that will provide the security sector with improved real-time situational awareness with wide applications in the defence, crime prevention and border management environments.

In the past year we strengthened the capabilities of the ground-based air defence system (GBADS) that acts as a defensive shield against the use of air power by opposing forces. The Cheetah C-RAM system was jointly developed by Denel Dynamics and our associated company, Rheinmetall Denel Munition, and has the capacity to protect forces against the light artillery weapons increasingly used by irregular forces and militias.

Denel has ongoing discussions with the South African Air Force and the Department of Defence on the upgrading of the current Rooivalk Mk1F fleet. The world-class capabilities of this combat helicopter have strengthened Denel's reputation as a globally respected defence manufacturer and continue to give our forces unrivalled levels of protection, mobility and firepower.

ARMSCOR has placed an order with Denel to undertake a study on future supportability of the Rooivalk Mk1 and possible obsolescence. In addition, we are looking at options for the development of a new Rooivalk Mk2. Such a programme will require strong intergovernmental support and might lead to greater collaboration with international partners.

Denel's technology and expertise extends beyond the immediate confines of the defence environment. The scope of capabilities accumulated within the group is increasingly available to agencies, companies and entities that require solutions to address issues that confront broader civil society. Thus, the proven Mechem Explosives and Drug Detection System (MEDDS) developed by Denel to detect landmines and explosives in post-conflict scenarios can now be utilised with great success in the national efforts to combat rhino poaching and ivory smuggling. The MEDDS system combines modern technology with the unique abilities of Mechem trained sniffer dogs to detect a wide range of contraband and substances at airports, border posts and within our national parks system.

CREATION OF A DYNAMIC AND VIBRANT ORGANISATION

As a state-owned enterprise Denel shares government's objectives for the transformation of the economy, job creation and skills development. Through internships, learnerships and bursaries Denel makes significant contributions towards the development of critical and scarce skills in the country. The DTA was established as a hub for the training of artisans in the aviation sector, but continues to extend its reach to serve the broader engineering and manufacturing sectors.

Through various initiatives we create opportunities for young employees at Denel to extend their horizons and participate in breakthrough initiatives that also contribute to the reputation of the company as a leading innovator.

The SARA project is a collaboration between young engineers at Denel and post-graduate students at various universities to develop a Small African Regional Aircraft that can serve regional destinations not covered by major airlines. A full-scale model of the SARA made its debut at the Denel pavilion at AAD2016. Similarly, young engineers at Denel Land Systems responded to the need in the market for a lighter general-purpose machine gun used by infantry soldiers. The DMG-5 team developed a product with excellent export potential and their efforts were recognised by Denel when they were awarded the annual Rooivalk Group CEO Award for Excellence.

Younger employees at Denel participate in mentorship programmes to ensure they follow career paths that are best-suited to their individual skills. In partnership with the Henley Business School, the Denel Trailblazers programme offers formal leadership development to employees from junior to executive levels. During the past year some 84 employees successfully participated in the programme.

We have met our target to spend 3% (R68m) of our annual personnel cost on employee skills development and have also put in place a structured succession plan to ensure the future growth and sustainability of the organisation. Black employees comprise 62% of the Denel workforce and female representation has grown from 23% two years ago to 26%. During the past year 84% of new appointments came from ACI communities and more than 50% were female.

We place a high premium on national socio-economic imperatives, including transformation and skills development. In the past year we allocated more than R7.2m to our flagship corporate social investment project, the Schools Outreach Programme. This programme provides maths and science tuition to learners in historically disadvantaged areas. It has now been extended to six provinces with the Eastern Cape, Limpopo and KwaZulu-Natal added to our initial focus on Gauteng, Mpumalanga and the North West.

APPRECIATION

The board of Denel, chaired by Mr Daniel Mantsha, is playing a significant role in the success of our business and provides strategic leadership and oversight.

I want to express my appreciation to the leadership of our shareholder, the Department of Public Enterprises, as well as the DoD&MV, our partners and colleagues in the SANDF and ARMSCOR for their ongoing support.

A special word of appreciation also goes to the executive leadership team of Denel and our employees across all our campuses. The continued success of Denel will depend on the contributions made by our most important assets – the almost 5 000 men and women who make up the core of our business.

Zwelakhe Ntshepe
Acting Group Chief Executive Officer

OPERATIONAL REVIEW








DENEL AEROSTRUCTURES

Denel Aerostructures (DAe) is the leading aerospace company in Africa, a powerhouse in aerospace design and manufacturing for the military and commercial aviation sectors. As a strategic partner in global programmes the company continues to build on its long-standing reputation for innovation, quality and specialised solutions in aerospace design and manufacturing. DAe uses advanced manufacturing technologies to design and produce complex composite and metallic aircraft structures, which it supplies to OEMs and other aerostructure suppliers.

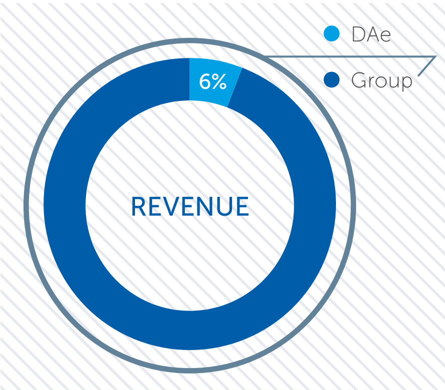
MAIN ACTIVITIES, INCLUDING KEY PRODUCTS AND SERVICES

- The design, development, manufacture, supply and support activities of the Airbus A400M wing-to-fuselage fairing (WFF) and top shells (TS) structural assemblies. In addition to these design-to-build work packages, DAe was also awarded the build-to-print work packages of the ribs, spars and sword (RSS) for the vertical tail fin and ISO-locks and central guide vertical restraint system (CGVR) for the cargo hold system of the aircraft;
- The manufacture of winglets for a North American business jet and sub-assemblies for the secondary structure of the Airbus A350-1000 pylon;
- Collaborative research with partners such as the Department of Trade and Industry (the dti), Aerospace Industry Support Initiative (AISI), the CSIR and Airbus; and
- Providing engineering support to other Denel entities, such as engineering support on the Rooivalk combat support helicopter programme, design support on the Seeker 400 UAVS and Hoefyster.

KEY HIGHLIGHTS AND ACHIEVEMENTS

- Performance of the top shells programme celebrated its 67th consecutive on-time completion. All non-A400M programmes remain on track barring the Winglet programme;
- The development of a strategic relationship with Boeing is maturing in pursuit of new business opportunities and revenue diversification. In this regard, DAe was invited to a Boeing bidders conference where a restructured Boeing supply chain moving from having finished parts suppliers, towards developing focused factories for manufacturing and assembly was launched by Boeing; and
- There is progress in positioning the SARA within the national government stakeholder environment. The plan is to endorse SARA as a National Flagship Programme. There is already expressed interest to participate in the programme by sister state-owned companies.

CONTRIBUTION TO GROUP REVENUE 2016/17



	2016/17 Rm	2015/16 Rm	Var %
Revenue	553	621	(11)
Export revenue	538	583	(8)
EBIT	(7)	7	(200)

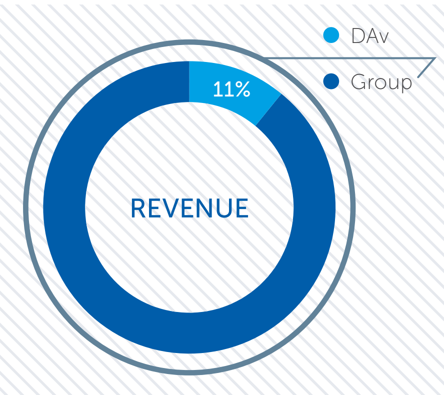
440 employees

B-BBEE LEVEL 4

DENEL AVIATION

The OEM of the Rooivalk combat support helicopter, Denel Aviation (DAv) is also the design authority of the Oryx medium transport helicopter and the Cheetah multi-role fighter aircraft. DAv is an accredited and certified provider of aircraft MRO solutions (including upgrades and systems integration) for both fixed and rotary wing aircraft, associated components and ground support equipment. DAv through the DTA provides apprenticeship training in several trades from general engineering trades to advanced aircraft type training.

CONTRIBUTION TO GROUP REVENUE 2016/17



	2016/17 Rm	2015/16 Rm	Var %
Revenue	1 092	1 407	(22)
Export revenue	365	275	33
EBIT	90	89	(90)

MAIN ACTIVITIES, INCLUDING KEY PRODUCTS AND SERVICES

» Rooivalk OEM, Oryx and Cheetah design authority and comprehensive MRO, engineering and flight test services, upgrade solutions, systems integration, certification and continued airworthiness support;

» Accredited MRO service centre for Airbus Helicopters Super Puma AS332, Puma SA330 and Bo105 helicopters;

» Primary MRO service provider for the SAAF Oryx and Rooivalk helicopters with responsibility for continued aircraft airworthiness;

» Accredited Lockheed Martin Hercules Service Centre for C-130 and L-100 aircraft with a sound and well-positioned infrastructure offering a wide range of MRO services for both transport and tactical fixed-wing aircraft, including the Cheetah and Mirage fighter aircraft platforms;

» Accredited Airbus Helicopters dynamic component repair and overhaul centre for depot-level maintenance for Puma and Super Puma helicopters, including depot level maintenance for avionics, electrical, oxygen and hydro-mechanical components. The facility is also accredited by the South African National Accreditation System (SANAS) to carry out repairs and calibration of ground support and test equipment;

» Through the DTA, Denel provides advanced and type training, as well as apprenticeship training for the aerospace, engineering and defence industries;

» Accredited MRO centre for Russian Helicopters in Africa for the Mi-8 and Mi-17 variants of helicopters;

» Approved by the South African Civil Aviation Authority (SACAA), the European Aviation Safety Agency (EASA) as an approved Aircraft Maintenance Organisation (AMO) for civil registered aircraft and components;

» Certified to the AS9100C, Aerospace Standard and ISO9001:2008, Standard by Bureau Veritas International; and

» Certified by the South African Bureau of Standards (SABS) to the OHSAS 18001 safety standard and ISO14001, Environmental Standards.

KEY HIGHLIGHTS AND ACHIEVEMENTS

» An order for a System Engineering Study was received from ARMSCOR and executed during 2016 relating to the obsolescence, concept requirement and programme metrics. The output of this contracted Systems Engineering Study will serve as an input to the User Requirement Specification (URS) for the Rooivalk Upgrade by ARMSCOR;

» Minister of DoD&MV, Hon Ms Mapisa-Nqakula, during AAD2016, confirmed government's support to engage with like-minded partner nations to co-develop and co-produce an upgraded Rooivalk platform;

» DAv continued to ensure availability of aircraft for the SAAF as primary customer and other defence forces both on the African continent and beyond, through its service offering;

» The contract to support Cheetah aircraft for a South American client was successfully concluded during the 2016/17 financial year. The client indicated that Denel's performance was exemplary; and

» The DTA continued to play a significant role in the Denel group achieving its skills development goals. Plans are also at an advanced stage in setting up a satellite campus in the North West province.

605 employees

B-BBEE **LEVEL 5**

DENEL DYNAMICS

As an innovation leader in advanced systems technology, Denel Dynamics (DD) has as its core business the design, development and manufacture of tactical missiles and precision-guided weapons. In similar fashion, it also offers competitive tactical UAVS and high-speed target systems, and develops satellite systems for the SA government through South African National Space Agency (SANSA).

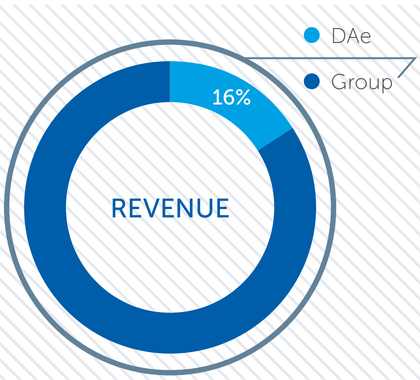
MAIN ACTIVITIES, INCLUDING KEY PRODUCTS AND SERVICES

- The renowned missile systems include the joint SA-Brazil 5th generation A-Darter air-to-air, the Umkhonto-IR air defence and the Ingwe and Mokopa anti-armour systems, as well as precision-guided munitions and the Umbani and Raptor II stand-off weapons. From the Ingwe system, the Ingwe portable launch system was successfully developed. DD has initiated the Marlin programme to demonstrate air-to-air beyond visual range (BVR) missile technologies, to be followed by a full development.
- In addition to the battle-proven Seeker 200 UAVS, newly qualified Seeker 400 UAVS and Skua high-speed target drone system, the small-sized Hungwe UAS for tactical requirements is currently under development.
- Denel's recently acquired Spaceteq develops space solutions to solve a number of real life challenges for national, as well as international clients. The product range includes an earth observation satellite system.
- The CIL addresses the knowledge gap between the company's ageing specialists and the growing population of young engineers and technologists. CIL develops graduate engineers by identifying real user requirements for new products and using the intern project as a vehicle for training and building technical skills and knowledge.

KEY HIGHLIGHTS AND ACHIEVEMENTS

- The A-Darter air-to-air missile's seeker performance qualification flight trials were successfully completed. Its critical design review was completed, thus finalising the design baseline for industrialisation and manufacturing.
- DD performed the BVR programmed flight test with the Marlin missile successfully launched at Denel OTR in July 2016. The main objective of the test was to prove safe launch of the missile from an aircraft platform, which also showed the missile airframe was stable. This test laid the foundation for captive and guided flight tests and for further technology development of the missile.
- A medium range, low-cost guided weapon flight test conducted for a client in early 2017 was successful, with the weapons released hitting the target within set specifications and the client expressing satisfaction with the weapon's performance.
- DD successfully concluded a long-range IIR guided weapon test, which showed exceptional accuracy of the system.
- On the heels of a programme contracted in September 2015, the short-range 140 kg precision-guided weapon was successfully air launched from the Seeker 200 test platform. The weapon was designed and developed in 18 months, with a programmed flight test in November 2016 and the successful initial guided flight test in March 2017.
- Final flight tests for Seeker 400 were successfully executed, in which the night operations capability and long-endurance capability were demonstrated.
- A contract to develop a laser imaging fuse was completed successfully ahead of schedule.
- Successful migration of the Spaceteq entity to the Houwteq facility, which affords improved capabilities and a rejuvenated workforce.
- Self-funded product development to the value of R22m was executed to enhance the DD product portfolio.
- Continued successful skills development through CIL that was established to accommodate bursary students into the business. In recent times the interns have built several potential projects that require investment to bring to fruition, including a sense and avoid system for a land vehicle navigating through obstacles, an intelligent grenade system, a tactical observation system for use by infantry soldiers to observe enemy positions in closed environments such as urban warfare, and an infrared dynamic scene generator.

CONTRIBUTION TO GROUP REVENUE 2016/17



	2016/17 Rm	2015/16 Rm	Var %
Revenue	1 672	1 821	(8)
Export revenue	1 016	1 242	(18)
EBIT	2	120	(98)

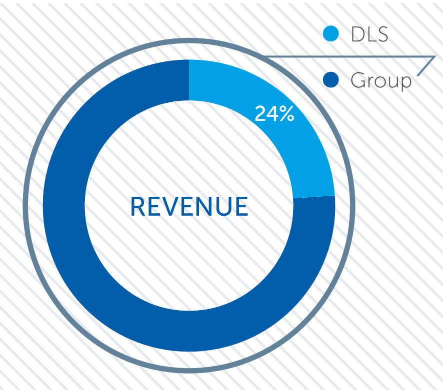
803 employees

B-BBEE **LEVEL 5**

DENEL LAND SYSTEMS

Denel Land Systems (DLS) is a leading project-based, consolidated systems designer and integrator of combat turrets, artillery and infantry systems, small arms and armoured vehicles. Part of DLS, the Mechem division is a global leader in solutions for a safer environment through the clearance of landmines and explosive remnants of war (ERW), as well as mine and ballistic-protected vehicle design and manufacture. Its customers include the United Nations (UN), other international agencies, governments and commercial customers worldwide.

CONTRIBUTION TO GROUP REVENUE 2016/17



	2016/17 Rm	2015/16 Rm	Var %
Revenue	2 675	2 603	3
Export revenue	1 955	1 761	11
EBIT	174	139	25

MAIN ACTIVITIES, INCLUDING KEY PRODUCTS AND SERVICES

» Technology and engineering capabilities for Level 5 systems, taking complex systems and products through entire lifecycle, providing product and logistic support, including qualification, maintenance, upgrades and decommissioning, as required;
» Development and industrialisation of the Badger family of new generation infantry combat vehicles (ICVs), under Project Hoefyster;
» International industrialisation capability with supply of infantry combat turrets as demonstrated with the AV8 programme;
» Artillery systems, combat turrets, armoured vehicle systems and rapid-fire small- and medium-calibre weapons. DLS provides a range of highly competitive, world-class products successfully marketed and delivered in key markets of interest;
» DLS has added a new arm to its combat systems capability with the GBADS product family;
» Mechem utilises a range of technologies, services and products in the ERW clearance applications that include manual demining, battle area clearance, stockpile destruction and explosive ordnance disposal, vehicle-mounted demining, mechanical demining, landmine surveys, range clearance, quality assurance and victim assistance;
» Design and manufacture of mine-protected vehicles (MPVs), e.g. Casspir range of vehicles; and
» Supply of canine technologies to private and government working dog institutions.

KEY HIGHLIGHTS AND ACHIEVEMENTS

» Successful client demonstration on the T5 artillery project, followed by three artillery platforms buy-off contract with the SANDF;
» Started industrialisation and production of the Badger fleet, which is progressing towards full-scale production in 2017;
» Achieved major milestones with AV8 programme with delivery to the client of LCT30 light combat turrets, anti-tank guided weapon turrets (ATGW) and remote controlled weapon station turret (RCWS) systems;
» Significant progress with the DLS management succession planning programme and human capital development, notably to develop and grow young engineering capability. Young artillery engineers formed an integral part of the core demonstration and engineering teams on the T5 and local artillery buy-off. DLS young engineers also spearheaded the technology progression and presentation of a lightweight SS-77 product called DMG-5 at AAD2016;
» Achieved a major contract milestone with the successful installation of a Military Image Interpretation Computer Systems (MIICS) and associated training system for the SAAF (Project Achilles) in the Joint Air Reconnaissance Intelligence Centre (JARIC) at AFB Waterkloof. This project has the main requirements for a Level 5 system, which include system engineering, command and control, secure communication infrastructure, Level 5 integrated logistic support, etc., which DLS is able to meet;
» Mechem cleared large tracts of land and roads of mines and other ERW through various demining or ERW clearing projects in several African countries;
» The new generation Casspir vehicle continues to generate interest and the UN has awarded six contracts to Mechem. Delivery of the first 25 Casspirs to the Angolan armed forces was successfully executed;
» Mechem expanded its field facility services to include engineering support in South Sudan and catering services for the UAE embassy in Mogadishu; and
» Successfully completed the SANParks canine contract. Mechem provided 16 trained dog teams to operate in the Kruger National Park, and currently also provides canine cargo detection services to many freight forwarders to two of South Africa's major international airports.

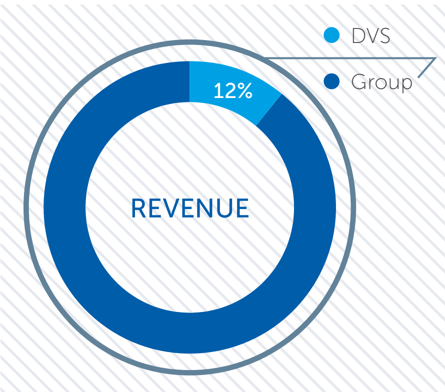
761 employees

B-BBEE LEVEL 6

DENEL VEHICLE SYSTEMS (PTY) LTD

Denel Vehicle Systems (DVS) is a subsidiary of Denel SOC Ltd, which provides turnkey vehicle systems to military and police customers in South Africa and in selected export markets. DVS has three divisions, i.e. Denel OMC, Denel Gear Ratio and Denel Mechatronics. DVS has close relationships with the SANDF, especially the SA Army, ARMSCOR and the SAPS, as well as with the NIMR and IGG companies in the UAE and several other local and international customers, suppliers and collaborators.

CONTRIBUTION TO GROUP REVENUE 2016/17



	2016/17 Rm	2015/16 Rm	Var %
Revenue	1 171	664	76
Export revenue	862	274	215
EBIT	110	90	22

MAIN ACTIVITIES, INCLUDING KEY PRODUCTS AND SERVICES

- Denel OMC designs, develops, manufactures, upgrades and supports a wide range of armoured vehicles, from combat vehicles to armoured patrol vehicles, including mine protected vehicles. Its product range comprises the RG12, RG21, RG31, RG32 vehicles, international product support (spares) and maintenance, as well as configuration control support to the SA Army's military vehicle fleet;
- Denel Gear Ratio manufactures power packs and driveline components, which encompasses a process of design, development, manufacture, assembly and testing, along with after-sales support; and
- Denel Mechatronics supplies fire directing systems and related fire control subsystems. Its offering encompasses a process of design, development, manufacturing and after-sales support. The product range includes advanced sights for combat systems, notably the Badger infantry combat vehicle, platform independent weapons subsystems, remote unmanned turrets incorporating the latest defence technologies, turret integration, electronics integration and unmanned aerial targets.

KEY HIGHLIGHTS AND ACHIEVEMENTS

- The successful delivery of pre-production N35 4x4 vehicles to a customer in the UAE with a number already deployed into theatre;
- Unveiling and launch of the Africa Truck demonstrator vehicle at AAD2016;
- Deliveries of RG32M mine-resistant light armoured vehicles to the Namibian armed forces have progressed well and are set to be completed early in the new financial year;
- Secured a first order for the new SDROW (self-defence remotely-operated weapon system) designed and developed by the Mechatronics division;
- Received an order from a customer in the UAE for the supply of the first prototype RG12 vehicle, with further opportunity to supply additional vehicles;
- Successfully delivered all required Bell transfer cases;
- Secured a follow-on order for the supply of nine RG31 vehicles to a customer in the UAE;
- Successfully developed and implemented a web-based supplier portal, in addition to continuous supplier and SMME development; and
- Maintained ISO and safety accreditation, and equipment renewal through capital investments and skills development through mentoring and training, along with succession planning to replace ageing workforce.

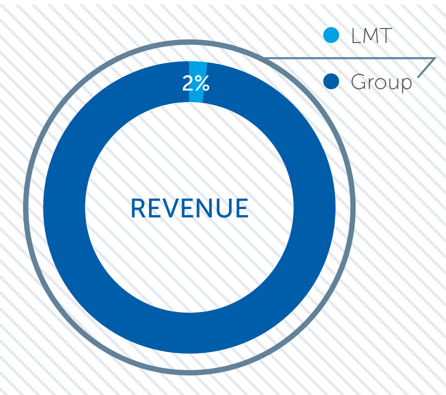
654 employees

B-BBEE **LEVEL 5**

LMT HOLDINGS SOC LTD (RF)

LMT Holdings SOC Ltd (RF) (LMT) specialises in the design and manufacture of armoured vehicles with protection against ballistic, landmine and improvised explosive devices (IEDs). Its design capabilities provide for integration of protection technologies into the armoured vehicles with, amongst others, flat or semi-flat floor landmine protection.

CONTRIBUTION TO GROUP REVENUE 2016/17



	2016/17 Rm	2015/16 Rm	Var %
Revenue	152	422	(64)
Export revenue	150	413	(64)
EBIT	(4)	45	(109)

MAIN ACTIVITIES, INCLUDING KEY PRODUCTS AND SERVICES

- LMT covers the complete value chain, from R&D, design, full-scale production to after-sales support and training. The product portfolio consists of armoured cabins and armoured containers to 4x4 armoured vehicles providing very high levels of ballistic, landmine and IED protection whilst still retaining exceptional on- and off-road mobility;
- Products in service are the LM5, LM8 and LM13 armoured vehicles, with the LM14 MRAP vehicle currently in development;
- Product development consists of a design centre and fully equipped prototype workshop to manufacture vehicles up to the product baseline; and
- Production capability includes full-scale hull fabrication and complete vehicle assembly.

KEY HIGHLIGHTS AND ACHIEVEMENTS

- Launched the new LM14 MRAP vehicle at AAD2016;
- Showcased the Meerkat system at AAD2016, designed to elevate and retract remote weapon stations from a vehicle;
- Successfully demonstrated the LM13 vehicle in Egypt;
- Continued the execution of the LM13 vehicle contract for a Middle East client, which is set to be completed within the next 12 months;
- Successful completion and delivery of the MLS system to a customer in Asia;
- Successfully completed the armoured ambulance development for a client in the Middle East, with production continuing;
- Received an order from a client in Africa for the supply of 14 LM5 APC vehicles over a two-year period. This is a significant step towards expansion into Africa;
- LMT developed and produced trailers for the 'Plofadder' landmine clearance system for a customer in the UAE;
- LMT produces components for the Badger infantry combat vehicle under sub-contract from DLS;
- Recertified as an ISO9001:2008 company; and
- Obtained OHSAS18001 certification.

204 employees

DENEL OVERBERG TEST RANGE

As one of the most versatile missile and aircraft test ranges anywhere, Denel OTR specialises in performance evaluation and verification services on in-flight systems. It provides support for the qualification of airborne systems, as well as validating the operational effectiveness of the military systems for SA's military-industrial users, international defence forces and armament industries.

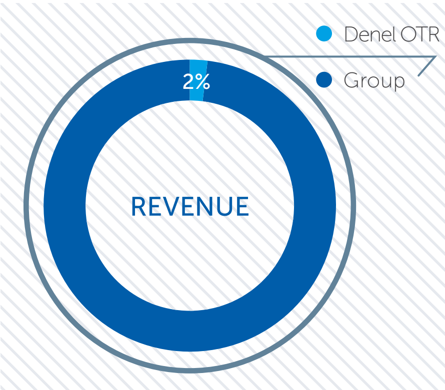
MAIN ACTIVITIES, INCLUDING KEY PRODUCTS AND SERVICES

- Flight testing of sophisticated missile, rocket, bomb and guided munitions systems;
- Evaluation and measurement of aircraft performance, avionic system evaluation, carriage and release clearance of ordnance and other payloads;
- Measurement of trajectories of all types of bombs, as well as other guided and unguided munitions;
- Execution of anti-tank tests, helicopter-based tests, and electronic warfare tests; and
- Mobile test range support services in remote locations.

KEY HIGHLIGHTS AND ACHIEVEMENTS

- Provided in-flight test services to the SANDF in terms of a multi-year contract;
- Successfully tendered for a new five-year contract with the DoD&MV to deliver in-flight test services up to 31 March 2022, the first time an order for a five-year period was placed. It will cover about 40% of Denel OTR's annual revenue for this period.
- Conducted tests for two established international clients, namely a ground-to-air defence test for an Air Force involving missiles fired at static and dynamic targets, and an air-to-ground test for a European air force in which stand-off missiles were released at various targets;
- Provided essential support to DD for various in-service and development tests;
- Continued with technology renewal programme focused on upgrading and maintaining capabilities to meet client requirements, including the complete refurbishment of a cinetheodolite instrument and procurement of various new high-speed video cameras and hardware interfaces;
- Completed various R&D projects, including developing the technology for a radio-controlled moving target with a range in excess of 10km. This target has already been successfully used in a recent test; and
- Maintained ISO9001:2008 and ISO14001:2004 certification, which underlines Denel OTR's commitment to quality service within environmental management principles.

CONTRIBUTION TO GROUP REVENUE 2016/17



	2016/17 Rm	2015/16 Rm	Var %
Revenue	137	116	18
Export revenue	43	37	16
EBIT	10	14	(29)

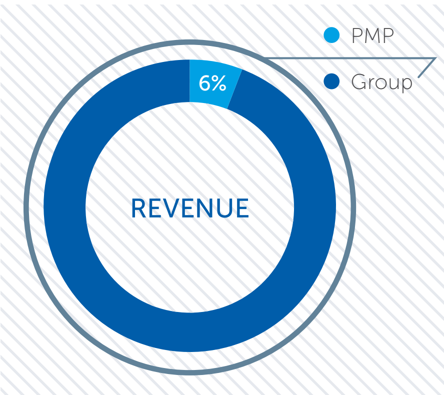
158 employees

B-BBEE LEVEL 4

PRETORIA METAL PRESSINGS

As an integrated manufacturer of small- and medium-calibre ammunition and technology related products and services, Pretoria Metal Pressings (PMP) serves military and commercial customers worldwide, including the SANDF, the SAPS and security agencies both locally and abroad. Its small- and medium-calibre ammunition is used by soldiers and police, on fighting vehicles, helicopters, fighter aircraft and navy vessels. The entity supplies handgun and rifle ammunition to the commercial sector, with its hunting ammunition acclaimed by local and international users. It also provides industry with mining drill bits and brass strip for various commercial applications.

CONTRIBUTION TO GROUP REVENUE 2016/17



	2016/17 Rm	2015/16 Rm	Var %
Revenue	583	503	16
Export revenue	158	179	(12)
EBIT	(44)	(61)	(28)

MAIN ACTIVITIES, INCLUDING KEY PRODUCTS AND SERVICES

» PMP's small calibre ammunition ranges from 5.56mm to 12.7mm and the medium calibre from 20mm to 35mm, all of which conform to international military standards;
» Percussion caps of all types, as well as links for various small- and medium-calibre rounds;
» Power cartridges, rocket motors and canopy fragilisation systems for the safe ejection of pilots from aircraft;
» Rock drill bits under the brand name Probit for the mining industry;
» Primary explosives and explosive products for commercial use in the private sector;
» PMP's non-ferrous foundry and rolling plant produces up to 80tons of brass strip daily. A major portion is used by PMP to manufacture ammunition, with the remainder of the brass strip sold in the local and international commercial market; and
» Hunting ammunition in the Pro-Amm, Standard, Super and African Elite ranges has a proud reputation for quality, accuracy and reliability in SA, as well as in the European and US markets.

KEY HIGHLIGHTS AND ACHIEVEMENTS

» The first demonstrator of the fully automatic 20x42mm iNkunzi Strike weapon system has been completed and undergoing functional tests. Further design improvements are intended to establish the baseline for finalisation of two weapons systems to be qualification units. The qualification phase for the weapon is expected to be completed by March 2018;
» Additional export orders for the iNkunzi PAW weapon system were received, showing the market's positive acceptance of this innovative system. This is further attested by increased enquiries for the PAW system;
» PMP prides itself on having produced the DTA's top achiever for 2016 in the person of Lesego Selemela. With an average of 96% for all her modules, she was rated the overall top student at the academy where she qualified as a millwright. PMP remains committed to the training of aspiring young engineers, technicians and artisans, with both on-the-job and theoretical training being given priority to ensure maximum outcomes for the business; and
» Whilst the proposed modernisation of PMP's manufacturing plant has been delayed due to funding constraints, installation of a modern 3D printer for "rapid prototype development" was implemented. With accuracy of the printed products within 0.17mm, this investment complements PMP's delivery of quality products. The technology makes it possible to identify certain design inadequacies before components are machined, thereby reducing valuable development time and costs. The system lends itself ideally to complex products that are costly to machine, once-off items and products of which the interface with other products needs to be confirmed before serial production is undertaken.

1 093 employees

B-BBEE LEVEL 4

FINANCIAL PERFORMANCE

Revenue **R8 057m**	
Local revenue	Export revenue
R2 970m	**R5 087m**
37%	63%

Net profit **R333m**		
Significant R&D investment	Forex loss	EBIT
R609m	**R232m**	**R628m**

EXTRACTS FROM THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

	GROUP		
	2016/17	2015/16	2014/15
	Rm	Rm	Rm
STATEMENTS OF COMPREHENSIVE INCOME			
Revenue	8 057	8 228	5 852
Gross profit	1 821	1 672	1 137
Other operating expenses	(1 483)	(1 455)	(939)
Share of profit in associated companies	154	132	64
EBIT	628	637	399
Net finance costs	(272)	(267)	(123)
Profit before tax	356	434	276
Net profit for the year	333	395	270
STATEMENTS OF FINANCIAL POSITION			
Cash and cash equivalents	2 021	2 003	1 909
Total assets	12 463	13 002	9 687
Equity	2 651	2 321	1 927
Borrowings	3 265	3 717	2 158
RATIOS			
Debt/equity ratio	1.2:1	1.6:1	1.1:1
Current asset ratio	1.4:1	1.6:1	1.7:1
EBIT %	8%	8%	7%

Revenue declined to R8bn (R2015/16: R8.2bn), the slight decrease in 2016/17 is primarily the result of budgetary constraints of the local clients. In order to mitigate the local economic constraints, Denel has intensified its sales to the export markets. Export revenue have increased by 7% to 63%, driven primarily by the Middle East and to a lesser extent Africa. Denel anticipates that this increase in the export market will continue to grow and the local revenue will increase as the Hoefyster production project matures.

The gross profit margins have improved by 2.28% to 22.6% in 2016/17 (2015/6: 20.3%). The improved margins arise from the non-core business entities. Increased cost pressures continue to negatively impact the operating margins as it reduces from 6.1% in 2015/16 to 5.9%.

Earnings before interest and taxation (EBIT) of R628m is 1% below prior year (2015/16: R637m). The earnings have been negatively affected by foreign exchange losses of R232m, mainly related to the revaluation of debtors and a weakening of the rand. Whilst this was in relation to projects that have been delayed, we are expecting final completion in 2017/18.

Denel reviewed the impairment of the intangible asset previously done in 2015/16 for R159m. Based on this review, management felt comfortable to reverse R72m of the previous impairment. Further details are disclosed on page 148 of the consolidated annual financial statements.

Total assets have decreased to R12.5bn (2015/16: R13bn), driven mainly by the decrease in trade and other receivables. The sale of the Phillipi site (R156m) occurred in 2017, as well as slight improvements on deliveries.

We have reduced interest-bearing debt by R452m (12%) to R3.3bn compared to March 2016.

CAPITAL MARKETS

Denel continues to receive support from the capital markets. Fitch Ratings has affirmed both of Denel's National Long-Term Rating and National Short-Term Rating as positive. The outlook for both ratings remains stable, with the National Long-Term Rating at 'AAA (zaf)' while the National Short-Term Rating is at 'F1+ (zaf). Fitch notes that the decision to affirm the ratings reflects the continuing strong links between Denel and the state – mainly driven by the government's irrevocable and unconditional guarantee for R1.85-billion of the group's R3bn DMTN. This guarantee expires on 30 September 2017 and we expect this to be renewed. The guarantees are essential for Denel to retain its rating. The Fitch Ratings report notes that Denel continues to deliver a strong top-line performance benefitting from organic growth. The maintained rating confirms to Denel that despite the national downgrade, the company is viewed as a positive investment.

FINANCIAL STRUCTURE AND LIQUIDITY

Denel has the R3bn DMTN programme registered with the JSE, which is updated on a regular basis to comply with JSE listing requirements. The DMTN programme allows for short- and long-term debt issuance to fund the company for the next five years. The debt consists of an R585m five-year corporate bond and short-term commercial paper of R1.265bn, which are issued for a 12-month, 18-month and a 3 to 6 month basis, as and when required. Unsecured debt issued under the DMTN programme amounts to R690m that matures in 2018.

Business operations are funded through a combination of cash generated, short- and medium-term bank credit facilities, corporate bonds and commercial paper. Denel has access to funding from various sources. The defence industry requires high upfront working capital investment, and this often places defence companies in a challenging position from a cash management point of view.

CASH

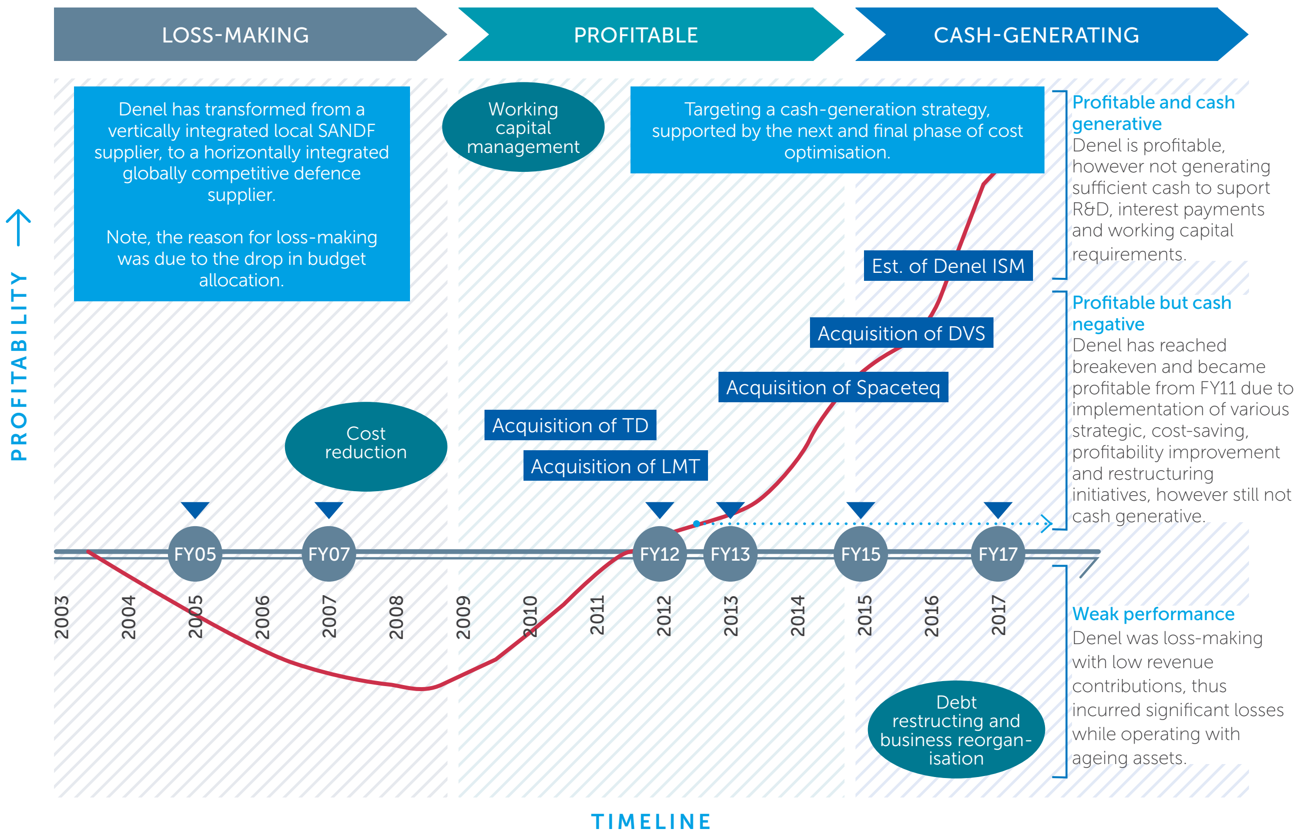
Cash generated from operations shows an improvement of R1.08bn in 2016/18. The contraction in revenue resulted in lower levels of trade receivables in the year whilst the net working capital impact was a positive R197m. As major contracts shifted to production and delivery in the year, this eased cash invested in stock in the prior year.

An increase in finance costs due to unplanned utilisation of borrowing facilities negatively affected the cash levels during the year. In order to mitigate the cash constraints, stringent capital spending was applied.

PERFORMANCE OVERVIEW

Profitability, cash generation and business sustainability			
Description	**Target**	**Achievement**	**2016/17 Outcomes and 2017/18 Outlook**
EBIT margin	5%	8%	Continued cost optimisation measures to improve profitability.
Cash generated from operations	>R685m	R376m	Strategic balance sheet management and effective working capital management. Obtain cost effective funding.

BUSINESS OUTLOOK



Denel's focus on revenue growth for the last five years has resulted in the turnaround of the business. The revenue has more than doubled in the last five years, which provides Denel with the critical mass to retain strategic and sovereign capabilities.

The highly competitive international landscape in a fast-changing advanced technology industry remains a challenge, which requires constant reinvention and review of business processes and strategies in order to remain relevant and competitive. In addition, Denel's high growth, with an already high debt to equity ratio, has put significant strain on our cash resources and the Denel business model. In the review of our business entities, our product portfolios, the international and local market, our business processes and cost structures, we have recognised that certain of our entities must be repositioned and that our cost structures require repositioning.

The next phase is to further improve profitability and cash generation to enable Denel to repay the debt and sustain growth. Management has identified a number of actions, including cost optimisation and business process improvements that will be executed in the next financial year.

TEN-YEAR REVIEW

AS AT 31 MARCH 2017

There have been significant improvements in Denel's financial performance since 2010/11. The following table illustrates the group's ten-year financial performance:

	2017 Rm	2016 Rm	2015 Rm	2014 Rm	2013 Rm	2012 Rm	2011 Rm	2010 Rm	2009 Rm	2008 Rm
CONSOLIDATED INCOME STATEMENTS										
Revenue	8 057	8 228	5 852	4 588	3 918	3 568	3 252	3 610	3 924	3 818
Gross profit	1 821	1 672	1137	899	826	862	503	578	639	600
Other operating expenses	(1 483)	(1 455)	(939)	(879)	(940)	(958)	(897)	(846)	(1 285)	(1 082)
Operating profit/(loss)	474	505	335	224	117	100	(314)	(162)	(463)	(233)
Net finance costs	(272)	(203)	(123)	(92)	(107)	(84)	(120)	(139)	(73)	(61)
Depreciation	(142)	(131)	(126)	(128)	(97)	(93)	(93)	(92)	(112)	(108)
Profit/(Loss) before taxation	356	434	276	190	82	49	110	(236)	(508)	(312)
Net profit/(loss) after taxation for the year from continuing operations	333	395	270	194	71	41	111	(246)	(533)	(321)
Income tax expense	(23)	(39)	(6)	4	(11)	(8)	1	(10)	(25)	(9)
Non-controlling interest in profit/(loss)	(12)	17	4	-	-	-	(47)	(65)	(91)	(13)
EBIT	628	637	399	282	189	133	230	(97)	(435)	(251)
Net profit/(loss) for the year	333	395	270	194	71	41	111	(246)	(533)	(347)
CONSOLIDATED STATEMENTS OF CASH FLOWS										
Net cash inflows/(outflows) from operations	376	(701)	281	474	(151)	360	178	(344)	(806)	72
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION										
Non-current assets	3 286	3 113	2 458	2 293	2 177	2 131	2 110	1 677	1 623	1 476
Current assets	9 177	9 733	7 145	5 712	4 497	3 420	2 921	3 343	3 107	3 607
Assets held for sale	-	156	84	84	104	91	7	-	9	58
Total assets	12 463	13 002	9 687	8 089	6 778	5 642	5 038	5 020	4 739	5 140
Current liabilities	6 513	6 212	4 094	2 484	2 465	3 659	3 704	3 671	3 446	3 081
Non-controlling interest	4	19	3	6	8	-	-	(34)	31	102
Non-current loans and borrowings	853	1 995	888	1 616	1 406	101	101	101	53	1
Current loans and borrowings	2 412	1 722	1 270	259	507	1 865	1 845	1 943	1 074	234
Total equity surplus	2 651	2 321	1 927	1 664	1 472	695	654	609	849	1 328

	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
	%	%	%	%	%	%	%	%	%	%
RETURNS %										
Gross profit to revenue	22.6	20.3	19.4	19.6	21.1	24.2	15.5	16.0	16.3	15.7
Other operating expenses to revenue	18.4	17.7	16.0	19.2	24.0	26.8	27.6	23.4	32.7	28.3
Operating profit/(loss) to revenue	5.9	6.1	5.7	4.9	3.0	2.8	(9.7)	(4.5)	(11.8)	(6.1)
Net profit/(loss) to revenue	4.1	4.8	4.6	4.2	1.8	1.1	3.4	(6.8)	(13.6)	(9.1)
Operating profit/(loss) to average total assets	3.7	4.5	3.8	3.0	1.9	1.9	(6.2)	(3.4)	(9.9)	(4.8)
Operating profit/(loss) to ordinary shareholders' interest [1]	19.1	23.8	18.7	14.3	10.8	14.8	(48.0)	(26.6)	(54.5)	(17.5)
RATIOS										
Debt/equity ratio	1.2	1.6	1.1	1.1	1.3	2.8	3.0	3.4	1.3	0.2
Current asset ratio	1.4	1.6	1.7	2.3	1.8	0.9	0.7	0.8	0.9	1.2
Net finance cost cover	1.3	2.1	2.2	2.1	0.8	0.7	1.2	(1.6)	(6.9)	(5.2)
Revenue per employee (Rm)	1.6	1.6	1.3	1.1	0.9	0.8	0.7	0.7	0.8	0.5
STATISTICS										
Number of shares in issue (million) [2]										
Class A ordinary shares	1 000	1 000	1 000	1 000	1 000	1 000	1 000	1 000	1 000	1 000
Class B ordinary shares	225	225	225	225	225	225	225	225	225	225
Total shares	1 225	1 225	1 225	1 225	1 225	1 225	1 225	1 225	1 225	1 225
Number of employees	4 941	5 114	4 559	4 136	4 219	4 716	4 716	5 090	5 067	7 276

1. *The ratio was calculated using the average ordinary shareholders' interest.*
2. *Refer note 19 of the notes to the consolidated annual financial statements, page 158.*

SHAREHOLDER'S COMPACT

KEY PERFORMANCE AREA	KEY PERFORMANCE INDICATOR	2016/17 TARGETS	2016/17 ACTUAL
Security of supply and retention of capabilities in areas required by the DoD&MV	Retained strategic capabilities in support of the DoD&MVs requirements as per register	100%	**100%**
Research and development	Research and development investment	8.5% of revenue limited to R740m	**R609m [1] (7.6%)**
Programme delivery	Achieving contracted cash flow targets on major programmes.	>85%	**96%**
	Achieving of cardinal milestones as contractually agreed by clients for selected major programmes	>85%	**86%**
Employment	Maintain employee numbers	Retention of jobs	**4 941 [2]**
Maximise the appointments from designated groups in order to address employment equity requirements	ACI as % of total appointments	80%	**84%**
	Women as % of total appointments	40%	**51%**
B-BBEE level	B-BBEE contributor level (new codes)	Level 5	**Level 4**
Preferential procurement and enterprise development (current baseline for women owned=1.3%)	Local content	70%	**76%**
	B-BBEE (% of recognised spend):	75%	**100%**
	Procurement from black-owned suppliers as % of local spend	25%	**27%**
	Black woman-owned as a % of total local spend	5%	**9%**
	Black youth-owned as a % of total local spend	1%	**1.60%**
	Spend on companies with ownership by persons with disabilities	0.2%	**0% [3]**
	Small and emerging enterprises suppliers developed	20	**73**
Corporate social investment	Total CSI spend	R3.5m	**R7.2m**
Training spend	% of personnel cost	3%	**3%**
Skills development - scarce and critical skills	Total number of engineering trainees (bursaries and internships)	50	**85**
	Total number artisan trainees	100	**177**
	Total number of DTA artisan (enrolments during the year Denel sponsored only)	85	**66 [4]**
Cash	Cash generated from operations, measured on a quarterly basis as budgeted	>R685m	**R380m [5]**
Order intake	Value of new orders to be concluded in 2016/17	≥R2bn	**R5.2m**
Profitability management	EBIT margin	5%	**8%**

1. *The R&D spend was below the target of 8,5% of revenue (R684m). The spend was affected by the cash constraints.*
2. *New appointments were placed on hold due to financial constraints.*
3. *The spend on companies with ownership of people with disabilities due to Denel's inability to identify the relevant companies for spend.*
4. *Additional recruitment placed on hold due to liquidity constraints.*
5. *Cash generated from operations was below target due to a delay on major contracts.*

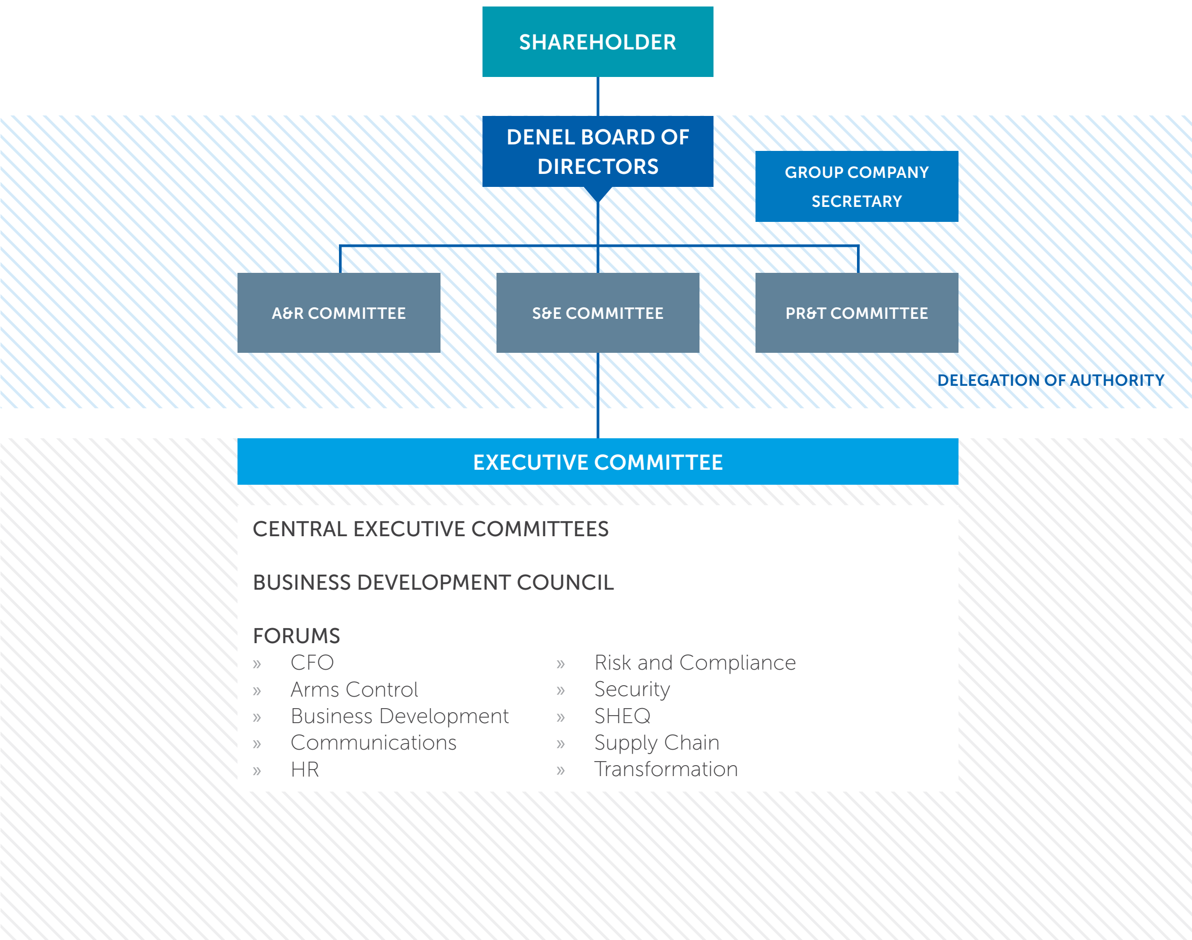
PART 5

HOW WE ARE GOVERNED

CORPORATE GOVERNANCE

As a state-owned company, Denel's sole shareholder is the South African government. The shareholder representative, in the person of the Minister of Public Enterprises, appoints a board of directors to oversee the functioning of the company's executive management. The organisation is in essence a group comprising entities, including subsidiaries, as well as associated companies in which Denel has shareholding of varying degrees.

The board commits itself to applying and enforcing the applicable corporate governance principles. It further recognises that sound corporate governance enhances the long-term sustainability of the company and provides assurance to its stakeholders that the company is well managed. Risk management and internal control systems are in place, which are designed in accordance with best practice and in compliance with King III report recommendations, as well as the governance requirements of the Companies Act. Denel adheres to the King III report on corporate governance. Following the launch of King IV, the company is in the process of implementing the principles of King IV.



DENEL BOARD OF
DIRECTORS

LUGISANI DANIEL MANTSHA (47)

BJuris, LLB

INDEPENDENT NON-EXECUTIVE DIRECTOR

Appointed to the board as chairman on 24 July 2015

DENEL BOARD COMMITTEE MEMBERSHIPS: Chairman of the board

VALUE ADD TO THE BOARD: Legal expertise and business leadership

ZWELAKHE NTSHEPE (60)

GROUP EXECUTIVE: ACTING GROUP CHIEF EXECUTIVE OFFICER

Post-graduate diploma (Management studies), MBA

DENEL BOARD COMMITTEE MEMBERSHIPS: Invitee to the board, audit and risk, personnel, remuneration and transformation and social and ethics committees

VALUE ADD TO THE BOARD: Business management, negotiation skills, marketing and business development

Appointed to the group executive committee in September 2003 and acting group chief executive officer with effect 24 September 2015

DIRECTOR'S ACTIVE MEMBERSHIP OF OTHER BOARDS:
Non-executive director
Rheinmetall Denel Munition (Pty) Ltd
LMT Holdings SOC Ltd (RF)

ODWA MHLWANA (40)

GROUP CHIEF FINANCIAL OFFICER

NDip (Internal auditing), BCompt, BCompt (Hons), CA (SA)

DENEL BOARD COMMITTEE MEMBERSHIPS: Invitee to the board, audit and risk, personnel, remuneration and transformation and social and ethics committees

VALUE ADD TO THE BOARD: Finance, auditing, management, corporate governance and strategy formulation

Appointed as group chief financial officer with effect 1 June 2017

DIRECTOR'S ACTIVE MEMBERSHIP OF OTHER BOARDS:
Executive director
Denel Vehicle Systems (Pty) Ltd
Mhlwana & Associates
Non-executive director
Rheinmetall Denel Munition (Pty) Ltd
Tawazun Dynamics LLC
LMT Holdings SOC Ltd (RF)

DENEL BOARD OF DIRECTORS

MPHO KGOMONGOE (42)

BCom

INDEPENDENT NON-EXECUTIVE DIRECTOR

Appointed to the board on 24 July 2015

DENEL BOARD COMMITTEE MEMBERSHIPS: Acting audit and risk committee chairperson

VALUE ADD TO THE BOARD: Auditing and risk management

PINKIE MAHLANGU (43)

BProc, Certificate (business rescue proceedings)

INDEPENDENT NON-EXECUTIVE DIRECTOR

Appointed to the board on 24 July 2015

DENEL BOARD COMMITTEE MEMBERSHIPS: Member of the personnel, remuneration and transformation and the social and ethics committees

VALUE ADD TO THE BOARD: Legal expertise

DIRECTOR'S ACTIVE MEMBERSHIP OF OTHER BOARDS:
Non-executive director
Aqua Emerald Investments (Pty) Ltd
Director
Bungela Trading and Projects SV
Mahlangu Inc Sole Proprietor: (PM)
Mahlangu Attorneys

THAMSANQA JUSTUS MSOMI (45)

BA (Law)

INDEPENDENT NON-EXECUTIVE DIRECTOR

Appointed to the board on 24 July 2015

DENEL BOARD COMMITTEE MEMBERSHIPS: Member of the audit and risk and the personnel, remuneration and transformation committees

VALUE ADD TO THE BOARD: Legal, policy development, implementation and execution and governance

DIRECTOR'S ACTIVE MEMBERSHIP OF OTHER BOARDS:
Executive director
Mpezama Consulting (Pty) Ltd (Dormant)

REFILOE MOKOENA (54)

BJuris, LLB

INDEPENDENT NON-EXECUTIVE DIRECTOR

Appointed to the board on 24 July 2015

DENEL BOARD COMMITTEE MEMBERSHIPS: Member of the social and ethics committee

VALUE ADD TO THE BOARD: Corporate compliance and regulatory

DIRECTOR'S ACTIVE MEMBERSHIP OF OTHER BOARDS:
Non-executive director
Road Accident Fund
Executive director
Morakana Minerals Development Strategists
Director
PRIREF
Right Play Trading 110 (Deregistration in process)
Bathopele Mining Investments (In the process of resigning)
Akani Aviation Leadership Initiative SA
Obaratile Aids Initiative (Deregistration in process)

THEMBA NKABINDE (63)

MBA, BMil, Project management programme

INDEPENDENT NON-EXECUTIVE DIRECTOR

Appointed to the board on 24 July 2015

DENEL BOARD COMMITTEE MEMBERSHIPS: Chairman of the personnel, remuneration and transformation committee

VALUE ADD TO THE BOARD: Industry knowledge, project management and business leadership

DIRECTOR'S ACTIVE MEMBERSHIP OF OTHER BOARDS:
Strategic equity partner
Aurecon
Director
B-CAT Military (Pty) Ltd
SA Intelligence Fire Fighting High Tech Co Ltd

KHUMBUDZO NTSHAVHENI (40)

MBA, BA (Hons) (Labour Relations), BA (Hons) (Development Studies), BA (Political Science)

INDEPENDENT NON-EXECUTIVE DIRECTOR

Appointed to the board on 24 July 2015

DENEL BOARD COMMITTEE MEMBERSHIPS: Chairperson of the social and ethics committee and member of the audit and risk committee

VALUE ADD TO THE BOARD: Governance, information communication technology (ICT), business and operational management

DIRECTOR'S ACTIVE MEMBERSHIP OF OTHER BOARDS:
Non-executive director
Limpopo Tourism Agency
Member
Nkho Trading CC
Trustee
Bokamoso BA Rona Investment Trust
Director
Fair Wheather Trading 504 (Pty) Ltd
GEN Y Tech (Pty) Ltd
Muro Energy (Pty) Ltd
National Student Leadership Academy
Phore Farms (Pty) Ltd
Value Chain Supermarkets (Pty) Ltd

Governance principles and the main duties of the board, under the leadership of the chairman; executive and non-executive directors and group chief executive officer (GCEO) are clearly documented in the board charter. Our board charter includes a schedule of matters reserved for the board and the terms of reference of the respective board committees. Our governance framework was developed to meet the group's strategic objectives and compliance requirements. At the same time, it balances the interests of stakeholders, and minimises and avoids conflicts of interest, whilst practicing good corporate behaviour. The board further delegated management accountability to the GCEO through the Delegation of Authority policy and performance contract.

As a SOC, the company enters into an annual shareholder's compact with the government of South Africa represented by the Minister of Public Enterprises. This contract sets out annual key performance company deliverables that cover but are not limited to social and economic drivers.

Although each of the group's subsidiary companies has a separate board of directors, the Denel board and its committees oversee all significant aspects and transactions of the subsidiaries. The subsidiaries are also governed by the limits of authority set by the board in the Delegation of Authority.

The board plays a critical role in strategy planning and establishes clear benchmarks to measure the company's performance. Sound corporate governance practices underlie our values, culture and processes. The group is managed in an efficient, accountable, transparent and ethical manner. This ethos is embedded in all the group's activities and thus Denel's governance framework goes beyond mere compliance with legislation.

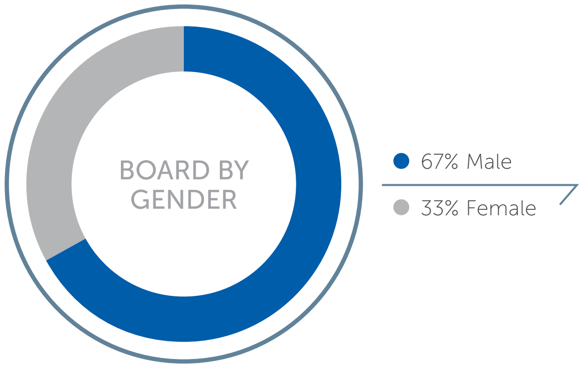
RESPONSIBILITY AND ACCOUNTABILITY

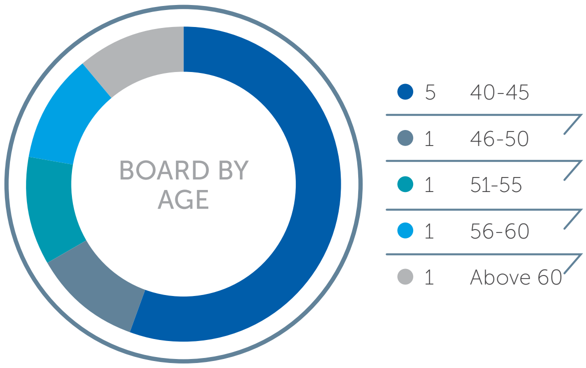
Our board provides leadership and strategic oversight, and specifically oversees the internal control environment to sustain value for the company's shareholder and stakeholders. The board ensures adherence to principles of good governance and accountability as espoused in its board charter and the King III report. All of the members of the board are individually and collectively aware of their responsibilities to the group's stakeholders and each director brings experience, independence and judgement.

The day-to-day governance of the group is the responsibility of Denel's management, which regularly reports to the board and its sub-committees. The board and respective committee chairpersons play an important role in addressing governance issues that arise from time to time. These board members have regular interactions with executive directors, senior management and other stakeholders.

COMPOSITION OF THE BOARD

The Denel group has a unitary board, comprising two executive directors, the GCEO and the GCFO, as well as seven non-executive directors. They all meet the board's independence criteria in terms of being free from any business relationship that could generally hamper their objectivity or judgement on the business and activities of the group. The company supports the principles of gender diversity at board level. Collectively, the board believes the current mix of knowledge, skill and experience meets the requirements to lead the company effectively.





APPOINTMENT AND RETIREMENT OF DIRECTORS

In terms of Denel's Memorandum of Incorporation (MOI), the shareholder appoints the chairman, GCEO and non-executive directors. The remaining executive director is appointed by the board with the approval of the shareholder.

Our shareholder reviews the composition of the board on an annual basis to ensure the rotation of directors at appropriate intervals and for the board to remain dynamic in its thinking and abilities. The term of office for the non-executive directors is a period of three years subject to annual review and confirmation by our shareholder at the AGM. Whilst retiring non-executive directors are eligible for re-appointment, director retirement is staggered to ensure continuity. Our executive directors comprise the GCEO and GCFO who are appointed on fixed-term contracts.

In the previous financial year, the GCEO and GCFO were placed on special leave pending the outcome of an investigation by the board. The matter has been resolved in that both the GCFO and GCEO have resigned on 30 August 2016 and 8 November 2016 respectively. The MOI stipulates that should an executive director be placed on suspension he or she may no longer be an executive director of the company and consequently, Messrs ZN Ntshepe and ZM Mhlwana have been Acting GCEO and Acting GCFO respectively since 24 September 2015 and attended to board matters in an ex-official capacity.

Ms N Mandindi and Mr NJ Motseki tendered their resignations from the board of directors with effect from 23 August 2016 and 16 January 2017 respectively.

FORMALISATION OF DIRECTOR APPOINTMENTS AND REMUNERATION

Our executives have contracts of employment with the company that are subject to Denel's conditions of service. Non-executive directors have their appointments formalised through a letter of appointment from our shareholder. The appointment letter indicates term of office of the non-executive directors, legislation governing their appointment, as well as information pertaining to their remuneration.

Remuneration for non-executive directors is based on the shareholder remuneration guidelines, approved by the shareholder representative and confirmed at the AGM. The shareholder approved a 4.6% increase in fees for non-executive directors at the AGM held on 23 August 2016. Non-executives receive a fee paid by Denel based on their attendance of meetings.

DIRECTORIAL INDEPENDENCE, EFFECTIVENESS AND PERFORMANCE EVALUATION

It is incumbent upon directors to act in the best interest of the company at all times as guided by the King III report, the Companies Act and best practice. Accordingly, the independence of individual non-executive directors is considered at every board meeting and evaluated annually by a firm of governance experts as part of the board's effectiveness review. Not only does this process create value for the group and its stakeholders, but it also ensures greater accountability. With a view to ensuring governance best practice is applied, a board effectiveness review was performed by an external service provider during the financial year. The following areas among others were identified for improvement:

- Additional skills set in risk management, IT and accounting (preferably a Chartered Accountant) should be presented at board level and;
- Expediting the filling of the three board of directors vacancies.

Action plans are being developed to address the gaps and engagements with the shareholder are ongoing with regards to filling of vacancies.

MANAGING CONFLICT OF INTEREST

The principle of effective management of conflicts of interest is paramount to limit risk and ensure transparency. Our board members declare their interests at each board and sub-committee meeting regarding any agenda item to prevent a director's personal interests taking precedence over those of the company. Directors' interests are declared by the individual directors in a register which is presented to our shareholder at every AGM for consideration. Moreover, the conflict of interest schedule has been enhanced significantly. Board members who have personal interests in a matter under discussion disclose their interests and recuse themselves from the meeting.

For the period under assessment no such conflict of interest was declared by our directors regarding agenda items tabled at either the board or committee meetings. A similar practice applies to all employees of the group.

BOARD INDUCTION AND SHARING OF INFORMATION

Given that Denel operates in a highly technical environment, a comprehensive induction for new directors assists them in acquiring a greater understanding of Denel's business operations, its range of products and services, as well as the manner in which these integrate into defence systems. As such, they need to appreciate the specific legislative framework applicable to the group as a defence manufacturer, as well as the business risks, governance processes and delegation of authority. It further implies that directors are continuously briefed on relevant new legislation and regulations. This year the board was updated on the key differences between, King III and King IV report of corporate governance. The board's focus will be the implementation of King IV with a view to fully comply by the end of 2018. The board members attended several defence exhibitions to further their knowledge of the defence industry.

For the directors to add value in their interactions with stakeholders, continuous training includes board meetings being held on a rotation basis at different entities. Not only does this allow board members an opportunity to interact with entity executives, but they also see operations in situ. By circulating quarterly reports to board members, they are kept abreast of developments outside of scheduled board meetings. Importantly, attendance at some of the defence exhibitions in which Denel participates, allows board members to have a first-hand experience of the global defence market, where the group's products and services compete with the best on offer.

GROUP COMPANY SECRETARY

With the group company secretary being responsible for developing systems and processes to enable the board to discharge its specific functions, Denel ensures significantly enhanced organisational efficiency. This function has the effect of limiting risk and improving accountability. As such, the group company secretary also advises the board on corporate governance issues, sets the annual plan for the board in conjunction with the chairman and monitors compliance with relevant legislation, including the Public Finance Management Act, no. 1 of 1999 (PFMA) and the Companies Act. The incumbent, to whom all directors have access for company-relevant services and guidance, further has the important function of keeping the board updated on any new relevant legislation.

BOARD MEETINGS

Meetings of the board are convened by formal notice as per annual schedule. The schedule is compiled by the group company secretary and approved by the board. Special meetings are convened as and when required to address specific material issues. Corporate governance, especially transparency and accountability, is enhanced with comprehensively compiled board documents submitted by the executive management.

KEY ISSUES CONSIDERED AND APPROVED/NOTED BY THE BOARD THIS YEAR:

COMMITTEE	RESPONSIBILITY	FOCUS FOR 2017/18
Board	During the 2016/17 financial year, the board fulfilled the following duties in accordance with its mandate: » Reviewed and approved the strategy and strategic objectives of Denel » Approved the group's revised Delegation of Authority » Set the tone of the group's values, including principles of ethical business practice and requirements of being a responsible corporate citizen » Confirmed that the group complies with all applicable laws and best corporate governance practice » Reviewed strategic partnerships and ensured their adherence to the applicable laws » Exercised independent, informed and effective judgement to bear on material decisions of the group companies » Reviewed and approved the integrated report and the consolidated annual financial statements for 2016/17 » Reviewed and approved the Shareholder's Compact for 2017/18 » Reviewed and approved the Corporate Plan for 2017/18 » Assessed the stability in executive management » Statement on performance management	» Delivery on strategy » Improvement on group liquidity » Supply chain » Transformation » Diversification of market and product portfolio

BOARD MEETING AND AGM ATTENDANCE FOR THE YEAR ENDING 31 MARCH 2017

BOARD MEMBER	BOARD MEETINGS										AGM
	Total	Special 28 Apr 16	Special 8 Jun 16	Special 8 Jun 16	Special 9 Jun 16	Special 23 Jun 16	26 Jul 16	27 Oct 16	Budget 30 Nov 16	24 Feb 17	23 Aug 16
Mr R Saloojee [1]	0/0	-	-	-	-	-	-	-	-	-	-
Mr F Mhlontlo [2]	0/0	-	-	-	-	-	-	-	-	-	-
Mr LD Mantsha (Chairman)	10/10	√	√	√	√	√	√	√	√	√	√
Ms M Kgomongoe	10/10	√	√	√	√	√	√	√	√	√	√
Mrs PM Mahlangu	10/10	√	√	√	√	√	√	√	√	√	√
Ms N Mandindi [3]	5/6	√	√	√	√	√	A	-	-	-	A
Ms R Mokoena	8/10	A	√	√	√	√	√	√	√	√	√
Mr NJ Motseki [4]	8/8	√	√	√	√	√	√	√	√	-	√
Mr TJ Msomi	9/10	√	√	√	√	√	A	√	√	√	√
Lt Gen TM Nkabinde (rtd)	9/10	√	√	√	√	√	√	√	√	√	√
Ms KPS Ntshavheni	8/10	A	A	√	√	√	√	√	√	√	√
Mr Z Ntshepe [5]	8/9	√	√	√	√	A	√	√	√	√	√
Mr Z Mhlwana [5]	9/9	√	√	√	√	√	√	√	√	√	√

A Apology
T Via telecon

1. Resigned from 8 November 2016
2. Resigned from 30 August 2016
3. Resigned from 23 August 2016 (accepted resignation at AGM)
4. Resigned from 16 January 2017
5. Acting from 24 September 2015

BOARD COMMITTEES

The board has delegated specific responsibilities to three standing sub-committees, namely the audit and risk (A&R) committee, the personnel remuneration and transformation (PR&T) committee and the social and ethics (S&E) committee. The board committees assist the directors to discharge their duties and ensure board effectiveness in discharging its duties. The A&R committees' terms of reference are set out in the board charter and are reviewed annually to limit risk and ensure they remain in line with relevant regulations, company requirements and best practice in corporate governance.

Whereas the A&R committee meets four times a year, in agreement with the company's MOI, the other board sub-committees meet at a minimum three times a year. Executives regularly attend the board sub-committee meetings in line with their roles and responsibilities.

Minutes of the sub-committee meetings, including the respective chairman reports, form an integral part of the board meeting documentation to keep the board abreast of the sub-committees' activities. Significant matters discussed at these sub-committee meetings are regularly submitted with recommendations to the board for the board to deliberate and decide.

AUDIT AND RISK COMMITTEE

The A&R committee, including its chairperson, comprises only independent non-executive directors, with the executive directors as standing invitees to the committee meetings. Members of the A&R committee have considerable expertise in various fields, notably also risk management and commercial and legal experience necessary to oversee and guide the board.

The A&R committee provides the following support to the group: the audit and risk function, corporate governance, the governance information technology (IT) and other business risk.

With a view to improve accountability and limiting risk, the appointment of members of the A&R committee is reconsidered and voted on at every AGM.

The A&R committee's terms of reference are reviewed and updated annually for relevant new legislation and best practice. The terms of reference include the A&R committee's mandate, which is to ensure the integrity of financial reporting, the adequacy of governance, soundness of the internal control environment and the robustness of risk management processes.

The A&R committee provides the following support activities to the board of directors:

- Reviews the integrated report, including the consolidated annual financial statements, and considering reports of the auditors on the consolidated annual financial statements;
- Reviews and assesses the risk control process and systems;
- Reviews the effectiveness of the company's internal controls;
- Considers matters emanating from the group's ethics hotline, planned management actions and the results of enquiries;
- Agreeing the scope of the auditors' work and their fees;
- Monitors the performance of the internal audit function;
- Considers the combined assurance model, assessing levels of assurance that is provided by auditors, regulators, management and other assurance providers;
- Considers treasury controls and related risk management processes; and
- IT governance.

COMMITTEE MEMBERS:
Ms M Kgomongoe (Acting Chairperson)
Ms KPS Ntshavheni
Mr TJ Msomi
1x vacancy

KEY ISSUES CONSIDERED AND RECOMMENDED TO THE BOARD/NOTED BY THE A&R COMMITTEE THIS YEAR:

COMMITTEE	RESPONSIBILITY	FOCUS FOR 2017/18
Audit and Risk	During the 2016/17 financial year, the A&R committee, amongst others focused on the following: » Reviewed and recommended for adoption to the board the consolidated annual financial statements and the integrated report for 2016/17. » Recommended to the board the insourcing of the internal audit function » Reviewed the reports from the internal and external auditors regarding the effectiveness of the internal control environment. » Monitored the appropriateness of the group's combined assurance model » Approved the external and internal audit plans » Reviewed of the quality and effectiveness of the external audit process » Reviewed the performance and expertise of the GCFO and overall finance function » Reviewed the going concern assertion as at 31 March 2017 » Reviewed the quarterly performance report before submission to the executive authority	» Implementation of King IV » External audit firm rotation » Strengthen supply chain and IT governance

A&R COMMITTEE MEETINGS ATTENDANCE FOR THE YEAR ENDING 31 MARCH 2017

MEMBERS	AUDIT AND RISK COMMITTEE MEETINGS				
	Total	Special 25 Apr 16	21 Jun 16	4 Oct 16	27 Jan 17
Ms M Kgomongoe (Interim Chairperson)	4/4	√	√	√	√
Mr TJ Msomi	4/4	√	√	√	√
Ms KPS Ntshavheni	4/4	√	√	√	√
STANDING INVITEES					
Mr R Saloojee [1]	0/0	-	-	-	-
Mr F Mhlontlo [2]	0/0	-	-	-	-
Mr Z Ntshepe [3]	1/4	√	A	A	A
Mr Z Mhlwana [3]	4/4	√	√	√	A
Mrs PM Mahlangu [4]	4/4	√	√	√	√

1. *Resigned from 8 November 2016*
2. *Resigned from 30 August 2016*
3. *Acting from 24 September 2015*
4. *Requested to attend meetings as from 1 February 2016 as observer*

A *Apology*

SOCIAL AND ETHICS COMMITTEE

Only independent non-executive directors serve on the S&E committee. This includes the chairman who is confirmed at every AGM. The executive directors are standing invitees to committee meetings and relevant exco members may attend the committee meetings by invitation. External experts as proposed in the regulations are appointed to the committee by the board, as and when necessary.

The S&E committee advises the board on good corporate citizenship and ethical relationships, reporting to the board and the shareholder on the group's commitment in this regard. The committee's terms of reference are reviewed and updated annually.

An annual work plan ensures that it meets all monitoring and reporting responsibilities within the annual cycle. A significant responsibility of the committee is to consider the group's corporate and social investment (CSI) programmes, transformation and enterprise development (ED) initiatives, occupational health and safety (OHS), stakeholder management and the ethics policy.

The S&E committee provides the following support activities to the board of directors:

- Evaluating policies and measures in place to prevent fraud and corruption;
- Reviewing the CSI strategies and progress thereon;
- Evaluating the stakeholder engagement model, monitoring the status and from time to time assessing effectiveness;
- Reviewing the transformation strategies, progress on initiatives and improvement plans; and
- Reviewing OHS policies and monitoring effectiveness.

COMMITTEE MEMBERS:
Ms KPS Ntshavheni (Chairperson)
Ms R Mokoena
Mr J Motseki (resigned from board on 16 January 2017)
Mrs P Mahlangu (appointed to the committee effective 1 March 2017)

KEY ISSUES CONSIDERED AND RECOMMENDED TO THE BOARD/NOTED BY THE S&E COMMITTEE THIS YEAR:

COMMITTEE	RESPONSIBILITY	FOCUS FOR 2017/18
Social and Ethics	During the 2016/17 financial year, the S&E committee, amongst others focused on the following: » Reviewed the Transformation Plan 2017 » Considered matters relating to the stakeholder management » Considered matters relating to group supply chain and transformation in particular B-BBEEE and ED » Considered matters relating to OHS and environmental management » Corporate social investments	» Stakeholder engagement particularly youth in the business » Ethics » Transformation objectives

S&E COMMITTEE MEETINGS ATTENDANCE FOR THE YEAR ENDING 31 MARCH 2017

MEMBERS	SOCIAL AND ETHICS COMMITTEE MEETING				
	Total	22 Jun 16	Joint with PR&T 6 Jul 16	6 Oct 16	15 Feb 17
Ms KPS Ntshavheni (Chairperson)	4/4	√	√	√	√
Ms R Mokoena	4/4	√	√	√	√
Mr NJ Motseki 1	3/3	√	√	√	-
STANDING INVITEES					
Mr R Saloojee 2	0/0	-	-	-	-
Mr F Mhlontlo 3	0/0	-	-	-	-
Mr Z Ntshepe 4	0/4	A	A	A	A
Mr Z Mhlwana 4	4/4	√	√	√	√
Mrs PM Mahlangu 5	2/3	√	√	A	-
INVITEES					
Lt Gen TM Nkabinde (rtd) (Chairman of PR&T)	1/1	-	√	-	-
Ms N Mandindi	0/1	-	A	-	-

1. *Resigned from 16 January 2017*
2. *Resigned from 8 November 2016*
3. *Resigned from 30 August 2016*
4. *Acting from 24 September 2015*
5. *Requested to attend meetings as from 1 June 2016 as observer*

A *Apology*

PERSONNEL, REMUNERATION AND TRANSFORMATION COMMITTEE

Denel's personnel, remuneration and transformation committee, referred to as the PR&T committee, comprises only independent non-executive directors. Its scope of responsibilities is detailed in the terms of reference, which are reviewed and approved annually by the board.

The PR&T committee gives assurance that remuneration arrangements with employees support the group's strategic objectives and enable the recruitment, motivation and retention of senior executives, whilst complying with the requirements of regulation.

The responsibilities of the PR&T committee include reviewing the design and management of Denel's remuneration and reward principles, policies and implementation strategies.

The PR&T committee provides the following support activities to the board of directors:

- Evaluating the performance of the executive management, and for setting appropriate remuneration;
- Overseeing the group's performance in respect of EE, transformation and employees development, taking into consideration the legal requirements and monitoring of targets set by the company; and
- Overseeing the skills development and retention of critical skills and talent.

For the sake of transparency and accountability, the performance of each executive is assessed relative to the prevailing business climate and market conditions, as well as key predetermined targets. In accordance with principles of good governance, executives being evaluated are recused from the meeting. Standing invitees to the committee's meetings include the two executive directors, the group executive: HR and Transformation, and any other executives whose roles and responsibilities are relevant to the matters under consideration.

COMMITTEE MEMBERS:
Lt Gen TM Nkabinde (Rtd) (Chairman)
Mrs PM Mahlangu
Ms N Mandindi (resigned from board on 23 August 2016)
Mr TJ Msomi (appointed to the PR&T committee effective 1 March 2017)

KEY ISSUES CONSIDERED AND RECOMMENDED TO THE BOARD/NOTED BY THE PR&T COMMITTEE THIS YEAR:

COMMITTEE	RESPONSIBILITY	FOCUS FOR 2017/18
Personnel, Remuneration and Transformation	During the 2016/7 financial year, the PR&T committee, amongst others focused on the following: » Considered the long-term incentive plan 2017 » Reviewed and recommended for adoption to the board the salary increase effective 1 April 2017 » Considered the retention strategy transformation and skills development » Considered HR policies	» Long-term incentive plan » Transformation improvements » Retention and skills development » Succession planning

PR&T COMMITTEE MEETINGS ATTENDANCE FOR THE YEAR ENDING 31 MARCH 2017

MEMBERS	PERSONNEL, REMUNERATION AND TRANSFORMATION COMMITTEE MEETINGS						
	Total	Special 25 Apr 16	23 Jun 16	Special 6 Jul 16	5 Oct 16	Special 14 Oct 16	9 Feb 17
Lt Gen TM Nkabinde (rtd) (Chairman)	6/6	√	√	√	√	√	√
Mrs PM Mahlangu	6/6	√	√	√	√	√	√
Ms N Mandindi	1/3	A	√	A	-	-	-
STANDING INVITEES							
Mr R Saloojee [1]	0/0	-	-	-	-	-	-
Mr F Mhlontlo [2]	0/0	-	-	-	-	-	-
Mr Z Ntshepe [3]	3/6	√	A	√	A	√	A
Mr Z Mhlwana [3]	3/6	√	A	A	√	A	√

1. *Resigned from 8 November 2016*
2. *Resigned from 30 August 2016*
3. *Acting from 24 September 2015*

A *Apology*

EXECUTIVE COMMITTEE

ZWELAKHE NTSHEPE (60)

ACTING GROUP CHIEF EXECUTIVE OFFICER

Post-graduate diploma (Management studies), MBA

DENEL BOARD COMMITTEE MEMBERSHIPS: Invitee to the board, audit and risk, personnel, remuneration and transformation and social and ethics committees

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Business management, negotiation skills, marketing and business development

Appointed as acting group chief executive officer with effect 24 September 2015

ODWA MHLWANA (40)

GROUP CHIEF FINANCIAL OFFICER

NDip (Internal auditing), BCompt, BCompt (Hons), CA (SA)

DENEL BOARD COMMITTEE MEMBERSHIPS: Invitee to the board, audit and risk, personnel, remuneration and transformation and social and ethics committees

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Finance, auditing, management, corporate governance and strategy formulation

Appointed as group chief financial officer with effect 1 Junes 2017

NATASHA DAVIES (45)

GROUP EXECUTIVE: HUMAN RESOURCES AND TRANSFORMATION

MCom (Business Management), BCur (Hons), Executive leadership programme

DENEL BOARD COMMITTEE MEMBERSHIPS: Permanent invitee to the personnel, remuneration and transformation and social and ethics committees

DIRECTORSHIPS: None

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership, business management, accomplished in all areas of the HR value chain, transformation and change management

Appointed to the group executive committee in July 2013

THEO KLEYNHANS (56)

GROUP EXECUTIVE: STRATEGY

BEng (Electronics), MBL, Executive leadership programme

DIRECTORSHIPS: Chairman of Denel Vehicle System (Pty) Ltd

Non-executive director of Pioneer Land Systems (LLC)

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Engineering, operations and business management and executive leadership

Appointed to the group executive committee in August 2017

MXOLISI MAKHATINI (45)

ACTING GROUP EXECUTIVE: BUSINESS DEVELOPMENT

BSc (Electronic Eng), NDip (Electrical Eng), MSAIEE

DIRECTORSHIPS: Former chairman of the AMD marketing workgroup

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Specialist experience in the design of control systems, manufacturing, programme and business management, business development and marketing

Appointed to the group executive committee in May 2016

THAMSANQA MBELE (49)

GROUP CHIEF OPERATIONS OFFICER

MBL, Masters in Engineering Management (MEM), attended various executive leadership programmes

DENEL BOARD COMMITTEE MEMBERSHIPS: Permanent invitee to audit and risk, personnel, and social and ethics committees

DIRECTORSHIPS: Non-executive director of Denel Areostructures SOC Ltd and Hensoldt Optronics (Pty) Ltd

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership, strategy and business management, programme management, operations management

Appointed to the group executive committee in April 2016

VUYELWA QINGA (53)

GROUP EXECUTIVE: COMMUNICATION AND PUBLIC AFFAIRS

BJournalism and media studies, Management development programme

DIRECTORSHIPS: Council member of UP, director of Cygniline (Pty) Ltd

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Strategic leadership, corporate communication, media relations, image and reputation management and stakeholder engagement

Appointed to the group executive committee in May 2013

VUYOKAZI XAXA (46)

GROUP COMPANY SECRETARY AND HEAD OF LEGAL

B.Iuris, LLB, post-graduate diploma in Cyberlaw, Executive Leadership Development Programme

DIRECTORSHIPS: Non-executive director of Centurion Aerospace Village

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: General law advisory, in particular corporate law, compliance, corporate governance. Business management, strategic leadership

Appointed to the group executive committee in June 2017

DENEL BUSINESS ENTITIES' CHIEF EXECUTIVE OFFICERS

STEPHAN BURGER (59)

CHIEF EXECUTIVE OFFICER: DENEL LAND SYSTEMS

BEng (Mechanical), Post-graduate qualification (System Engineering), Certificate (positive negotiations, finance and quality)

DIRECTORSHIPS: None

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership, business management, product development of defence systems, system integration, business development and general management

Appointed as chief executive officer in November 2004

ISMAIL DOCKRAT (47)

CHIEF EXECUTIVE OFFICER: DENEL INTEGRATED SYSTEMS AND MARITIME

MBA, NDip (Electronics Eng), Certificate (programme management)

DIRECTORSHIPS: Previous non-executive director of Denel Areostructures SOC Ltd and Turbomeca Africa (Pty) Ltd, CEO of Wesgro, GM at Trade and Investment South Africa

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Strategic leadership, business management, programme management and turnaround management

Appointed as chief executive officer in November 2014

MICHAEL KGOBE (48)

CHIEF EXECUTIVE OFFICER: DENEL AVIATION

Masters (Aeronautical maintenance and production management), Executive leadership programme

DIRECTORSHIPS: Non-executive director of Turbomeca Africa (Pty) Ltd

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Business management, engineering and project management

Appointed as chief executive officer in March 2010

TSEPO MONAHENG (53)

CHIEF EXECUTIVE OFFICER: DENEL DYNAMICS

BSc (Physics and Mathematics), BSc (Electronics Eng), MBA

DIRECTORSHIPS: None

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership, strategy, business development and programme management

Appointed as chief executive officer in May 2013

PHALADI PETJE (51)

CHIEF EXECUTIVE OFFICER: PRETORIA METAL PRESSINGS

BA (Hons) Economics, BEd, PDM (Bus Admin), Diploma (Management), Executive leadership programme

DIRECTORSHIPS: None

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Strategic planning, business development and business process re-engineering

Appointed as chief executive officer in May 2013

JOHAN STEYN (59)

CHIEF EXECUTIVE OFFICER: DENEL VEHICLE SYSTEMS (PTY) LTD

BEng Mech, BEng (Hons), MBA

DIRECTORSHIPS: Executive director of Denel Vehicle Systems (Pty) Ltd, former managing director of BAE Systems Land Systems South Africa (Pty) Ltd

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Strategic leadership, operations, programme management, product development of armoured vehicles, system integration, business development, global partnering and negotiations

Appointed as chief executive officer in January 2001

ABRIE VAN DER WALT (58)

CHIEF EXECUTIVE OFFICER: DENEL OVERBERG TEST RANGE

MSc (Computer Science), Executive leadership programme

DIRECTORSHIPS: None

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Business management and executive leadership experience

Appointed as chief executive officer in December 2005

RESIGNATIONS:

The following executives resigned in the current financial year period:
Dr S Nell - 29 August 2016
Mr Jan Wessels - 31 August 2016
Ms NF Msiza - 28 February 2017

The Denel group executive committee (exco) is chaired by the GCEO and in keeping with connectivity includes all entity CEOs as standing invitees. The responsibilities of the committee include overseeing the day-to-day management of the group's affairs, executing the decisions of the board, strategy development and reviews of the group's values, health and safety aspects, operations and financial performance. In accordance with good governance, the exco meets on a regular basis.

CODE OF ETHICS

Denel's values, as set out on page 06, underpin its code of ethics and are addressed to all stakeholders who have an interest in the group's activities and the manner in which it conducts business. The group's code of ethics includes details of how the group plans to implement its values and vision, as well as guidance on ethical standards and how to achieve them.

Over time Denel has strengthened policies and processes to ensure employees have clear guidance to make ethical choices and an understanding of the due diligence required in all business decisions. Having recently updated its code of ethics, Denel now sets clear expectations for directors, employees, suppliers, clients and other stakeholders.

Regular awareness training regarding the code and our ethical standards helps us to embed a culture of responsible business conduct throughout the group.

Adhering to the principles of openness and transparency Denel communicates regularly and comprehensively with all stakeholders regarding the group's approach to responsible business conduct. The group has a whistle-blowing mechanism that is operated by an independent organisation (refer page 102). External stakeholders have also been made aware of the company's ethics policy and hotline via our procurement and legal departments.

Ethics matters are monitored and reported to both the A&R and the S&E committees.

INTERNAL CONTROL

Whereas the board oversees the system of internal control within Denel, the implementation of these systems rests with the executive management. On a regular basis, the board's A&R sub-committee is presented with a formal review of the effectiveness of the group's internal controls. This review is informed by the combined assurance matrix, which identifies significant processes and assurances.

INTERNAL AUDIT

The independent internal audit function which was previously outsourced to an external firm has been fully in-sourced in the current financial year, under the authority of the Chief Audit Executive (CAE). As a permanent Denel employee, the CAE administratively reports to the GCEO and has unrestricted access to the chairman of the board and the chairman of the A&R committee. An internal audit charter is in place, which regulates the interaction between the group, management, internal auditors and the board. For the sake of transparency and accountability, the charter is tabled annually to the A&R committee for consideration and approval. The board is confident that the internal auditor department has discharged its duties fully in terms of the internal audit charter.

BUSINESS ENTITIES

Denel's entities follow the group policies, governance and financial control systems. As such, they comply fully with the PFMA, Companies Act and other relevant legislation, including that of foreign countries where they conduct business.

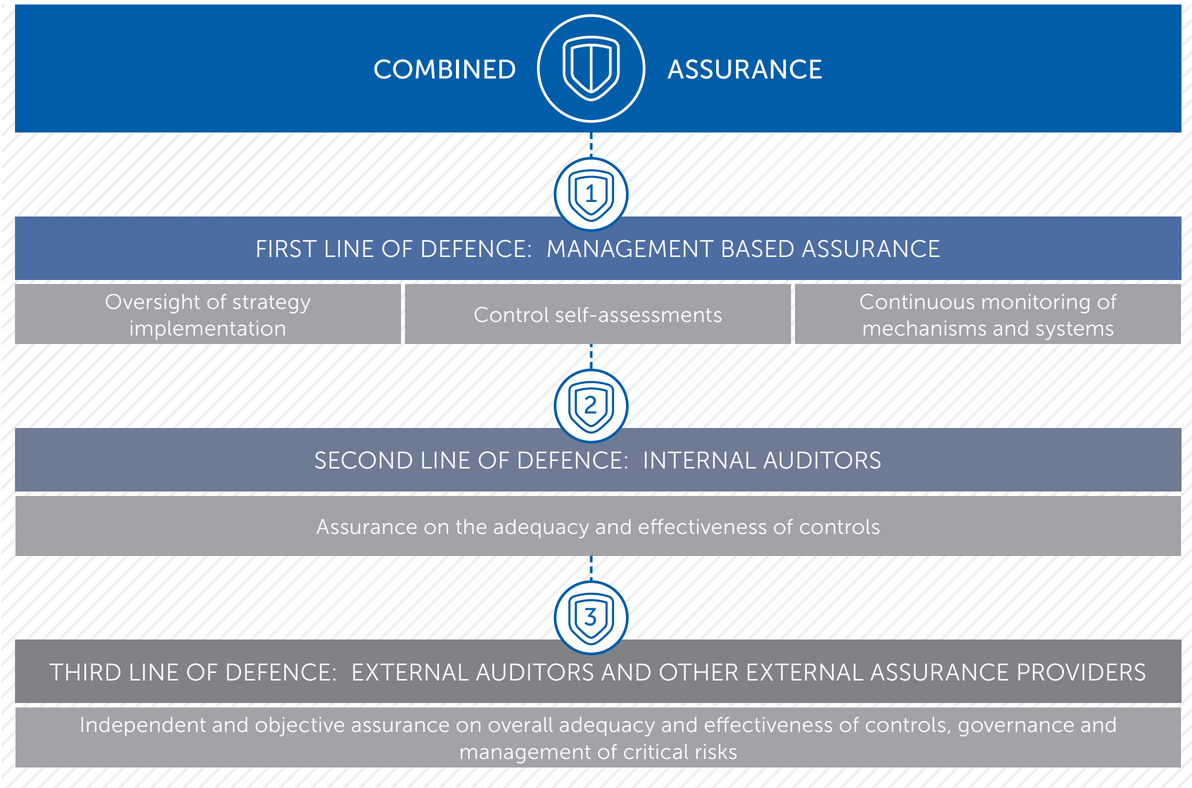
All entities are accountable to the GCEO. This material arrangement is further enhanced by each entity CEO being part of the group exco, whilst each entity's CEO is a standing invitee to the group exco. Apart from the business development council, IT steering committee, various forums are held regularly, i.e. arms control, business development, CFO, HR, legal, risk and compliance, security, SHEQ, supply chain and transformation forum. In these engagements not only operational matters are discussed, but also topics relevant to executive management and the leadership of the group in implementing the group's strategies.

COMBINED ASSURANCE

A combined assurance matrix is in force to enable the board to appreciate the effectiveness of the system of internal control and risk management in the group. This combined assurance approach ensures coordination among the different assurance providers, and prevents unintended audit duplication and audit fatigue whilst optimising audit costs. Denel also uses the combined assurance as input to the three-year rolling audit plan for the following year.

Assurance is provided through management self-assessments, observations and other related monitoring activities. This also includes the risk management process, internal audit, external audit, as well as various external bodies. External bodies involved in Denel include the National Key Point Secretariat, National Conventional Arms Inspections and Audit Directorate, ARMSCOR, SABS, Deutscher Kraftfahrzeug- Überwachungs-Verein (German Motor Vehicle Inspection Association) (Dekra), OEMs and SANAS. Whilst internal audit is risk-based and assesses the control environment, management assurance covers all critical business processes and their performance. Internal audit completes its assurance processes based on the approved audit plan designed for Denel's risk profile. External audit follows a specific audit scope approved by the A&R committee and places reliance on internal audit work, as and where appropriate.

The effectiveness of Denel's system of internal control, financial, operational and other regulatory controls is continuously reported to and assessed by the A&R committee to enable the board to discharge its oversight responsibilities.



FRAUD AND CORRUPTION

Denel's fraud and corruption prevention strategy is underpinned by the group's values of integrity, along with the requirements of the PFMA to prevent financial misconduct and fraud, and by the principles of the UN Global Compact. The S&E committee advises the board on good corporate citizenship and ethical relationships in implementing the group strategy.

FRAUD AND CORRUPTION AWARENESS

Denel continuously raises awareness among employees regarding the system of internal controls. This includes the delegations of authority, supply chain and other policies aimed at protecting the organisation's assets and reputation, preventing fraud and corruption, and promoting ethical conduct. The system provides for segregation of duties to promote transparency and accountability at various levels of the group.

The values of Denel, ethics and fraud and corruption prevention awareness are included in the group's induction programme. Additionally, fraud and corruption prevention awareness is continuously promoted through the group's newsletters and other forms of communication.

DETECTION OF FRAUD AND CORRUPTION

Management continuously interrogates financial, HR and supply chain information to detect possible instances of fraud and corruption as part of the day-to-day control activities.

Fraud detection tests were also included in the external and internal auditors' procedures. Whilst there may have been instances of fraud detected within the group, these were dealt with accordingly and in certain instances the relevant authorities notified. None of the identified cases included management at group nor at entities. The deficiencies identified were mitigated and management is in the process of improving internal prevention controls.

Denel constantly refines the parameters of its continuous control monitoring (CCM) system to increase data accuracy and improve the detection of discrepancies in the procurement and payment environment which might be susceptible to fraud and corruption. Internal audit reviewed all discrepancies and no instances of fraud were identified.

WHISTLE-BLOWING

Denel has an independent, confidential hotline accessible to all stakeholders, through which fraudulent and unethical behaviour may be reported. The hotline number is published on the intranet and website, as well as on supplier and customer orders, in the group's newsletters and communicated on noticeboards. Seventeen cases were reported through the hotline and none was to be fraud related.

Denel is comfortable that diligent management assessments, as well as external and internal audit procedures that include the Auditor-General requirements of supply chain fraud risk assessment, highlighted no instances of fraud and are effective in complementing fraud and corruption detection.

To report suspected incidents of fraud and corruption employees and stakeholders call

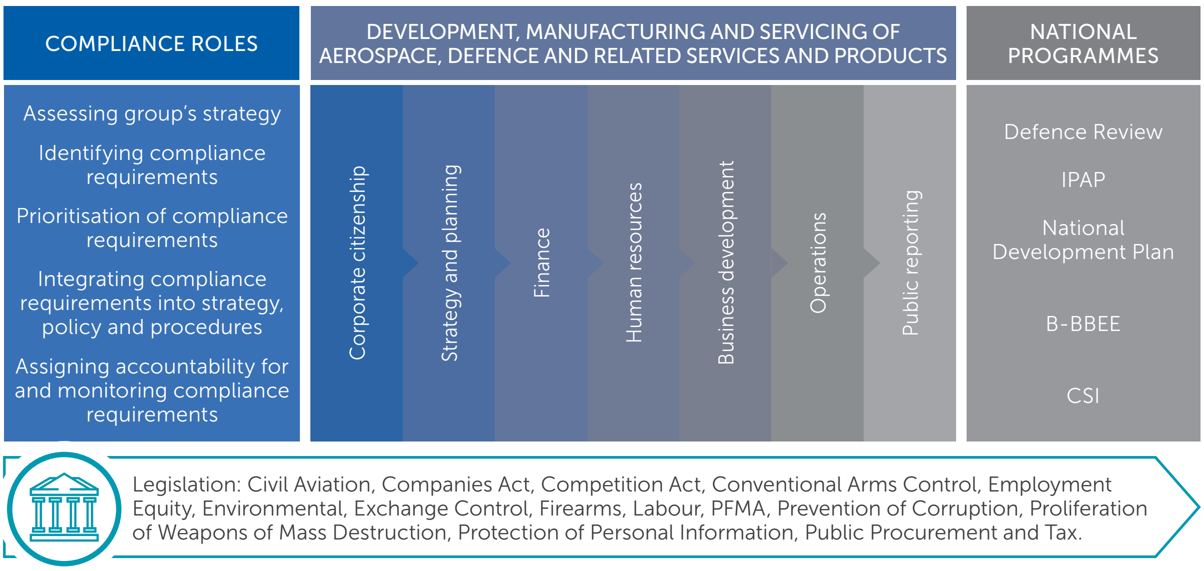
0800 20 48 80

LEGAL, REGULATORY AND PUBLIC POLICY COMPLIANCE

The nature of Denel's business requires assessment of and integration of legal, regulatory and public policy requirements into the strategy and operational processes of the group to meet its contractual, moral and corporate citizenship obligations. As a state-owned company (SOC) that trades globally, the observation of laws that govern the group and its activities forms the foundation for good corporate governance. It also demonstrates stewardship and responsibility to the shareholder and other stakeholders. No material non-compliances were identified during the year under review.

LEGAL COMPLIANCE FRAMEWORK

Denel has systems that enable the company to meet its legal and regulatory obligations regarding protection of confidential information, occupational health and safety, the environment, quality management, as well as industry and trading requirements. The framework is illustrated in the diagram below:



REMUNERATION REPORT

The philosophy underpinning the remuneration strategy and policy is that people should be rewarded for making a positive and appropriate difference to Denel. This is premised on their performance and contributions to achieve Denel's vision, strategic drivers, values and objectives to be a dynamic, vibrant, financially sustainable, transformed and profitable business. The remuneration strategy and policy is a management tool designed to support, reinforce, and align employee behaviour and actions to Denel values and objectives.

The remuneration philosophy supports our human capital strategy which aims to attract and retain employees of the right calibre and competence, and motivate employees to perform in line with our business and operational objectives. To ensure internal equity, Denel will evaluate and grade jobs to provide equitable remuneration to employees in accordance with their assigned duties and responsibilities, while differentials will be based on fair practices.

The remuneration strategy seeks to:

- Provide remuneration that attracts, retains, measures and motivates employees and helps to develop a high-performance culture;
- Ensure that remuneration levels are competitive in the market;
- Provide a "total reward" approach, which involves creating a suitable mix of financial and non-financial rewards;
- Remunerate practices that encourage highly competent individuals to consistently and effectively apply their competencies to enhance business performance;
- Ensure remuneration is capped at a maximum monetary value, related to market remuneration, per job level above which no individual may progress;
- Develop a remuneration process that provides for equitable pay and that is fair, consistent and transparent but differentiates between non-performance, average and excellent performers;
- Ensure alignment with Denel business strategy;
- Be fit for purpose, not one size fits all;
- Be flexible and adaptable in response to Denel's entities operating environment;
- Be fair and equitable and supportive of diverse needs (i.e. remuneration does not discriminate unfairly based on criteria that are not work-related or outside the employee's control such as race, gender, family responsibility, disability, age, etc.);
- Reinforce teamwork and a culture of belonging and high commitment;
- Comply with legislation and relevant guidelines; and
- Withstand scrutiny of stakeholders and the general public.

EXECUTIVE DIRECTORS' REMUNERATION

The PR&T committee reviews the remuneration of the executives. In doing so, the PR&T committee considers market benchmarks, internal pay parity, individual performance, as well as the guidelines on remuneration provided by the DPE for SOCs. Annual salary increases as approved by the shareholder at the AGM.

The following amounts were either paid or accrued to the executives during the year:

EXECUTIVES	REMUNERATION [8] R'000	COMPANY CONTRIBUTIONS R'000	TOTAL 2016/17 R'000	TOTAL 2015/16 R'000
EXECUTIVE DIRECTORS				
Mr R Saloojee [1]	6 407	-	6 407	4 725
Mr F Mhlontlo [2]	9 672	155	9 827	3 497
Sub-total	**16 072**	**155**	**16 234**	**8 222**
PRESCRIBED OFFICERS				
Mr ZN Ntshepe	2 758	193	2 951	2 763
Mr ZM Mhlwana	3 480	311	3 791	1 906
Ms N Davies	2 113	118	2 231	2 124
Mr T Kleynhans [3]	1 359	76	1 435	-
Mr GTT Mbele [4]	2 284	133	2 417	-
Ms NF Msiza [5]	1 518	85	1 603	-
Ms V Qinga [6]	1 947	109	2 056	-
Mr JM Wessels [7]	953	53	1 006	2 297
Sub-total	**16 412**	**1 078**	**17 490**	**9 090**
Total	**32 491**	**1 233**	**33 724**	**17 312**

SHORT-TERM INCENTIVE

Payment of short-term incentives, referred to as performance pay, is linked to the performance of the group and the individuals. Individuals qualify for performance pay when performance targets have been exceeded based on gain share principles. The relevant performance pay pool is determined based on the excess of net profit achieved above the performance target. Other performance indicators are used to moderate the performance pay allocations.

The following short-term incentives were either paid or accrued to the executives during the year:

EXECUTIVES	TOTAL 2016/17 R'000	TOTAL 2015/16 R'000
EXECUTIVE DIRECTORS		
Mr R Saloojee	-	-
Mr F Mhlontlo	-	-
Sub-total	**-**	**-**
PRESCRIBED OFFICERS		
Mr ZN Ntshepe	1 470	1 246
Mr ZM Mhlwana	1 723	1 356
Ms N Davies	966	1 018
Mr T Kleynhans [3]	1 344	-
Mr GTT Mbele [4]	1 680	-
Ms NF Msiza [5]	-	-
Ms V Qinga [6]	966	-
Mr JM Wessels [7]	-	1 068
Sub-total	**8 149**	**4 688**
Total	**8 149**	**4 688**

1. *Resigned on 8 November 2016.*
2. *Resigned on 30 August 2016.*
3. *Appointed as executive manager on 1 August 2016.*
4. *Appointed as executive manager on 10 April 2016.*
5. *Appointed as executive manager on 7 April 2016, resigned on 28 February 2017.*
6. *Appointed as executive manager on 1 April 2016.*
7. *Resigned 30 September 2016.*
8. *Refer note 29, page 175 of the notes of the consolidated annual financial statements for more detail.*

LONG-TERM INCENTIVES

Denel has in the past not implemented a long-term incentive scheme, despite it being provided for in the DPE remuneration guidelines. This was mainly due to financial constraints the group faced at the time. In light of improving financial performance, the board has recently approved the implementation of such a scheme for qualifying executives.

NON-EXECUTIVE DIRECTORS' REMUNERATION

The PR&T committee assists the board in reviewing non-executive directors' fees for discussion with the shareholder. Market benchmarks and the DPE's remuneration guidelines for SOCs are used to determine and make recommendations on non-executive directors' fees, which are presented at the AGM for consideration and approval by the shareholder.

The following amounts were either paid or accrued to the non-executive directors during the year:

	TOTAL	
NON-EXECUTIVE DIRECTORS	2016/17 R'000	2015/16 R'000
Mr LD Mantsha	891	597
Ms M Kgomongoe	367	343
Ms PM Mahlangu	279	187
Mr Mahumapelo	-	278
Ms N Mandindi	96	212
Ms R Mokoena	223	171
Mr NJ Motseki	204	238
Mr TJ Msomi	255	235
Lt Gen TM Nkabinde (rtd)	290	205
Ms KPS Ntshavheni	345	321
Total	**2 950**	**2 787**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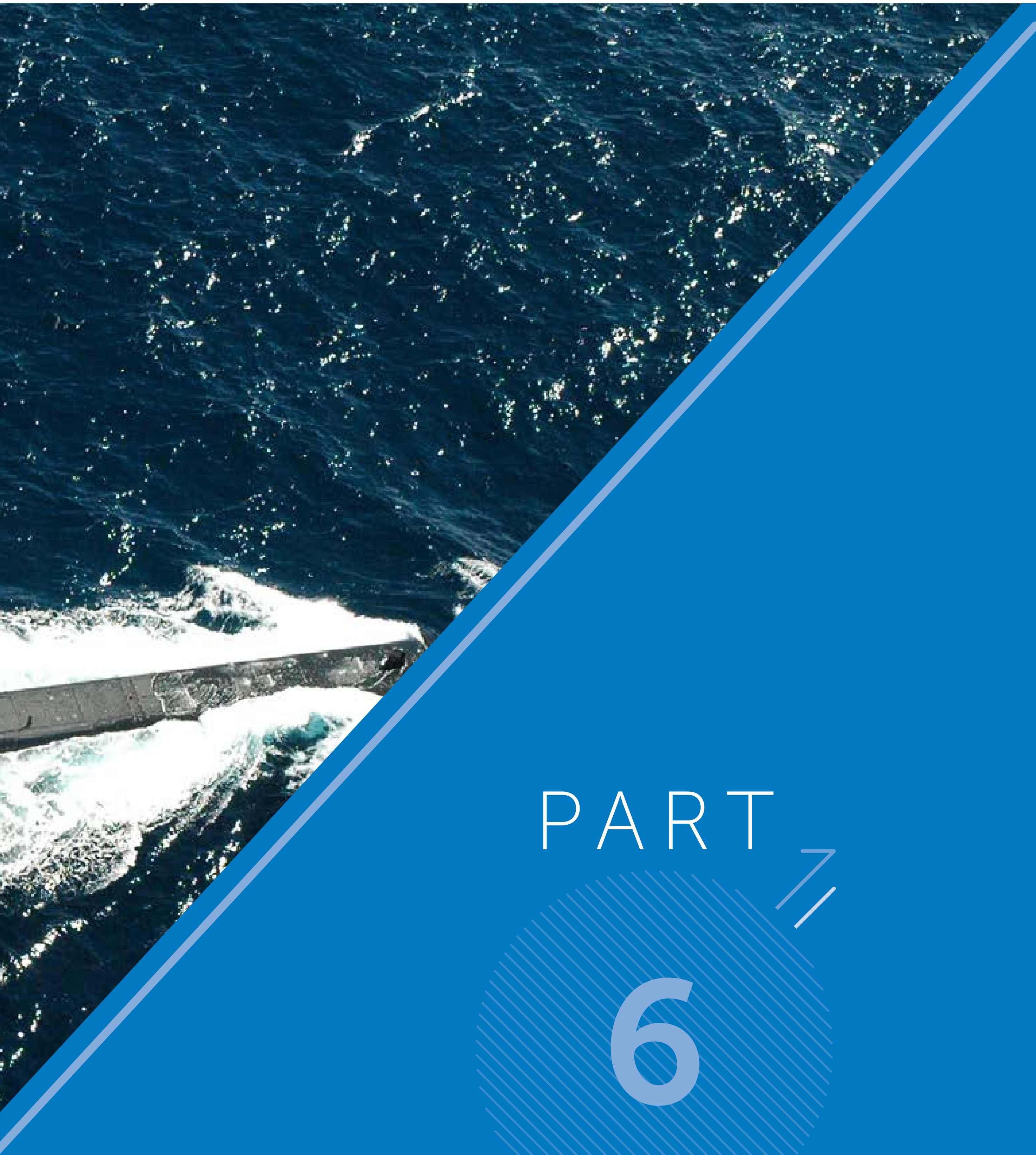

PART 6

CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

REPORT OF THE AUDIT AND RISK COMMITTEE

The A&R committee presents this report for the financial year ended 31 March 2017. This report has been prepared based on the requirements of the South African Companies Act, no. 71 of 2008, the King Code of Governance Principles for South Africa 2009 and the Public Finance Management Act, no. 1 of 1999.

DISCHARGE OF RESPONSIBILITIES

During the year ended 31 March 2017, the committee has convened four times in order to discharge both its statutory and board responsibilities. The composition of the board and attendance of meetings are included on pages 90 to 94. The board is satisfied that it has discharged its responsibilities in accordance with the King Code III, the Companies Act and the PFMA, and further responsibilities assigned to it by the board as contained in the terms of reference detailed on page 91.

In discharging its responsibilities during the year under review, the A&R committee:

- Reviewed the consolidated annual financial statements and integrated report prior to submission to and approval by the board, and satisfied itself that they fairly present the consolidated and separate results of operations, cash flows, and the financial position of Denel and comply, in all material respects, with the relevant provisions of the Companies Act and IFRS;
- Reviewed the adequacy, reliability and accuracy of financial information provided by management;
- Confirmed the going concern as the basis of preparation of the consolidated annual financial statements;
- Reviewed any significant legal and tax matters and considered any concerns identified that could have a material impact on the financial statements;
- Reviewed the effectiveness of internal controls;
- Reviewed the group's compliance with legal, environmental and regulatory provisions;
- Reviewed the assurance provided as contained in the combined assurance model;
- Reviewed the group's policies on risk assessment and management, including fraud and information technology risks as they relate to financial reporting, together with the going concern assessment, and found them to be sound;
- Reviewed the board's declaration of interest;
- Reviewed the effectiveness of systems and process of risk management and the mitigation thereof;
- Considered the reports of the internal and external auditors on the group's systems of internal control, including financial controls, risk management and maintenance of effective internal control systems. Significant issues raised and the adequacy of corrective action in response thereto were reviewed;
- Reviewed the activities of the internal audit function, including committee's charter, terms of reference, rolling three-year strategic plan and committee's 2016/17 work plan which were approved by the board;
- Reviewed the independence and objectivity of the external auditors. SizweNtsalubaGobodo, supported by Kwinana and Associates, are the independent external auditors. The external auditors were appointed at the AGM of 19 July 2012 for the 2012/13 to 2016/17 financial years and re-appointed annually during the said periods;
- Reviewed and approved the external audit plan, the budgeted and final fee for the reporting period and the terms of engagement of the external auditors;
- Pre-approved all audit and permissible non-audit services that the external auditor provides;
- Reviewed the external audit and evaluated the quality of the external audit process and concluded it to be satisfactory;
- Reviewed the external auditors' report and obtained assurances from the external auditors that adequate accounting records were being maintained;
- Reviewed the findings and recommendations of the external auditors and confirmed that no unresolved issues of concern exist between the group and the external auditors in relation to the group; and
- Reviewed the adequacy and effectiveness of the control framework and governance structures implemented within the IT environment.

INTERNAL CONTROLS

The A&R committee is of the opinion that the internal accounting controls are adequate to ensure that financial records may be relied upon for preparing the consolidated annual financial statements, and accountability for assets and liabilities is maintained. This opinion is based on the information and explanations given by management regarding various processes and initiatives aimed at improving the internal control environment and the integrity of information, discussions with internal audit, as well as the independent external auditors on the results of their audits.

EXPERTISE AND EXPERIENCE OF THE GROUP CHIEF FINANCIAL OFFICER AND FINANCE FUNCTION

The A&R committee has satisfied itself that the acting GCFO has appropriate expertise and experience. The A&R committee has considered, and has satisfied itself, of the appropriateness of the expertise, the adequacy of resources of the finance function and experience of the senior members of management responsible for the function.

CONCLUSION

Based on the results of the formal review of the group's system of controls and risk management, nothing significant has come to the attention of the committee to indicate any material breakdown in the functioning of the controls, procedures and systems during the year under review. The committee is satisfied that the consolidated annual financial statements are based on appropriate accounting policies, supported by reasonable and prudent judgements and estimates.

The A&R committee has evaluated the consolidated annual financial statements of Denel SOC Ltd and the group at year ended 31 March 2017 based on the information provided to it, considers that they comply, in all material respects, with the requirements of the Companies Act, the PFMA and IFRS. The A&R committee has recommended to the board that no material uncertainties existed to negatively impact the going concern of the group and all entities in the group.

The A&R committee recommended the consolidated annual financial statements and the integrated report for the year ended 31 March 2017 for approval by the board on 27 July 2017.

On behalf of the Audit and Risk committee

Ms Mpho Kgomongoe
Acting Audit and Risk committee Chairperson

INDEPENDENT AUDITORS' REPORT TO PARLIAMENT ON DENEL SOC LTD AND ITS SUBSIDIARIES

Report on the audit of the consolidated and separate financial statements

OPINION

We have audited the consolidated and separate financial statements of Denel SOC Ltd and its subsidiaries (the group) set out on pages 120 to 203 which comprise the consolidated and separate statement of financial position as at 31 March 2017, and the consolidated and separate statement of income and comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, as well as the notes to the consolidated and separate financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated and separate financial statements present fairly, in all material respects, the consolidated and separate financial position of the group as at 31 March 2017, and the group`s financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) and the requirements of the Public Finance Management Act of South Africa, 1999 (Act No. 1of 1999) (PFMA) and the Companies Act of South Africa, 2008 (Act No.71 of 2008) (Companies Act).

BASIS FOR OPINION

We conducted our audit in accordance with the International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the consolidated and separate financial statements section of our report.

We are independent of the group in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) together with the ethical requirements that are relevant to our audit in South Africa. We have fulfilled our other ethical responsibilities in accordance with the IRBA code and in accordance with other ethical requirements applicable to performing audits in South Africa. The IRBA code is consistent with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (parts A and B).

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

MATERIAL UNCERTAINTY RELATED TO GOING CONCERN

We draw attention to the directors' report which indicates that the government guarantee (R1.865bn) will expire on the 29th of September 2017. We concur with management's assessment to prepare the consolidated annual financial statements on a going concern basis. We further have noted that management have submitted an application for the renewal of the guarantee. In the event that the government guarantees are not renewed at maturity date, it may cast a material uncertainty on Denel SOC Ltd's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

KEY AUDIT MATTERS

Key audit matters are those matters that, in our professional judgement, are of most significance in our audit of the consolidated and separate annual financial statements of Denel SOC Ltd for the year ended 31 March 2017. These matters were addressed in the context of our audit of the consolidated and separate annual financial statements as a whole and forming our opinion thereon. We do not provide a separate opinion on these matters.

KEY AUDIT MATTER	HOW THE MATTER WAS ADDRESSED IN THE AUDIT
Programme management and related provisions	
The administration and accounting of contracts involves a high level of estimation and judgement which poses a risk to the group. The following are some of the areas of judgement related to program management: » The amount of revenue recognised in the year, which is based on the construction standards, IAS 11, is dependent on the appropriate assessment of the cost to complete the project. This estimated total costs to complete the project is highly complex and judgemental and is based on assumptions; » The contracts periods are long, as such the cost to complete the contracts involves a high level of estimation; » The management assessment process to arrive at the completion date, total costs for material, labour and overheads to be incurred, discounting factor used is complex and highly judgemental and is based on assumptions, specifically, which are affected by expected future market or economic conditions; and » Determining the estimated total cost to complete also affects the onerous contract provision. The determination of total costs to complete will affect whether the contract value is determined to be lower than the costs to complete a programme, which then leads to a contract being onerous.	Some of the procedures we performed to address the risk include: » We obtained an understanding of the contract process, and controls around the contract process specifically in relation to project cost estimation; » We reviewed estimated cost to completion computations to assess the reasonableness of the financial assumptions incorporated thereon to ensure that the revenue calculations are based correct cost to completion; » We reviewed the assumptions used such as the completion date, total costs for material, labour and overheads to be incurred, discounting factor used, to arrive at the total costs to complete the programme; » We re-performed calculations of revenue recognised; » Compared the prior year cost to complete to the current year cost to complete to assess the reasonability and reliability of the estimation process; and » Compared the assessed total cost to completion to the contract value and determined that the project is profitable and hence contract is not onerous and no provisions need to be raised.
Valuation of goodwill	
Goodwill represents a significant portion of the total assets of the Group. As required by the applicable accounting standards, goodwill is tested annually for impairment or whenever there is an impairment indicator by management to assess the recoverability of the carrying value of goodwill. This impairment assessment is considered to be a matter of most significance for the current year audit due to the significant judgements made by management regarding: » Revenue growth (including market share and revenue growth); » Operating margins; » Cash flow forecasts and assumptions; » Valuation model; and » The discount rates applied to the projected future cash flows. Included in the analyses used to perform the impairment assessment	We focused our testing of the impairment of goodwill on the key assumptions made by management. Our audit procedures included: » We have tested the mathematical accuracy of the valuation models and are satisfied that the approach adopted by management in the valuation models is in line with market practice and the applicable requirements of *IAS36: Impairment of Assets* which was also confirmed with our internal valuation experts; » Management's forecasts were agreed to approved in budgets; » We further assessed the Group's budgeting procedures (which form the basis of the forecasts) by comparing budgets to actual results and held discussions with management on the reasonability of the forecasts used in the valuations where past results were not available or adjustments are made to the in-country budgets; » The terminal growth rate was compared to long term inflation rates obtained from independent sources; » Our valuation experts independently recalculated a weighted average cost of capital discount rate (which includes a country risk premium) for the group taking into account independently obtained data such as the cost of debt, risk free rates in the market; market risk premiums, debt/equity ratios as well as the beta of comparable companies; and this was compared to the discount rate used by management. The discount rates of management were considered to be within an acceptable range of our independent calculation; and » We re-performed the value in use calculation as calculated by management. We performed sensitivity analysis on the value-in-use calculation with focus on the discount rate, the annual growth rates, the terminal growth rate and forecast cash flows for each entity. We further performed sensitivity procedures to determine the maximum decline that would result in limited or no headroom and compared our results with that of management. We also focused on the adequacy of disclosures of the Group's disclosures about those assumptions to which the outcome of the impairment is most sensitive, those that have the most significant effect on the determination of the recoverable amount of goodwill.

OTHER MATTER

The audit report of Denel SOC Limited for the consolidated and separate financial statements for the financial year ended 31 March 2017, dated 31 July 2017 has been withdrawn and replaces with this audit report. The 31 July 2017 audit report erroneously omitted the paragraph relating to the material non-compliance with section 51(1)(b)(ii) of the Public Finance Management Act.

The previously omitted paragraph has now been included in this audit report. The inclusion of the non-compliance with section 51(1)(b)(ii) of the Public Finance Management Act in this audit report does not change the unqualified audit opinion on the consolidated and separate financial statements as previously issued on the 31 July 2017.

RESPONSIBILITIES OF THE ACCOUNTING AUTHORITY FOR THE CONSOLIDATED AND SEPARATE ANNUAL FINANCIAL STATEMENTS

The board of directors, which constitutes the accounting authority, is responsible for the preparation and fair presentation of the consolidated and separate financial statements in accordance with IFRS and the requirements of the PFMA and the Companies Act and for such internal control as the accounting authority determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated and separate financial statements, the accounting authority is responsible for assessing the group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the accounting authority either intends to liquidate the group or to cease operations, or has no realistic alternative but to do so.

AUDITOR RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED AND SEPARATE ANNUAL FINANCIAL STATEMENTS

Our objectives are to obtain reasonable assurance about whether the consolidated and separate financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated and separate financial statements.

As part of an audit in accordance with the ISAs, we exercise professional judgement and maintain professional scepticism throughout our audit of the consolidated and separate financial statements, and the procedures performed on reported performance information for selected objectives and on the public entity's compliance with respect to the selected subject matters.

We also:

- Identify and assess the risks of material misstatement of the consolidated and separate financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the public entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting authority.
- Conclude on the appropriateness of the accounting authority use of the going concern basis of accounting in the preparation of the financial statements. We also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on Denel SOC Limited and its subsidiaries ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. Our conclusions are based on the information available to us at the date of the auditor's report. However, future events or conditions may cause a public entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.
- Communicate with the accounting authority regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- Confirm to the accounting authority that we have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on our independence, and where applicable, related safeguards.

REPORT ON THE AUDIT OF THE ANNUAL PERFORMANCE REPORT

INTRODUCTION AND SCOPE

In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof we have a responsibility to report material findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report. We performed procedures to identify findings but not to gather evidence to express assurance.

Our procedures address the reported performance information which must be based on the approved performance planning documents of the public entity. We have not evaluated the completeness and appropriateness of the performance indicators established and included in the planning documents. Our procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information relating to future periods that may be included as part of the reported performance information. Accordingly our findings do not extend to these matters.

We evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the Performance management and reporting framework, as defined in the general notice, for the following selected objectives presented in the "Performance against the Shareholder Compact" section of the integrated report of the state-owned company for the year ended 31 March 2017:

OBJECTIVES	PAGES IN THE INTEGRATED REPORT
Ensure commercially viable defence material design, development, manufacturing, test and evaluation and support capabilities aligned to national security requirements and key international markets.	80
Prudent cash management and the creation of a cash buffer to cover minimum of six months of operational costs; and sustainability.	80

We performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. We performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

We did not identify any material findings on the usefulness and reliability of the reported performance information for the following objectives:

- Ensure commercially viable defence material design, development, manufacturing, test and evaluation and support capabilities aligned to national security requirements and key international markets.
- Prudent cash management and the creation of a cash buffer to cover minimum of six months of operational costs; and sustainability.

OTHER MATTER

We draw attention to the matter below. Our opinions are not modified in respect of this matter.

Achievement of planned targets

Refer to the "Performance against the shareholder compact" section of the Integrated Report on page 80 for information on the achievement of planned targets for the year and explanations provided for the under/over achievement of a significant number of targets.

REPORT ON AUDIT OF COMPLIANCE WITH LEGISLATION

INTRODUCTION AND SCOPE

In accordance with the PAA and the general notice issued in terms thereof we have a responsibility to report material findings on the compliance of Denel SOC Ltd with specific matters in key legislation. We performed procedures to identify findings but not to gather evidence to express assurance.

The material finding in respect of the compliance criteria for the applicable subject matter is as follows:

EXPENDITURE MANAGEMENT

Effective steps were not always taken to prevent irregular expenditure amounting to R116 million as disclosed in note 35 to the annual financial statements as required by section 51(1)(b)(ii) of the PFMA.

OTHER INFORMATION

The Denel SOC Ltd.'s and its subsidiaries accounting authority is responsible for the other information. The other information comprises the information included in the annual report, which includes the director's report, the audit and risk committee's report and the company secretary's certificate as required by the Companies Act. The other information does not include the consolidated and separate financial statements, the auditor's report thereon and those selected objectives presented in the annual performance report that have been specifically reported on in the auditor's report.

Our opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and we do not express an audit opinion or any form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated and separate financial statements and the selected objectives presented in the annual performance report, or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

INTERNAL CONTROL DEFICIENCIES

We considered internal control relevant to our audit of the consolidated and separate financial statements, "Performance against the Shareholder Compact" section of the integrated report and compliance with applicable legislation; however, the objective is not to express any form of assurance thereon. The matter reported below is limited to the finding on compliance with legislation included in this report.

FINANCIAL AND PERFORMANCE MANAGEMENT

The matter identified and reported under the audit of compliance with legislation has arisen due to non-adherence with operational policies in the procurement and contract management processes.

OTHER REPORTS

We draw attention to the following engagements conducted by various parties that have, or could potentially have, an impact on the matters reported on the public entity`s financials, performance and compliance related matters. The reports do not form part of our opinion on the financial statements or our findings on the reported performance information or compliance with legislation.

INVESTIGATIONS

During the financial year under review the group conducted investigations into alleged irregularities, fraud and corruption within the procurement environment. No material findings that had an effect on the group were noted.

AGREED-UPON PROCEDURE ENGAGEMENTS

Agreed-upon procedures engagements were performed on the following:

- Six agreed upon procedures engagements were performed during the reporting period solely to confirm that the issue of commercial notes complies in all respects with relevant provisions of the Commercial Paper Regulation issued by the registrar of Banks as required by paragraph 3(5) (j) for commercial paper, issued under the Denel SOC Ltd ZAR 3 billion Domestic Medium Term Note Programme.
- One agreed upon procedure engagement performed on behalf of Denel SOC Ltd to verify the costs on a contract.

AUDIT TENURE

In terms of the IRBA Rule published in Government Gazzette 39475 dated 4 December 2015, we report that SizweNtsalubaGobodo has been the auditor of Denel SOC Ltd for five years.

SizweNtsalubaGobodo Incorporated
Registered Auditor

Per: Aaron Mthimunye
Chartered Accountant SA
Director
Registered Auditor
24 January 2018

20 Morris Street East
Woodmead
2191

Sizwe Ntsaluba Gobodo
AUDIT•ADVISORY•FORENSICS

STATEMENTS OF RESPONSIBILITY

DIRECTORS' STATEMENT

The board of directors is pleased to present its report and the audited consolidated annual financial statements for the year ended 31 March 2017.

The directors are responsible for the integrity and fair presentation of the consolidated annual financial statements of Denel SOC Ltd and its subsidiaries. The consolidated annual financial statements presented on pages 120 to 203 have been prepared in accordance with IFRS, the Companies Act and PFMA. These consolidated annual financial statements have been prepared in accordance with appropriate accounting policies and include amounts based on judgements and estimates made by management. The directors have supervised the preparation of information included in the integrated report and are responsible for both its accuracy and consistency.

The directors are responsible for going concern and are satisfied that at the time of approving the consolidated annual financial statements it is appropriate to use the going concern basis in preparing these consolidated annual financial statements. In arriving at this conclusion, the directors considered the solvency and cash position at 31 March 2017, the cash requirements for at least 12 months from that date and the borrowing facilities available. It also took into account the strong order book, robust business plan and prospects for the future. The going concern including additional factors that were considered is discussed in more detail on pages 118 of this report.

The external auditors are responsible for independently auditing and reporting on the consolidated annual financial statements. The independent auditors' report appears on pages 110 to 114.

During the year under review, the directors retained full and effective control over the group and monitored management in implementing the approved plans, risk management and strategies. The board is satisfied that the risk management processes are effective.

The directors are of the opinion that the consolidated annual financial statements fairly present the financial position of Denel SOC Ltd and its subsidiaries and the results of their operations and cash flows for the year ended 31 March 2017.

The consolidated annual financial statements of Denel SOC Ltd for the year ended 31 March 2017, as set out on pages 120 to 203, have been prepared under the supervision of Mr Odwa Mhlwana CA (SA) and were approved by the board of directors on 27 July 2017 in terms of the Companies Act and the PFMA, and are signed on their behalf by:

Daniel Lugisani Mantsha
Chairman of the board

Zwelakhe Ntshepe
Acting Group Chief Executive Officer

CERTIFICATE BY THE GROUP COMPANY SECRETARY

The Group Company Secretary certifies that the company has lodged with the Companies and Intellectual Property Commission all such returns as are required of a public company in terms of the Companies Act and that all such returns are true, correct and up to date.

Vuyokazi Xaxa
Group Company Secretary

DIRECTORS' REPORT

The financial results in this report are based on the results of the Denel group, and in context the term 'group' refers to the company, its subsidiaries and associated companies. The nature of the group's business is described on page 08, as well as in the operational review section on pages 67 to 74 of this report.

FINANCIAL AND OPERATIONAL REVIEW

	GROUP	
	2016/17	2015/16
	Rm	Rm
Revenue	8 057	8 228
Gross profit	1 821	1 672
Other income	136	288
Operating expenditure	(1 483)	(1 455)
EBIT	628	637
Net finance costs	(272)	(203)
Net profit	333	395

Denel posted a profit of R333m (2015/16: R395m). The decrease for the year under review can be attributed to softer local demand, as well as foreign exchange losses of R232m mainly relating to the revaluation of revenue recognition debtors, partially offset by growth in export sales. In the review of our business entities, product portfolios, the international and local market, our business processes and cost structures, we have recognised that certain of our entities and cost structures require repositioning.

EXTERNAL INTEREST EXPENSE ON BORROWINGS

Business operations are funded through a combination of cash generated, short- and medium-term bank credit facilities, corporate bonds and commercial paper borrowings. The amount of R1.85bn of debt is unconditionally guaranteed by the government and total debt amounted to R3.265bn (2015/16: R3.717bn) at year-end, resulting in net external interest paid of R249m (2015/16: R184m). This amount excludes the unwinding of interest on long-term provision. Refer to the funding section of this report on page 162.

IMPAIRMENT OF ASSETS

Impairment assessments were performed on assets and no assets were impaired. However, Denel reviewed the impairment of the UAV intangible asset done in 2015/16 and reversed R72m of the impairment. Further details are disclosed on page 148 of the consolidated annual financial statements.

SIGNIFICANT CONTRACTS

The contracts discussed below had a significant impact on the reported financial results, or will continue to have an impact on the group's performance.

HOEFYSTER

Denel is contracted by the local customer for the development and production of the new-generation infantry combat vehicle product system (Badger) programme, namely Project Hoefyster. The development phase was substantially completed and Denel Land Systems is on track to deliver the first 88 Badger ICV to the South African Army by May 2019, whilst gearing up for full-scale production. Denel Land Systems is in the process of assembling the first eight Badger turrets with the first four reaching an advanced stage of assembly. In the 2017/18 financial year the plan is to produce 56 turrets and deliver 20 complete systems. Deliveries of all 242 Badgers are set to be concluded in 2022. The base value of the programme is R9.4bn and revenue of R484m (2015/16: R676m) was recognised during the financial year.

HEAVY ARMOURED FIGHTING VEHICLE

During 2011 a South East Asian country contracted Denel to develop, manufacture, supply, deliver and commission a turret for a fleet of 8x8 armoured fighting vehicles. The required industrial participation activities have been implemented and the first systems have been successfully manufactured, assembled and tested in the end-user country. Progress is in accordance with the delivery requirements of the client with numerous systems having been accepted with some already in service. Major milestones reached on the AV8 turret system contract are the completion of the light combat turret (LCT30) product baseline and the assembly of 30 LCT30 systems, five ATGW systems and the integration of 30 remote-control weapon station systems. The base value of the programme is R3.7bn and revenue of R953m (2014/15: R1.193bn) was recognised during the 2016/17 financial year.

AIR-TO-AIR MISSILE

The development of the A-Darter 5th generation air-to-air missile, in a collaboration programme between the governments of SA and Brazil, is now in the qualification phase. The final qualification test to demonstrate performance will be done within the 2017 calendar year. The value of the programme is R2bn and revenue of R101m (2015/16: R100m) was recognised during the year.

The follow-on production contract for the SAAF with a value of R939m was placed on Denel during March 2015 and revenue to the value of R219m (2015/16: R119m) was recognised during the year. The outputs of the contract are the industrialisation and manufacturing of the A-Darter missile. The order also includes the establishment of a logistic support capability required for the SAAF to operate the missile. The initial batch of four acquisition trainer missiles is planned for delivery in late 2017 with the final batch of operational missiles scheduled for delivery in the first quarter of 2020.

SEEKER 400

The Seeker 400 system produced for the SANDF has successfully completed the required system acceptance tests with the focus now on attainment of the military type certificate. This is expected to be accomplished in the 2017/18 financial year. The value of the programme is R358m of which R295m has been invoiced to date.

ANTI-ARMOUR MISSILE

Denel was contracted for the supply and integration of the Mokopa long-range anti-armour missile on a helicopter platform for a North African client. All the logistics support equipment was delivered this year, as well as the second batch of production missiles. The value of the programme is R418m and revenue of R57m (2015/16: R74m) was recognised during the year.

SURFACE-TO-AIR MISSILE

Denel was contracted for the supply of the Umkhonto infrared surface-to-air missile system for two frigates newly constructed in Europe for a North African client. The production of the fire control equipment has been completed and installation onto both frigates is complete. The Umkhonto missile round production and all deliveries to the customer have been completed. The total contract value is R800m and revenue of R243m (2015/16: R157m) was recognised during the year.

PRECISION-GUIDED MUNITIONS

Denel concluded a contract during 2010/11 to the value of R1.2bn for the sale of Al Tariq precision-guided munitions with a follow-on contract to the value of R400m concluded in 2014/15. The programme experienced a number of delays during the development phase, resulting in a production lag which has been recovered and a total of 580 full weapons kits plus 320 sub-kits were delivered to date. In addition, build kits for 420 IIR weapons are being shipped to Tawazun Dynamics LLC with a view to complete the MBARC production contract in the UAE. The programme conducted a series of successful flight trials on the newly developed imaging infrared (IIR) seeker and production was activated.

A centre of excellence for manufacturing of these weapons is being established in the buying country as a part of a joint venture established by Denel and that country's partner, which also contributes to Denel's offset programme. The programme accounted for revenue of R168m (2015/16: R428m) during the year.

ARMOURED VEHICLE PROGRAMMES

N35

Denel Vehicle Systems are contracted by a client in the UAE to finalise development of 4x4 and 6x6 variants of the N35 vehicle. DVS is also contracted to deliver 100 N35 4x4 vehicles to the same client, with 30 vehicles delivered to date. The development and production contracts will be concluded in the 2017/18 financial year. The total value of the contracts is R1,2bn with the possibility of a follow-on order. The programme accounted for revenue of R283m (2015/16: R50m) during the year.

MMP

Denel Vehicle Systems entered into a contract during 2015/16 with a Middle East client for the supply of 24 mobile mortar platform (MMP) armoured utility vehicles. All 24 vehicles have been delivered with the last batch of eight vehicles passing final acceptance during March 2017. The contract's value is R220m of which R208m (2015/16: Rnil) recognised during the year.

AIRBUS A400M

Denel was contracted during 2005/6 as a programme partner for the design, development, manufacture, supply and supporting activities of the WFF, TS and RSS structural components for the Airbus A400M military transport aircraft. The Airbus contract was historically loss-making and the DPE indemnified these losses up to R1.6bn.

Denel met all its major A400M deliverables for the 2016/17 financial year, including additional spares and modification sales. The deliverables consisted of 24 WFF, TS and RSS ship sets. On the cargohold system work packages 20 ISO-lock and eight central guide vertical restraint sets were delivered. The most notable programme performance was the TS programme which celebrated its 67th consecutive on-time completion. The total programme value of the five work packages amounts to R3.6bn and revenue of R510m (2015/16: R540m) was recognised during the year.

DENEL MEDICAL BENEFIT TRUST

The group provides a post-retirement medical subsidy to current and former employees who were appointed before 1 April 2000. The assets and liabilities are accounted for separately in the trust, and are not included in the consolidated annual financial statements of the group. The group has longevity and investment risk exposure as it is expected to fund actuarial losses that may arise. Although certain businesses have been unbundled from the group, the total liability remains with Denel. Owing to these risks, the group is in the process of implementing a voluntary settlement that will ensure the financial risk to the group terminates, whilst the qualifying employees continue to receive the benefit.

To date 86.5% of the qualifying beneficiaries have accepted the settlement offer made by Denel in lieu of the post-employment medical subsidy. Denel will ensure that through due process the open-ended liability risk is mitigated in terms of the remaining beneficiaries. The actuarial value of the fund and other disclosures are provided in note 32 of the consolidated annual financial statements.

FUNDING

Denel increased its DMTN programme from R2.2bn to R3bn in order to fund the growth of the company. Of the R3bn an amount of R1.85bn is government guaranteed with the guarantee maturing on 30 September 2017. Denel will apply to the shareholder to have this guarantee extended for a further five-year period. Denel raised guaranteed interest-bearing borrowings through the DMTN with a coupon value of R1.85bn (2015/16: R1.85bn). The debt consists of a R300m 18-month corporate bond, R585m five-year corporate bond and short-term commercial paper of R964m. The balance of the DMTN of R460m is unsecured and R690m is utilised by means of a five-year bond maturing in June 2018. The group's borrowings are at an average interest rate of 8.64% (2015/16: 7.76%) that includes an average overnight borrowing rate of 9.38% (2015/16: 8.00%), and an average Commercial Paper Programme interest rate of 8.53% (2015/16: 7.50%), which resulted in borrowing cost of R288m (2015/16: R252m) during the year.

FitchRatings re-affirmed Denel's long-term rating at AAA(zaf) and short-term rating F1+(zaf) with a stable outlook during the year. The rating agency is relying strongly on continued shareholder support, strong operational performance that is led by DLS and DD, as well as Denel's large order book of more than R18bn.

The cash on hand together with the cash forecast for the next 12 months indicates that the group will be liquid for the foreseeable future. During the year under review, Denel tightly managed cash and working capital, ensuring minimal exposure to liquidity risk.

GOING CONCERN

The directors evaluated the appropriateness of the going concern assumptions used in the preparation of the consolidated annual financial statements and in particular considered the matters summarised below:

- The solvency and liquidity position of the group as at 31 March 2017;
- The availability of sufficient funds, including borrowing facilities, to meet the group's requirements over the next 12 months;
- The forecasted shareholder's equity for the foreseeable future will remain positive;
- The positive business results projected over the next five years and risks identified in the business plan underpinned by the confirmed order book of R18bn; and
- The shareholder continues to view Denel as a strategic asset and has in the past made a written undertaking that it will endeavour to assist the directors in maintaining its going concern status and extended the R1.85bn guarantee from one to five years during 2012/13.

Based on the factors above, the directors are satisfied that Denel has adequate reserves and cash resources to continue operating as a going concern. The consolidated annual financial statements were therefore prepared on this basis.

INTERNAL CONTROLS

The group has implemented a system of internal controls which is reviewed by the A&R committee on a quarterly basis. The board is satisfied that the system of internal controls is effective.

COMPLIANCE WITH LAWS AND REGULATIONS

The group has implemented a compliance process to meet applicable legal and regulatory requirements. The process entails implementing systems to ensure compliance with existing and emerging legislation. It further monitors the system, detects and addresses deficiencies that may lead to non-compliance. The board is satisfied that the group has in all material respects complied with the provisions of the PFMA, the Companies Act and other applicable legislation.

SUBSIDIARIES AND ASSOCIATED COMPANIES

The interests in subsidiaries and associated companies are set out in note 11, 12 and 34 of the consolidated annual financial statements.

CAPITAL EXPENDITURE

The board approved capital expenditure of R490m whereas R66m was utilised, mainly in upgrading the entities' production facilities.

SHARE CAPITAL AND SHARE PREMIUM

The authority to issue shares vests in the shareholder. Directors do not have the authority to issue shares of the company. There was no change in the authorised share capital of the company for the financial year under review.

DIVIDENDS

No dividend was recommended for the 2016/17 year (2015/16: Rnil).

COMPLIANCE WITH ACCOUNTING STANDARDS

The consolidated annual financial statements comply with IFRS.

AUDITORS

The consolidated annual financial statements are audited by SizweNtsalubaGobodo. The statutory auditor for the forthcoming year will be confirmed at the AGM scheduled for 23 August 2017.

DIRECTORATE

The following board members resigned during the year:

- Ms N Mandindi
- Mr NJ Moteski

Further details regarding the board of directors are discussed on pages 85 to 87.

GROUP COMPANY SECRETARY

The acting group company secretary for the period under review was Ms Vuyo Xaxa. Her business and postal addresses, which are also the address of the registered office of the company, are stated below:

Denel Building Head Office	PO Box 8322
Nellmapius Drive	Centurion
Irene	0046
Gauteng	South Africa
South Africa	

EVENTS AFTER REPORTING PERIOD

In order to identify events after the reporting period, all material matters affecting the Denel group between the approval of the consolidated annual financial statements and the publication of this report were taken into account.

No other matters arose between the financial year-end and the date of this report.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

AS AT 31 MARCH 2017

	Notes	GROUP 2016/17 Rm	GROUP 2015/16 Rm	COMPANY 2016/17 Rm	COMPANY 2015/16 Rm
ASSETS					
Non-current assets		3 286	3 113	3 243	3 233
Property, plant and equipment	8	1 134	1 210	632	685
Investment properties	9	728	680	719	671
Intangible assets	10	393	335	97	36
Investments in subsidiaries	11			1 295	1 341
Investments in associated companies	12	995	840	500	500
Deferred tax assets	13	36	48	-	-
Current assets		9 177	9 733	7 364	8 376
Inventories	14	2 623	2 341	1 773	1 685
Trade and other receivables	15	4 318	5 028	3 894	4 542
Other financial assets	16.1	209	361	141	361
Cash and short-term deposits	17	2 021	2 003	1 556	1 788
Income tax receivables		6	-	-	-
Non-current assets held for sale	18	-	156	-	156
Total assets		12 463	13 002	10 607	11 765
EQUITY AND LIABILITIES					
Equity					
Issued capital	19.2	1 225	1 225	1 225	1 225
Share premium	19.3	4 951	4 951	4 951	4 951
Revaluation reserve		43	43	43	43
Accumulated loss		(3 572)	(3 917)	(4 230)	(4 332)
Total equity attributable to equity holders of the parent		2 647	2 302	1 989	1 887
Non-controlling interest	20	4	19		
Total equity		2 651	2 321	1 989	1 887
Non-current liabilities		3 299	4 469	3 057	4 219
Loans and borrowings	21	853	1 995	690	1 973
Advance payments received	22	2 060	2 100	2 060	1 937
Provisions	23.1	385	373	307	309
Deferred tax liabilities	13	1	1	-	-
Current liabilities		6 513	6 212	5 561	5 659
Trade and other payables	24	1 941	2 154	1 620	1 829
Loans and borrowings	21	2 412	1 722	2 315	1 917
Other financial liabilities	16.2	170	331	93	277
Advance payments received	22	1 562	1 431	1 246	1 224
Income tax payables		1	11	-	-
Provisions	23.2	421	560	287	412
Preference dividends payable	20	6	3		
Total liabilities		9 812	10 681	8 618	9 878
Total equity and liabilities		12 463	13 002	10 607	11 765

CONSOLIDATED INCOME STATEMENTS AND STATEMENTS OF COMPREHENSIVE INCOME

YEAR ENDED 31 MARCH 2017

		GROUP		COMPANY	
		2016/17	2015/16	2016/17	2015/16
	Notes	Rm	Rm	Rm	Rm
CONTINUING OPERATIONS					
Revenue	2	8 057	8 228	6 289	6 614
Cost of sales	3	(6 236)	(6 556)	(4 838)	(5 355)
Gross profit		1 821	1 672	1 451	1 259
Other income	4	136	288	173	428
Other operating expenses	3	(1 483)	(1 455)	(1 254)	(1 189)
Operating profit		474	505	370	498
Finance costs	6.1	(352)	(280)	(359)	(289)
Finance income	6.2	80	77	92	63
Share of profit in associated companies	12	154	132		
Profit before tax		356	434	103	272
Income tax expense	7	(23)	(39)	-	-
Total comprehensive income for the year net of tax		333	395	103	272
Profit for the year is attributable to:					
Equity holders of the parent		345	378		
Non-controlling interest	20	(12)	17		
		333	395		

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

YEAR ENDED 31 MARCH 2017

	Total equity attributable to equity holders of the parent						
	Issued capital	Share premium	Revaluation reserve [1]	Accumulated loss	Total	Non-controlling interest	Total equity
	Rm	Rm	Rm	Rm	Rm	Rm	Rm
GROUP							
Balance at 1 April 2015	1 225	4 951	43	(4 295)	1 924	3	1 927
Preference dividends payable						(1)	(1)
Total comprehensive income			-	378	378	17	395
Profit for the year				378	378	17	395
Other comprehensive income			-	-	-	-	-
Balance at 31 March 2016	1 225	4 951	43	(3 917)	2 302	19	2 321
Preference dividends payable						(3)	(3)
Total comprehensive income			-	345	345	(12)	333
Profit for the year				345	345	(12)	333
Other comprehensive income			-	-	-	-	-
Balance at 31 March 2017	**1 225**	**4 951**	**43**	**(3 572)**	**2 647**	**4**	**2 651**
COMPANY							
Balance at 1 April 2015	1 225	4 951	43	(4 604)	1 615		
Total comprehensive income			-	272	272		
Profit for the year				272	272		
Other comprehensive income			-	-	-		
Balance at 31 March 2016	1 225	4 951	43	(4 332)	1 887		
Total comprehensive income			-	102	102		
Profit for the year				103	103		
Other comprehensive income			-	-	-		
Balance at 31 March 2017	**1 225**	**4 951**	**43**	**(4 230)**	**1 989**		

1. *The revaluation reserve relates to fair value adjustments made to property, plant and equipment on reclassification to investment properties.*

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEAR ENDED 31 MARCH 2017

	Notes	GROUP 2016/17 Rm	GROUP 2015/16 Rm	COMPANY 2016/17 Rm	COMPANY 2015/16 Rm
OPERATING ACTIVITIES					
Net cash flows from/(used in) operating activities		376	(701)	498	(711)
Receipts from customers		8 881	6 682	7 186	5 263
Payments to suppliers and employees		(8 331)	(7 254)	(6 602)	(5 757)
Cash from/(utilised in) operations	26	550	(572)	584	(494)
Increase in advance payments received	22	91	33	146	(98)
Interest paid	6	(316)	(230)	(323)	(240)
Interest received	6	79	77	91	65
Dividends received	4 & 12	-	25	-	56
Income tax paid		(28)	(34)	-	-
INVESTING ACTIVITIES					
Net cash flows from/(used in) investing activities		93	(995)	(59)	(1 029)
Purchase of property, plant and equipment	8	(63)	(158)	-	(107)
Proceeds from sale of property, plant and equipment		2	1	-	-
Proceeds from sale of investment properties	9	156	-	156	-
Purchases of intangible assets	10	(2)	(10)	(1)	(10)
Acquisition of subsidiary		-	(828)	-	(828)
Advances to subsidiaries				(169)	(84)
Net cash inflows/(outflows) before financing activities		469	(1 696)	439	(1 740)
FINANCING ACTIVITIES					
Net cash (outflows)/inflows from financing activities		(451)	1 559	(671)	1 740
Repayments of interest bearing borrowings		(2 056)	(1 282)	(2 033)	(1 275)
Proceeds from interest bearing borrowings		1 605	2 841	1 362	3 015
Net increase/(decrease) in cash and cash equivalents		18	(137)	(232)	-
Cash and cash equivalents:					
At the beginning of the year		2 003	1 909	1 788	1 788
Entity acquired		-	231		
At the end of the year	17	2 021	2 003	1 556	1 788

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

1. CORPORATE INFORMATION

Denel SOC Ltd is a company incorporated and domiciled in SA. The consolidated annual financial statements are presented in South African Rand (ZAR/Rand), rounded off to the nearest million (Rm) unless stated otherwise.

The consolidated annual financial statements for the year ended 31 March 2017 comprise the company, its subsidiaries and associated companies.

1.1 STATEMENT OF COMPLIANCE

The consolidated annual financial statements have been prepared in accordance with IFRS, the Companies Act and PMFA. The principal accounting policies adopted in the preparation of the consolidated annual financial statements are set out below:

BASIS OF PREPARATION

The consolidated annual financial statements are prepared on the historic cost basis, with the exception of derivative financial instruments, financial instruments at fair value through profit and loss, and investment properties, which are measured at fair value.

The preparation of the consolidated annual financial statements in conformity with IFRS requires management to exercise its judgement, as well as make certain critical accounting estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. The actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of IFRS that have a significant effect on the consolidated annual financial statements and estimates with a significant risk of material adjustment in the following financial year are discussed in note 1.2.

CHANGES IN ACCOUNTING POLICIES, RECLASSIFICATIONS AND DISCLOSURES

The accounting policies adopted are consistent with those of the previous financial year.

BASIS OF CONSOLIDATION

The consolidated annual financial statements reflect the financial position and operating results of the company, its subsidiaries and associated companies. The accounting policies have been applied consistently throughout the group.

An investee is consolidated in the group annual financial statements only if the group has control over the investee. Control over an investee is determined by three elements. The group controls an investee if the group has:

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee; and
- The ability to use its power over the investee to affect its returns, regardless of whether the power is exercised.

When the group has less than a majority of the voting or similar rights of an investee, the group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangement with the other vote holders of the investee;
- Rights arising from other contractual arrangements; and
- The group's voting rights and potential voting rights.

Where the company's interest in subsidiaries is less than 100%, the portion attributable to outside shareholders is reflected in non-controlling interest (refer note 20). Transactions with non-controlling interests are treated as transactions with equity owners of the group. For purchases from non-controlling interests, the difference between the consideration paid and relevant share acquired is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity where there is no loss of control.

The group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. The consolidation of a subsidiary commences when the group obtains control over the subsidiary and ceases when the group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated annual income statements and statements of comprehensive income from the date the group gains control until the date the group ceases to control the subsidiary.

INVESTMENTS IN SUBSIDIARIES AND ASSOCIATED COMPANIES

When the group ceases to have control, any retained interest in the business entity is re-measured at its fair value, with the change in the carrying amount recognised in profit and loss and it derecognises the assets (including any goodwill) and liabilities of the subsidiary at their carrying amounts at the date when control ceases. The fair value is the initial carrying amount for the purpose of subsequent accounting for the retained interest as an associated company, joint venture or financial asset.

Associated companies are those entities in which the group holds an equity interest and has significant influence, but which are not subsidiaries or joint ventures. The consolidated annual financial statements include the group's share of total recognised profits or losses of associated companies on an equity accounting basis, from the date significant influence commences until the date that significant influence ceases. Where the financial year-end of an associated company is different from that of the group, the share of recognised profit and loss of that associated company is adjusted only where the effect of transactions or events that occur between that date and 31 March is significant. When the group's share of losses exceeds its interest in an associated company, the group's carrying amount is reduced to Rnil and recognition of further losses is discontinued, except to the extent that the group has incurred legal or constructive obligations or made payments on behalf of the relevant associated company.

The considerations made in determining significant influence or joint control is similar to those necessary to determine control over subsidiaries.

SEPARATE FINANCIAL STATEMENTS

In the separate annual financial statements, investment in subsidiaries and associated companies that are not classified as held for sale in terms of *IFRS 5, Non-current assets held for sale and discontinued operations*, are accounted for at cost, less any impairment.

TRANSACTIONS ELIMINATED ON CONSOLIDATION

All inter-group transactions, balances and unrealised gains and losses are eliminated in preparing the consolidated annual financial statements. Unrealised gains arising from transactions with associated companies are eliminated to the extent of the group's interest in the business entity.

1.2 SIGNIFICANT JUDGEMENTS AND ESTIMATES

In the process of applying the group's accounting policies, the following judgements and estimates have been made, which are considered to have the most significant effect on the amounts recognised in the consolidated annual financial statements:

1.3 JUDGEMENTS

REVENUE, CONTRACT RISKS AND ONEROUS CONTRACTS

Management made significant judgements on the following contracts or programmes (for a more detail discussion refer to the directors' report, pages 116 to 119):

A400M contract

The contract costs to completion on the A400M contract have been calculated based on management's best estimates regarding labour hours, material costs and escalations, taking into account the technical and industrial uncertainties attached to the programme.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

ASSOCIATED COMPANIES

When considering control over an investment, the group considers the following facts which are significant to the shareholder' agreements for all associated companies whether:

- Denel has only one equity partner for each of the associated companies and the equity partner holds the majority of the shareholding;
- Denel and the equity partner will fund the company or guarantee funding, if additional funding is needed, in the same ratio as their shareholding;
- The equity partner has the right to appoint the majority of the board members;
- The equity partner has the right to appoint the CEO and CFO; and
- The equity partners are responsible for the day to day running and performance of the companies.

Where a material associated company uses accounting policies that differ from those of Denel, the associated company's annual financial statements are adjusted to reflect uniform accounting policies in applying the equity method.

DEFERRED TAX ASSET

Management has made judgement that there will be future taxable profit against which the deferred assets may be utilized.

ESTIMATES

REVENUE, CONTRACT RISKS AND ONEROUS CONTRACTS

The group accounts for a group of contracts, whether with a single customer or several customers as a single construction contract when the contracts are so closely inter-related that they are, in effect, part of a single project with an overall profit margin.

The group uses the percentage of completion method in accounting for recognising its contract revenue. The stage of completion is determined based on the costs incurred to date as a percentage of total estimated cost of each contract.

Contract revenue comprises the initial amount of revenue agreed in the contract, contract variation orders (CVOs) and claims and incentive payments.

Business entities in the group evaluate cost to completion on all contracts to determine the extent of revenue to be recognised, as well as to assess the profitability of a contract. In the instance where costs exceed expected revenue, a provision for contract losses is raised. In determining the cost to completion, the following assumptions are used:

- Labour hours are estimated based on a review of the outstanding functionalities and the experience of the project managers in conducting similar processes, as well as their understanding of the requirements. In cases where the process requires new and unique work, anticipated hours are used;
- The average labour rates are determined from known company labour rates based on normal capacity (determined during the annual budget process) for specialists and specific functional areas, depending on the mix of various processes and work content;
- Manufacturing overheads are allocated pro rata according to *IAS 11, Construction contracts.* Indirect costs are not specifically allocated to a product or an activity;
- Material costs are based on the engineering or production bills of material together with the latest material prices available. This also includes the purchasing price, import and purchasing levies, freight and handling costs and all direct procurement costs, less discounts and subsidies on purchases;
- Inflation and rates of exchange adjustments are made based on information supplied by reputable banks; and
- Technical obsolescence on aircraft and missile contracts where rapidly changing technology may result in a re-engineering requirement on these systems.

IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT

The group's impairment assessments for property, plant and equipment are based on fair value less cost of disposal using the estimated fair value of the assets less the estimated costs of disposal. Impairment assessments were performed on assets that demonstrated possible impairment indicators or change to originally determined indicators, including available capacity against the requirements.

PRODUCT WARRANTIES

Anticipated warranty cost is based on the technical risk estimations in terms of single opportunity production contracts and historical data in terms of repetitive production type contracts. The estimation is based on past experience (proven results) and varies per type of contract. This is expressed as a percentage of cost of sales, ranging from 0% to 10%, and is determined at the quotation phase and reviewed on a regular basis.

SITE RESTORATION

Certain business entities within the group carry out manufacturing and testing activities that contaminate the land on which they are situated. Management performed a detailed study in consultation with external specialists in the Denel Land Systems business entity that was identified as the most likely area to have such contamination. Following the study, a high-level review of the remaining business entities was performed, taking into consideration the results of the study and the nature of their business activities.

An estimate of the provision was determined based on consideration of the most stringent but realistic remediation objectives, based on current or future potential land-uses for the sites with due consideration given to the current legislative framework and local best practice.

In determining the provision for decommissioning, three key component costs were considered, namely:

- Remediation of contaminated land (typically soils and waste materials);
- Decommissioning of plant and equipment; and
- Demolition of buildings.

The amount raised as a provision was based on the detail study performed, taking into account the expected timing of decontamination ranging between three and 30 years. The anticipated future cash flows determined, based on a long-term inflation rate of 6.68%% (2015/16: 5.9%) have been discounted at an interest rate of 10.01% (2015/16: 10%), which is based on the risk-free rate of return and the expected long-term inflation rate.

COUNTERTRADE

The group endeavours to fulfil its countertrade obligations as indicated in note 25.5 of the consolidated annual financial statements. Certain obligations have been transferred to participating parties by means of back-to-back agreements.

Estimates used in calculating these obligations are as follows:

- Obligations for countertrade vary between 60% and 100% of export revenue;
- Calculation of possible liquidated damages or cost of exchanging credits should the group not fulfil its obligations is based on negotiations to exchange countertrade credits or the maximum penalty payable (between 4% and 100%) of the milestone obligation as mentioned above; and
- Exchange rates as at year-end have been used to convert the obligations to Rand.

POST-EMPLOYMENT BENEFIT OBLIGATIONS

The cost of the post-employment medical benefits is determined using an actuarial valuation. The actuarial valuation involves making assumptions about discount rates, expected rates of return on assets, mortality rates and medical cost inflation. Due to the long-term nature of this plan, such estimates are subject to significant uncertainty.

1.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1.4.1 REVENUE RECOGNITION

CONTRACT REVENUE

Contract revenue and costs relating to long-term construction contracts are recognised in profit and loss in proportion to the stage of completion of the project at year-end if the outcome of a contract can be estimated reliably. However, when the outcome of a contract cannot be reliably measured, revenue is recognised to the extent of contract costs incurred that are probable of being recovered, while contract costs are recognised in the period in which they are incurred. Expected losses on contracts are recognised immediately and in full and where it is probable that the total costs will exceed total revenue, the expected loss is recognised immediately. An expected loss is recognised as an expense. Depending on the nature of the contract, the stage of completion is determined as follows:

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

- For specific identified development contracts of sub-assemblies where there is a significant amount of uncertainty, the stage of completion is based on the extent of achievement of predetermined milestones within the contract. These significant uncertainties are only satisfied once customer certification takes place.
- On all other contracts, the stage of completion is determined with reference to costs incurred to date as a percentage of total estimated costs.

Contract revenue comprises:

- The initial amount of revenue agreed in the contract;
- Variations in contract work and incentive payments:

  i) To the extent that it is probable that it will result in revenue; and
  ii) It can be reliably measured.

- A claim is an amount that the group seeks to collect from the customer or another party as reimbursement for costs not included in the contract price. The measurement of the amounts of revenue arising from claims is subject to a high level of uncertainty and often depends on the outcome of negotiations. Therefore, claims are included in contract revenue only when:

  i) Negotiations have reached an advanced stage such that it is probable that the customer will accept the claim; and
  ii) The amount that is probable will be accepted by the customer and can be measured reliably. An expected loss on a contract is recognised immediately in profit and loss.

SALE OF GOODS AND SERVICES

Revenue from sale of goods and services comprises the invoiced value of goods and services, net of value added tax (VAT), rebates and discounts.

Revenue from the sale of goods is recognised in profit and loss when significant risks and rewards of ownership have been transferred to the buyer and the amount of revenue can be measured reliably.

No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due, associated costs or the possible return of goods and continuing management involvement with the goods.

INCOME FROM INVESTMENT PROPERTIES

Income from investment properties comprises mainly rental income received in terms of rental agreements and is recognised on a straight-line basis over the lease terms.

FINANCE INCOME AND COSTS

Finance income comprises mainly interest income on funds invested.

Finance income is recognised using the effective interest rate method when it is determined that such income will accrue to the group.

Finance costs mainly comprise interest expense on borrowings, unwinding of the discount on provisions and impairment losses recognised on financial assets.

OTHER INCOME

Other income is any income that accrues to the group from activities that are not part of the normal operations and is recognised as it is earned.

DIVIDENDS RECEIVED

Dividends are recognised in profit and loss when the right to receive the payment is established.

GOVERNMENT GRANTS RECEIVED

Government grants are recognised at fair value when there is reasonable assurance that the grant will be received and all relevant conditions will be complied with.

Where the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate.

1.4.2 PROVISIONS

Provisions are recognised when the group has a present legal or constructive obligation as a result of past events, for which it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability. The impact of the periodic unwinding of the discount is recognised in profit and loss as finance cost as it occurs.

Further details in this regard are contained in note 23.

1.4.3 TAXES

Income tax for the year comprises current and deferred tax. Income tax is recognised in profit and loss, except to the extent that it relates to items recognised directly in other comprehensive income (OCI).

Current tax expense is the expected tax payable on the taxable income (the results for the year, adjusted for items that are not taxable or not deductible) for the year. The group's liability for current taxation is calculated using tax rates and laws that have been enacted or substantially enacted at the reporting date and any adjustments relating to prior years.

Taxes are deferred for temporary differences between the values in the statement of financial position according to IFRS and according to their tax base. Deferred tax is not provided for the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination, and at the time of the transaction, affects neither the accounting profit and loss nor taxable profit and loss. Deferred tax is recognised in full on temporary differences arising from investments in subsidiaries and associated companies, except where the timing of the reversal of the temporary difference is controlled by the group and it is probable that the temporary difference will not reverse in the foreseeable future.

A deferred tax liability is recognised to the extent that the carrying value of an asset is greater than its tax base, or where the carrying value of a liability is less than its tax base.

A net deferred tax asset is regarded recoverable and therefore only recognised when, on the basis of all available evidence, it is probable that future taxable profit will be available against which the temporary differences (including carried forward tax losses) can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related taxation benefit will realised.

Deferred tax assets and liabilities are recognised on a net basis for each tax entity. Deferred tax assets and liabilities are offset when the related income taxes are levied by the same taxation authority, there is a legally enforceable right to offset and there is an intention to settle the balances on a net basis.

Deferred tax is measured at the tax rates expected to apply in the periods in which the timing differences are expected to reverse based on tax rates and laws that have been enacted or substantively enacted at the reporting date. Deferred tax is measured on a non-discounted basis.

Revenue, expenses and assets are recognised net of the amount of VAT except:

- Where the VAT incurred on the purchase of assets or services is not recoverable from the taxation authority, in which case the VAT is recognised as part of the cost of acquisition of the asset or as part of the expense item applicable; and
- Receivables and payables that are stated with the amount of VAT included.

The net amount of VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the consolidated statements of financial position.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

1.4.4 FINANCIAL INSTRUMENTS

The group initially recognises financial assets and liabilities on the trade date at which the group becomes a party to the contractual provisions of the instrument.

NON-DERIVATIVE FINANCIAL INSTRUMENTS

Non-derivative financial instruments comprise trade and other receivables, cash and short-term deposits, loans and borrowings, bank overdrafts and trade and other payables.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit and loss, any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below:

FINANCIAL ASSETS

The group has the following classes:

» Financial assets at fair value through profit and loss; and
» Loans and receivables (including insurance receivables and cash and cash equivalents).

Loans receivable
Loans receivable are subsequently measured at amortised cost. The amortised cost is determined using the effective interest rate method. Where a loan has been impaired, the impairment loss is recognised as an expense in profit and loss in the period in which the impairment has occurred.

Trade and other receivables
Trade and other receivables are carried at amortised cost less impairment losses. Impairment losses are recognised in profit and loss and are measured as the difference between the carrying amount and the present value of estimated future cash flows discounted at the original effective rate of receivables. Once an impairment loss has been recognised, recovery proceedings are continued. Impairment losses are decreased in subsequent periods only if the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment loss was recognised.

Cash and cash equivalents
Cash and cash equivalents comprise cash on hand, deposits held on call with banks, net of bank overdrafts, and investments in money market instruments with an original maturity of three months or less, all of which are available for use, unless otherwise stated.

FINANCIAL LIABILITIES

A financial liability is any liability that is a contractual obligation to deliver cash or another financial asset to another entity.

Financial liabilities are initially measured at fair value less transaction costs that are directly attributable to the raising of funds, and are subsequently carried at amortised cost. Any difference between the proceeds, net of transaction costs and the redemption value is recognised in profit and loss over the period of the borrowing.

Borrowings
After initial recognition, interest-bearing borrowings are measured at amortised cost using the effective interest rate method. Amortised cost is calculated after having taken into account any issue costs, discounts and premium on settlement. Interest-bearing borrowings are classified as current liabilities unless the group has an unconditional right to defer settlement of the liability for at least 12 months from the reporting date.

Trade and other payables
After initial recognition, trade and other payables are stated at amortised cost. Gains and losses on the de-recognition process are recognised in profit and loss.

DERIVATIVE FINANCIAL INSTRUMENTS

The group holds derivative financial instruments to hedge its exposure to foreign exchange risks arising from operational activities, and its exposure to volatility in commodity prices. The group does not hold these derivative financial instruments for trading purposes. The assets are initially measured at fair value. Subsequent to initial recognition, derivative financial instruments are stated at fair value. Any gains or losses on the measurement of the derivative financial instruments are recognised in profit and loss. The fair value of derivative financial instruments is determined by reference to the quoted market price for assets held or liabilities to be settled at the reporting date.

EMBEDDED DERIVATIVES

Embedded derivatives are separated from the host contract and accounted for separately. The group contracts in various currencies based on the preference and location of the customer. Where the economic characteristics and risks of the host contract and the embedded derivative are not closely related, then the embedded derivative is recognised separately. The embedded derivative is measured at fair value through profit and loss.

Foreign exchange embedded derivatives are brought into account when the group has entered into contracts denominated in foreign currencies, which are neither the measurement currencies of parties to the contract, nor the currencies in which those commodities are routinely traded in international commerce except if such currency is a common currency. Denel views the United States Dollar (USD), Pound Sterling (GBP) and EURO (EUR) as common currencies.

All foreign exchange embedded derivatives are measured at fair value. Gains or losses arising on subsequent measurement of embedded derivatives are recognised in profit and loss. The embedded derivative assets or liabilities are released to revenue, cost of sales, operating costs or a related asset to reflect a Rand host contract at the initial expected forward rate when risks and rewards pass to customers or the group.

OFFSET

Where a legally enforceable right of offset exists for recognised financial assets and financial liabilities, and there is an intention to settle the liability and realise the asset simultaneously, or to settle on a net basis, all related financial effects are offsetted.

DE-RECOGNITION OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

» The contractual rights to receive cash flows from the asset have expired; or
» The group retains the contractual right to receive cash flows from the asset, but has assumed an obligation to pay it in full without material delay to a third party under a 'pass-through' arrangement; or
» The group has transferred its contractual rights to receive cash flows from the asset and either:

- Has transferred substantially all the risks and rewards of the asset of ownership, or
- Has neither transferred nor retained substantially all the risks and rewards of ownership of the asset, but has transferred control of the asset.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expired. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a de-recognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit and loss.

1.4.5 FOREIGN CURRENCIES

FUNCTIONAL AND PRESENTATION CURRENCY

Items included in the annual financial statements of each of the group's business entities are measured using the currency of the primary economic environment in which the business entity operates (the functional currency). The consolidated annual financial statements are presented in Rand, which is the group's functional and presentation currency.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

RECORDING OF FOREIGN TRANSACTIONS

Foreign exchange transactions are accounted for at the foreign exchange rate ruling at the date of the transaction.

TRANSLATION OF FOREIGN CURRENCY TRANSACTIONS

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to Rand at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in profit and loss. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the prevailing date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to Rand at foreign exchange rates ruling at the dates the fair value was determined.

1.4.6 INVESTMENT PROPERTIES

Investment properties comprise property held to earn rentals, for long-term capital appreciation or both, and are not occupied by the group. Investment properties are treated as long-term investments and are initially measured at cost. Investment property shall be recognised as an asset when it is probable that the future economic benefits that are associated with the investment property will flow to the entity and the cost of the investment property can be measured reliably. All costs including the transaction costs of the property are included on initial recognition.

Subsequent to initial recognition, investment properties are carried at fair value, determined annually by independent external registered appraisers. Changes in fair value are recognised in profit and loss. The fair values are based on market values, being the estimated amount for which a property could be exchanged on the date of the valuation between a willing buyer and a willing seller in an arm's length transaction. This falls into level 3 of the fair value hierarchy.

The valuations are prepared by considering the aggregate of the net annual rentals receivable from the properties and where relevant, associated costs. A yield that reflects the specific risks inherent in the net cash flows is then applied to the net annual rentals to arrive at the property valuation. The range of RSA yields applied for each type of property is included below:

- Offices 10% to 15%; and
- Manufacturing 10% to 15%.

Valuations reflect, where appropriate, the type of tenants actually in occupation or responsible for meeting lease commitments or likely to be in occupation after letting of vacant accommodation and the market's general perception of their creditworthiness, the allocation of maintenance and insurance responsibilities between lessor and lessee, and the remaining economic life of the property. It has been assumed that whenever rental reviews or lease renewals are pending with anticipated revisionary increases, all notices and, where appropriate, counter-notices have been served validly and within the appropriate time.

Income from investment properties is accounted for as described in the revenue recognition policy. Compensation from third parties for investment property that was impaired, lost or given up is recognised in profit and loss when the compensation becomes receivable.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment, and its fair value at the date of reclassification becomes its cost for accounting purposes for subsequent recording. When the group begins to redevelop an existing investment property for continued future use as investment property, the property remains an investment property, which is measured based on the fair value model, and is not reclassified as property, plant and equipment during the development.

Investment properties are derecognised when they are either disposed of or permanently withdrawn from use and no future economic benefits are expected from their disposal. The difference between the net disposal proceeds and the carrying amount of the asset on retirement or disposal is recognised in profit and loss.

A property interest under an operating lease is classified and accounted for as an investment property on a property-by-property basis when the group holds it to earn rentals and for capital appreciation or both. Any such property interest under an operating lease is classified as an investment property and carried at fair value. Lease payments are accounted for as described in the accounting policy for leases.

1.4.7 PROPERTY, PLANT AND EQUIPMENT

The cost of an item of property, plant and equipment is recognised as an asset when it is probable that future economic benefits associated with the item will flow to the entity; and the cost of the item can be measured reliably. On initial recognition the assets are measured at cost.

Land is stated at its original cost price adjusted for impairment and is not depreciated. Other items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses.

The cost of an item of property, plant and equipment includes all costs that are incurred in order to bring the asset into a location and condition necessary to enable it to operate as intended by management and includes the cost of materials, direct labour and the initial estimate, where applicable, of the costs of dismantling and removing the item and restoring the site on which it is located.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment and depreciated separately.

Repairs and maintenance costs are recognised in profit and loss during the year in which it is incurred.

DEPRECIATION

Depreciation is provided on the straight-line basis which, it is estimated, will reduce the carrying amount of the assets to their residual values at the end of their useful lives. Lease improvements on leasehold properties are depreciated over the period of the lease or the expected useful life, whichever is the shorter period.

The estimated useful lives are as follows:

- Buildings 20 to 50 years;
- Plant, machinery and equipment 3 to 60 years;
- Vehicles 5 years;
- Office furniture 3 to 20 years; and
- Computer equipment 3 to 5 years

The determination of the useful economic life and residual values of property, plant and equipment is subject to management estimation. The group reviews all of its depreciation rates and residual values annually, to take account of any changes in circumstances, as well as any changes that could affect prospective depreciation charges and asset carrying values.

SUBSEQUENT EXPENDITURE

Subsequent expenditure relating to an item or part of an item of property, plant and equipment is capitalised when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. The carrying amount of the part that is replaced is derecognised in accordance with the principles set out below. All other costs are recognised in profit and loss as an expense when incurred.

DE-RECOGNITION

The carrying amount of an item of property, plant and equipment shall be derecognised at the earlier of:

- The date of disposal; or
- The date when no future economic benefits are expected from its use or disposal.

Gains and/or losses on de-recognition of items of property, plant and equipment are recognised in profit and loss.

TRANSFER TO INVESTMENT PROPERTIES

When an item of property, plant and equipment is transferred to investment properties following a change in its use, it is transferred to investment properties at its fair value at date of transfer. Any differences arising at the date of transfer between the carrying amount of the item immediately prior to the transfer and its fair value is recognised in other comprehensive income if it is a gain and in profit and loss if it is a loss.

SPARE PARTS

Major spare parts and servicing equipment qualify as property, plant and equipment when the group expects to use them for more than 12 months. Similarly, if the major spare parts and servicing equipment can be used only in connection with an item of property, plant and equipment, they are accounted for as property, plant and equipment.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

1.4.8 LEASES

The determination of whether an arrangement is, or contains a lease, is based on the substance of the arrangement at inception date of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset.

Leases that transfer substantially all the risks and rewards of ownership of the underlying asset to the group are classified as finance leases. Assets and liabilities acquired in terms of finance leases are capitalised at the lower of fair value and the present value of the minimum lease payments at inception of the lease. The discount rate used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease. The leased assets are depreciated over their estimated useful life. The capital element of future obligations under the leases is included as a liability in the consolidated statements of financial position.

Leases, where the lessor retains the risks and rewards of ownership of the underlying asset, are classified as operating leases. Payments made under operating leases are recognised in profit and loss on a straight-line basis over the term of the lease.

The interest expense component of finance lease payments is recognised in profit and loss using the effective interest rate method.

1.4.9 INTANGIBLE ASSETS

Intangible assets that are acquired separately by the group are initially measured and recognised at cost. Such cost are recognised only if it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity and the cost of the asset can be measured reliably. Subsequently, intangible assets are carried at cost less accumulated amortisation and accumulated impairment losses. Intangible assets are derecognised when they no longer meet the recognition criteria of an asset. This could be either when they are disposed of or where no future economic benefits are expected from use or disposal. The difference between the net disposal proceeds, if any, and the carrying amount of the assets on derecognition is recognised in profit and loss.

Intangible assets with a finite useful life are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation is charged to profit and loss on the straight-line basis over the estimated useful lives of intangible assets. The amortisation period and amortisation method are reviewed annually and any change is treated as a change in estimate.

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

RESEARCH AND DEVELOPMENT COSTS

Research costs are expensed in the year in which they are incurred. Development costs are capitalised only when the group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the ability of resources to complete and the availability to measure reliably the expenditure during the development period. Development costs initially recognised as an expense are not recognised as an asset in a subsequent period. Capitalised development costs are reviewed annually and are expensed if they no longer meet the criteria for capitalisation.

The amortisation of capitalised development costs commences once the product or service becomes available for sale or use. Capitalised development costs are amortised over the period of expected future economic benefits associated with the specific asset.

PATENTS

Patents are recognised at cost if it is probable that future economic benefits will flow to the group. Amortisation is charged on a systematic basis over the estimated useful lives of patents, where its legal rights determine the amortisation periods.

COMPUTER SOFTWARE

Computer software is initially measured and recognised at cost. Subsequently, intangible assets are carried at cost less accumulated amortisation and accumulated impairment losses. Amortisation is charged on a systematic basis over the estimated useful life of the software. The useful life of computer software is estimated to be between three and five years. Annual license fees on software are expensed in the year of accrual.

BUSINESS COMBINATIONS AND GOODWILL

Business combinations are accounted for using the acquisition method. This involves recognising identifiable assets (including previously unrecognised intangible assets) and liabilities (including contingent liabilities and excluding future restructuring costs) of the acquired business at fair value.

Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the business combination over the group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the group's cash-generating entities, or groups of cash-generating entities that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the group are assigned to those entities or groups of entities. Each entity or group of entities to which the goodwill is allocated:

» Represents the lowest level within the group at which the goodwill is monitored for internal management purposes; and
» Is not larger than a segment based on the group's reporting format determined in accordance with *IFRS 8, Segment reporting.*

Where goodwill forms part of a cash-generating entity or group of cash-generating entities, and part of the operation within that entity is disposed, the goodwill associated with the operation disposed is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed in this circumstance is measured based on the relative values of the operation disposed and the portion of the cash-generating entity retained.

When subsidiaries are sold, the difference between the selling price and the net assets plus cumulative translation differences and goodwill, is recognised in profit and loss.

A bargain purchase arising on acquisition is recognised immediately in profit and loss.

1.4.10 IMPAIRMENT

FINANCIAL ASSETS

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised in profit and loss.

NON-FINANCIAL ASSETS

The carrying amounts of the group's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. Internal and external indicators are considered. If any such indication exists, the asset's recoverable amount is estimated. The recoverable amount of non-financial assets is the greater of their fair value less cost of disposal and value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. In assessing the value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash flows, the recoverable amount is determined based on the cash-generating entity to which the asset belongs.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

For intangible assets that are not yet available for use, the recoverable amount is estimated at each reporting date.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating entity exceeds its recoverable amount. Impairment losses are recognised in profit and loss.

Impairment losses recognised in respect of cash-generating entities are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating entities and then to reduce the carrying amount of the other assets in the entity on a pro rata basis.

REVERSALS OF IMPAIRMENT

An impairment loss in respect of receivables carried at amortised cost is reversed if the subsequent increase in the recoverable amount can be related objectively to an event occurring after the impairment loss was recognised. Any subsequent reversal of an impairment loss is recognised in profit and loss to the extent that the carrying amount of the asset does not exceed its amortised cost at the reversal date.

An impairment loss in respect of goodwill is not reversed.

In respect of other non-financial assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount since the impairment loss was recognised.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. Such reversal is recognised in profit and loss. After such a reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

1.4.11 INVENTORIES

Inventories are measured at the lower of cost or net realisable value using the first-in-first-out (FIFO) formula. Net realisable value is the estimate of the selling price in the ordinary course of business less the cost of completion and selling expenses. The weighted average basis is used for certain inventory items, such as chemicals and liquids where it is not practical to apply the FIFO basis. The standard cost method is used where the results approximate the actual cost. Under a standard costing system the cost of a product is determined using predetermined rates for the material, labour and overhead expenses based on manufacturing specifications. Where inventory has been acquired on extended credit terms, the cost is adjusted with the interest expense and recognised over the payment period in profit and loss. Where trade discounts, rebates and similar items are received, it is deducted in determining the cost of inventory.

The following specific methods are applied in determining cost price:

RAW MATERIALS AND BOUGHT-OUT COMPONENTS

These are valued at direct cost of purchase plus the other costs incurred to bring it to their present location and condition.

WORK-IN-PROGRESS AND FINISHED PRODUCTS

These are valued at cost and include the cost of purchase of direct materials, direct labour, allocated variable and fixed production overheads based on normal production levels.

CONSUMABLE INVENTORIES

Consumable inventories, such as spare parts and maintenance equipment, are valued at the direct cost of purchase and classified as inventory.

1.4.12 BORROWING COSTS

Borrowing costs incurred on qualifying assets under construction are capitalised up to the date the assets are substantially complete. Capitalisation is suspended during extended periods in which active development is interrupted. All other borrowing costs are recognised as finance costs when incurred.

1.4.13 ADVANCE PAYMENTS RECEIVED FROM REVENUE CONTRACTS

In the case of comprehensive and/or long-term revenue contracts, advance payments are negotiated with local and foreign customers. These funds are used to finance the execution of contracts, which include advance payments to suppliers, finance long-lead inventory items and work-in-progress. Guarantees are provided to customers for advance payments received. Advance payments received are recognised as a current liability for an amount that is estimated to be settled within one year from reporting date and as a non-current liability for the amount to be settled after one year from reporting date. Advance payments received in foreign currency are recognised at the ruling spot rate on the date of receipt. Guarantees provided are disclosed as contingent liabilities.

1.4.14 EMPLOYEE BENEFITS

PENSION OBLIGATIONS

The group participates in a defined contribution fund, the assets of which are held in a separate trustee administered fund.

The group's obligations for contributions to the defined contribution retirement fund are recognised as an expense in profit and loss in the year to which they relate.

OTHER POST-RETIREMENT OBLIGATIONS

The group provides post-retirement medical aid contribution subsidies to qualifying retirees. The expected cost of this benefit is accrued over the period of employment and is funded by the Denel Medical Benefit Trust (DMBT). Independent qualified actuaries carry out valuations of these obligations on an annual basis (refer note 32.1).

1.4.15 COUNTERTRADE OBLIGATIONS

Countertrade obligations arise when the group has entered into export contracts where the buyer's country requires countertrade by the group or where the group has entered into local defence contracts that require the group to impose countertrade obligations on suppliers in favour of SA on all imported content. Countertrade obligations can be a percentage of the value of the export contract up to 100%. The buyer's country normally requires a combination of the following to discharge the obligation:

- Procurement of products and services from suppliers in the buyer's country; or
- Participation in a business venture or a form of investment in the buyer's country is prescribed.

Countertrade obligations are disclosed as contingent liabilities, and are only brought into account as liabilities to the extent that there are present obligations to settle.

1.4.16 SEGMENT REPORTING

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker (which includes a measure of segments' assets). The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the exco of Denel SOC Ltd.

1.4.17 HEDGE ACCOUNTING

For the purpose of hedge accounting, hedges are classified as:

- Fair value hedges when hedging the exposure to changes in the fair value of a recognised non-financial asset or non-financial liability or an unrecognised firm commitment; and
- Hedges of a net investment in a foreign operation.

If a fair value hedge meets the conditions for hedge accounting, any gain or loss on the hedged item attributable to the hedged risk is included in the carrying amount of the hedged item and is recognised in profit and loss.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

If an effective hedge of a forecast transaction subsequently results in the recognition of a financial asset or financial liability, the associated gain or loss recognised are recognised in profit and loss in the same period.

If a hedge of a net investment in a foreign entity meets the condition for hedge accounting, the portion of the gain or loss on the hedging instruments that is determined to be an effective hedge is recognised in OCI and the ineffective portion is recognised in profit and loss. On disposal of a foreign entity, the gain or loss recognised in equity is transferred to profit and loss as a reclassification adjustment.

Hedge accounting is discontinued on a prospective basis when the hedge no longer meets the hedge accounting criteria (including when it becomes ineffective), when the hedge instrument is sold, terminated or exercised when, the forecast transaction is no longer expected to occur or when the hedge designation is revoked.

1.4.18 NON-CURRENT ASSETS HELD FOR SALE

Assets are classified as non-current assets held for sale if the carrying amount would be recovered mainly through a sale transaction and not through continued use. This condition is regarded as met when a sale is highly probable; the asset or disposal group is available for immediate sale in its present condition and when management is committed to the sale. A business entity to be partially disposed, which remains to be consolidated, is not classified as held for sale.

Immediately before classification as held for sale, the measurement of the assets is done in accordance with applicable IFRSs. Then, on initial classification as held for sale, non-current assets or disposal groups are recognised at the lower of carrying amount and fair value less costs to its subsequent disposal.

Impairment losses on initial classification as held for sale are recognised in profit and loss. Gains, limited to previously recognised impairment losses and losses on subsequent measurement, are also recognised in profit and loss.

1.5 STANDARDS, INTERPRETATIONS AND AMENDMENTS ISSUED THAT ARE NOT YET EFFECTIVE

The following accounting standards, interpretations and amendments to publish accounting standards which are relevant to Denel but not yet effective, have not been adopted in the current year. The group is currently in the process of evaluating the detailed requirements of the following amendments to assess the possible impact on the group's consolidated annual financial statements:

NUMBER	TITLE	EFFECTIVE DATE
	Standards and amendments	
IFRS 9	***Financial instruments*** – Guidance on classification and measurement, impairment, hedge accounting and de-recognition. This standard replaces *IAS 39, Financial instruments: Recognition and measurement.*	1 January 2019
IFRS 15	***Revenue from contracts from customers*** – Provides a single, principle based five-step model to be applied to all contracts with customers.	1 January 2019
IFRS 16	***Leases*** – New standard that requires a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value.	1 January 2019
IAS 40	***Investment property*** – Transfers of investment property: Clarification of the requirements on transfers to, or from, investment property.	1 January 2018
IAS 7	***Statement of cash flows*** – The amendments require entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities rising from financing activities.	1 January 2017
IAS 12	***Income taxes*** – Recognition of deferred tax assets for unrealised losses narrow-scope amendment to clarify the requirements on recognition of deferred tax assets for unrealised losses on debt instruments measured at fair value.	1 January 2018

NUMBER	TITLE	EFFECTIVE DATE
	Interpretations	
IFRIC 22	***Foreign currency transactions and advance consideration*** – This interpretation addresses the exchange rate to use in transactions that involve advance consideration paid or received in a foreign currency.	1 January 2018

IFRS 9, Financial instruments

The completed standard comprises guidance on classification and measurement, impairment hedge accounting and derecognition. This standard introduces the following:

» A new approach to the classification of financial assets, which is driven by the business model in which the asset is held and their cash flow characteristics; and

» A new business model was introduced which does allow certain financial assets to be categorised as "fair value through OCI" in certain circumstances. The requirements for financial liabilities are mostly carried forward unchanged from *IAS 39, Financial instruments: Recognition and measurement*. However, some changes were made to the fair value option for financial liabilities to address the issue of own credit risk, the model introduces a single impairment model being applied to all financial instruments, as well as an "expected credit loss" model for the measurement of financial assets. IFRS 9 contains a new model for hedge accounting that aligns the accounting treatment with the risk management activities of an entity, in addition enhanced disclosures will provide better information about risk management and the effect of hedge accounting on the financial statements. IFRS 9 carries forward the derecognition requirements of financial assets and liabilities from IAS 39.

Denel will consider and apply the requirements of this new standard in the 2017/18 financial year.

IFRS 15, Revenue from contracts with customers

IFRS 15 provides a single, principle-based five-step model to be applied to all contracts with customers. The five steps in the model comprise of identifying the contract, identifying performance obligations in the contract, determining the transaction price, allocating transaction price to performance obligations in the contract and recognising revenue when (or as) the entity satisfies a performance obligation. Denel will consider and apply the requirements of this new standard in the 2017/18 financial year.

IFRS 16, Leases

IFRS 16 provides a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments. A lessee measures right-of-use assets similarly to other non-financial assets (such as property, plant and equipment) and lease liabilities similarly to other financial liabilities. As a consequence, a lessee recognises depreciation of the right-of-use asset and interest on the lease liability, and also classifies cash repayments of the lease liability into a principal portion and an interest portion and presents them in the statement of cash flows applying *IAS 7, Statement of cash flows*. Denel will consider and apply the requirements of this new standard in the 2017/18 financial year.

IAS 7, Statement of cash flows

The amendments require entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities rising from financing activities, namely: (i) changes from financing cash flows, (ii) changes arising from obtaining or losing control of subsidiaries or other businesses, (iii) the effect of changes in foreign exchange rates, (iv) changes in fair values, and (v) other changes.

The amendments will be applied prospectively and will not have a material impact on the group's consolidated annual financial statements.

IFRS 12, Income taxes

The amendments clarify that unrealised losses on debt instruments measured at fair value in the financial statements and at cost for taxation purposes give rise to a deductible temporary difference regardless of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by use. It further clarifies that (i) the carrying mount of an asset does not limit the estimation of probable future taxable profits, (ii) estimates for future taxable profits exclude taxation deductions resulting from the reversal of deductible temporary differences, and (iii) an entity assesses a deferred taxation asset in combination with other deferred taxation assets. Where taxation law restricts the utilisation of taxation losses, an entity would assess a deferred taxation asset in combination with other deferred taxation assets of the same type.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
2 REVENUE				
Contract revenue [1]	7 935	8 120	6 156	6 496
Sale of goods	7 775	7 976	5 973	6 329
Sale of services	160	144	183	167
Income from investment properties [2]	122	108	133	118
	8 057	**8 228**	**6 289**	**6 614**
3 COST OF SALES AND OTHER OPERATING EXPENSES				
Continuing operations				
Cost of sales	6 236	6 556	4 838	5 355
Other operating expenses	1 483	1 455	1 254	1 189
	7 719	**8 011**	**6 092**	**6 544**
Cost of sales and other operating expenses are arrived at after taking the following items into account:				
Amortisation of intangible assets (refer note 10)	11	16	7	12
Software	11	16	7	12
Auditors' remuneration	13	14	10	11
Current year	13	13	10	11
Other	-	1	-	-
Costs of inventories recognised as an expense (refer note 14)	4 032	3 025	3 097	1 868
Depreciation (refer note 8)	142	131	103	100
Buildings	29	20	25	17
Computer equipment	20	20	17	18
Office furniture	3	3	2	2
Plant and machinery	80	77	49	52
Vehicles	10	11	10	11
Directors remuneration [3]	19	12	19	12
Executive directors	16	8	16	8
Non-executive directors	3	4	3	4
Impairment (reversed)/raised	(36)	119	(77)	176
Intangible assets (refer note 10)	(72)	163	(72)	159
Inventories (refer note 3)	38	(57)	(8)	2
Trade and other receivables (refer note 15)	(2)	13	3	15
Loss on disposal of assets	-	1	-	-
Property, plant and equipment (refer note 26)	-	1	-	-
Net losses on financial instruments (refer note 5)	(232)	-	(361)	-
Operating expenses for investment properties	280	201	280	200

1. *Contract revenue also includes the sale of goods and services.*
2. *No lease incentives were granted during 2016/17 (2015/16: Rnil).*
3. *Directors' remuneration is excluded from Employees: Salaries and relevant costs. Directors' remuneration are disclosed in detail in the remuneration report, pages 103 to 105. Executive directors' remuneration is included from date of appointment as director.*

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
3 COST OF SALES AND OTHER OPERATING EXPENSES (continued)				
Operating lease payments [1]	86	96	71	81
Buildings	70	87	64	74
Computer equipment	4	5	3	4
Office furniture	4	3	4	3
Plant and machinery	8	1	-	-
Research and development costs [2]	609	544	599	523
Employees: Salaries and relevant costs [3]	2 275	2 278	1 691	1 704
Medical fund contributions	111	108	85	85
Pension costs: Defined contribution plan	177	154	146	120
Services costs	2 080	1 912	1 540	1 447
Employee and related provisions	(93)	49	(80)	7
Termination benefits	-	38	-	28
Other long-term benefit contributions	-	17	-	17
4 OTHER INCOME				
Administration and management fees	4	4	29	23
Dividends received	-	-	-	56
Fair value adjustment on investment properties (refer note 9)	48	162	48	162
Government grants received	14	18	13	18
Net gains on financial instruments (refer note 5)	-	50	-	107
Profit on disposal of property, plant and equipment (refer note 26)	-	1	-	-
Royalty income	12	-	12	-
Other [4]	58	53	71	62
	136	**288**	**173**	**428**
5 NET GAINS ON FINANCIAL INSTRUMENTS				
Settled transactions	(186)	(60)	(214)	(82)
Gains	135	156	107	134
Losses	(321)	(216)	(321)	(216)
Fair value adjustments	129	(4)	28	75
Gains	567	267	328	186
Losses	(438)	(271)	(300)	(111)
Firm commitments remeasurement	(175)	114	(175)	114
Gains	72	177	72	177
Losses	(247)	(63)	(247)	(63)
Refer note 3 and 4	**(232)**	**50**	**(361)**	**107**

1. *No lease incentives were received during 2016/17 (2015/16: Rnil).*
2. *The R&D costs are mainly customer funded. No amount (2015/16: R6m) was charged against provisions and no amount (2015/16: Rnil) has been capitalised during 2016/17.*
3. *Refer footnote 3 on page 140.*
4. *Other is mainly made up of scrap sales, insurance claims, low claim bonuses, discount received, as well as skills development levies rebates received.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
6 NET FINANCE COSTS				
The amounts below relate to financial instruments measured at amortised cost (financial liabilities, loans and receivables):				
6.1 FINANCE COSTS				
Non-current interest-bearing loans and borrowings	72	87	72	87
Current interest-bearing loans and borrowings	256	174	239	172
Inter-group finance costs			24	11
Finance costs on financial liabilities	328	261	335	270
Unwinding of discount on provisions (refer note 23.3)	24	19	24	19
	352	**280**	**359**	**289**
6.2 FINANCE INCOME				
Gross interest received	79	77	70	62
Unwinding of discount on provisions (refer note 23.3)	1	-	1	-
Inter-group finance income			21	1
	80	**77**	**92**	**63**
Net finance costs	**272**	**203**	**267**	**226**
6.3 RECONCILIATION				
Interest paid				
Finance costs (refer note 6.1)	352	280	359	289
Add back:				
Unwinding of discount on provisions (refer note 23.3)	(24)	(19)	(24)	(19)
Movement in interest accrued for the year	(11)	(31)	(11)	(31)
Discount (premium) on borrowings	(1)	-	(1)	1
As per the consolidated statements of cash flows	**316**	**230**	**323**	**240**
Interest received				
Finance income (refer note 6.2)	80	77	92	63
Add back: Unwinding of discount on provisions (refer note 23.3)	(1)	-	(1)	-
Movement in interest receivable for the year	-	-	-	2
As per the consolidated statements of cash flows	**79**	**77**	**91**	**65**

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
7 INCOME TAX EXPENSE				
SA normal tax [1]				
Current tax	11	61	-	-
Deferred tax (refer note 13)	12	(22)	-	-
	23	39	-	-
	%	%	%	%
Reconciliation of tax rate				
Effective tax rate	6.5	9.1	-	-
Adjustment in tax rate due to:	21.5	18.9	28.0	28.0
Exempt income	-	3.6	-	5.7
Deferred tax asset not recognised	10.0	13.0	24.0	26.0
Share of associated companies	12.1	8.5		
Other	(0.6)	(6.2)	4.0	(3.7)
SA normal tax rate	28.0	28.0	28.0	28.0
	Rm	Rm	Rm	Rm
The calculated tax losses available for offset against future taxable income are as follows:				
Calculated income tax losses	3 671	3 147	2 270	2 263
Capital gains tax losses	351	348	351	348
Total calculated tax losses	4 022	3 495	2 621	2 611
Calculated tax losses utilised	-	-	-	-
Net available calculated tax losses	4 022	3 495	2 621	2 611

The unused tax losses for which no deferred tax asset has been recognise is R128m (2015/16: R240m) for the group, whilst the amount for the company came to R88m (2015/16: R290m).

1. *No provision for SA normal tax has been made for any of the companies within the group that are in an assessed loss position.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	Land and buildings	Computer equipment	Office furniture	Plant and machinery	Vehicles	Assets under construction [1]	Total
	Rm	Rm	Rm	Rm	Rm	Rm	Rm
8 PROPERTY, PLANT AND EQUIPMENT							
GROUP							
2016/17							
Carrying value at 1 April	520	57	14	564	35	20	1 210
Additions	8	7	1	34	1	12	63
Depreciation for the year (refer note 3)	(29)	(20)	(3)	(80)	(10)	-	(142)
Disposals	-	-	-	(2)	-	-	(2)
Reclassification [1]	-	-	-	8	-	(8)	-
Transfer from intangible assets (refer note 10)	-	-	-	-	-	5	5
Carrying value at 31 March	**499**	**44**	**12**	**524**	**26**	**29**	**1 134**
Cost	752	279	51	1 849	130	29	3 090
Accumulated depreciation and impairment	(253)	(235)	(39)	(1 325)	(104)	-	(1 956)
Carrying value at 31 March	**499**	**44**	**12**	**524**	**26**	**29**	**1 134**
2015/16							
Carrying value at 1 April	289	67	12	488	33	26	915
Additions	33	13	3	69	12	5	135
Business acquired	77	3	2	61	1	-	144
Capitalised leases (refer note 21.1)	-	-	-	23	-	-	23
Depreciation for the year (refer note 3)	(20)	(20)	(3)	(77)	(11)	-	(131)
Disposals	-	(1)	-	-	-	-	(1)
Fair value at first consolidation	130	-	-	-	-	-	130
Reclassification [1]	11	-	-	-	-	(11)	-
Transfer to intangible assets (refer note 10)	-	(5)	-	-	-	-	(5)
Carrying value at 31 March	**520**	**57**	**14**	**564**	**35**	**20**	**1 210**
Cost	744	274	51	1 833	130	20	3 052
Accumulated depreciation and impairment	(224)	(217)	(37)	(1 269)	(95)	-	(1 842)
Carrying value at 31 March	**520**	**57**	**14**	**564**	**35**	**20**	**1 210**

Registers of property, plant and equipment are open for inspection at the business entities of the group. Assets under construction were financed by funds available within the group.

1. *During the year under review assets under construction of R8m for the group and R6m for the company (2015/16: R11m for both group and company) were completed and transferred to the category, plant and machinery (2015/16: Land and buildings) for both group and company. For 2015/16, the amount mainly consists of the upgrade of buildings taking place at Denel Overberg Test Range.*

	Land and buildings	Computer equipment	Office furniture	Plant and machinery	Vehicles	Assets under construction [1]	Total
	Rm	Rm	Rm	Rm	Rm	Rm	Rm
8 PROPERTY, PLANT AND EQUIPMENT (continued)							
COMPANY							
2016/17							
Carrying value at 1 April	301	49	10	275	34	16	685
Additions	5	4	1	49	1	5	45
Depreciation for the year (refer note 3)	(25)	(17)	(2)	(49)	(10)	-	(103)
Reclassification [1]	-	-	-	6	-	(6)	-
Transfer from intangible assets (refer note 10)	-	-	-	-	-	5	5
Carrying value at 31 March	**281**	**36**	**9**	**281**	**25**	**20**	**632**
Cost	502	181	29	1 270	122	20	2 104
Accumulated depreciation and impairment	(221)	(145)	(20)	(989)	(97)	-	(1 472)
Carrying value at 31 March	**281**	**36**	**9**	**281**	**25**	**20**	**632**
2015/16							
Carrying value at 1 April	278	64	10	278	33	20	683
Additions	29	8	2	49	12	7	107
Depreciation for the year (refer note 3)	(17)	(18)	(2)	(52)	(11)	-	(100)
Reclassification [1]	11	-	-	-	-	(11)	-
Transfer to intangible assets (refer note 10)	-	(5)	-	-	-	-	(5)
Carrying value at 31 March	**301**	**49**	**10**	**275**	**34**	**16**	**685**
Cost	497	180	29	1 237	121	16	2 080
Accumulated depreciation and impairment	(196)	(131)	(19)	(962)	(87)	-	(1 395)
Carrying value at 31 March	**301**	**49**	**10**	**275**	**34**	**16**	**685**

For further detail on property, plant and equipment, refer to accounting policies, note 1.4.7.

1. *Refer footnote 1, page 144.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
9 INVESTMENT PROPERTIES				
Fair value at 1 April	680	590	671	581
Fair value adjustment (refer note 4)	48	162	48	162
Transfer from/(to) assets held for sale (refer note 18)	156	(72)	156	(72)
Disposal of investment property	(156)	-	(156)	-
Fair value at 31 March	**728**	**680**	**719**	**671**

Valuations of investment properties were carried out at year-end by registered independent external appraisers, who have appropriately recognised professional qualifications and experience in the location and nature of the property being valued. The valuation is determined on valuation techniques that utilises unobservable inputs thus falling into level 3 of the fair value hierarchy. The highest and best use of the investment properties do not differ from its current use. Changes in fair value are recognised in profit and loss.

For further detail on investment properties, refer to accounting policies, note 1.4.6.

The following table shows the valuation technique used in measuring the fair value of investment property, as well as the significant unobservable inputs used:

Valuation technique	Significant unobservable inputs	Inter-relationship between key observable inputs and fair value measurement
Discounted cash flows: The valuation model considers the present value of net cash flows to be generated from the property, taking into account expected rental growth rate, void period, occupancy rate, lease incentive costs such as rent-free period and other costs not paid by tenants. The expected net cash flows are discounted using risk-adjusted discount rates. Among other factors, the discount rate estimation considers the quality of a building and its location (prime vs. secondary), tenant credit quality and lease terms.	• Expected market rental growth (6 - 7%, weighted average 4.5%); • Void periods (average six months after the end of each lease); • Occupancy rate (90 - 95%, weighted average 93%); • Rent-free periods (six months period on new leases required); and • Risk adjusted discount rates (11.25%, weighted average 13.1%).	The estimated fair value would increase/decrease if: • Expected market rental growth were higher/lower; • The occupancy rate were higher/lower; • Rent-free periods were shorter/longer; or • The risk-adjusted discount rate were low.

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
10 INTANGIBLE ASSETS				
Development costs	103	35	72	5
At cost	217	221	183	188
Accumulated amortisation and impairment	(114)	(186)	(111)	(183)
Goodwill [1 and 2]	259	259	-	-
At cost	331	331	-	-
Accumulated impairment	(72)	(72)	-	-
Software	23	33	17	23
At cost	198	198	159	159
Accumulated amortisation and impairment	(175)	(165)	(142)	(136)
Other [3]	8	8	8	8
At cost	34	34	8	8
Accumulated amortisation and impairment	(26)	(26)	-	-
Fair value at 31 March	393	335	97	36

1. *On 29 April 2015, Denel acquired 100% of the issued ordinary shares of Land Systems South Africa (Pty) Ltd, an unlisted company, which provides protected vehicle solutions. Denel has acquired the company to broaden its landward capability for a new product range. The acquisition was for a purchase consideration of R828m on the understanding that Denel would partner with the company on relevant opportunities and thereby maximise synergies. The goodwill of R242m comprises the value of the expected synergies arising from the acquisition. Since acquisition the name was changed to Denel Vehicle Systems (Pty) Ltd. Intangible assets under business acquired total R21m, consisting of software (R13m) and goodwill on business combination (R8m, after impairment of R2m). Refer note 34.*
2. *On 11 May 2012, Denel acquired 51% of the issued ordinary shares of LMT Holdings (Pty) Ltd, an unlisted company, who's core business is in the provision of protected vehicle solutions. LMT Holdings (Pty) Ltd have three subsidiaries i.e. LMT Products (Pty) Ltd, LMT Engineering (Pty) Ltd and LMT Properties (Pty) Ltd. The company has acquired LMT Holdings (Pty) Ltd to broaden its landward capability for a new product range. The acquisition was for a purchase consideration of R100 on the understanding that Denel would partner with the company on relevant opportunities and thereby maximise synergies. The goodwill of R9m (2015/16: R9m) comprises the value of the expected synergies arising from the acquisition. Since acquisition the name was changed to LMT Holdings SOC Ltd (RF). Refer note 34.*
3. *Intellectual property related to the development and industrialisation of the 20 X 42mm Neopup Personal Area Weapon.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
10 INTANGIBLE ASSETS (continued)				
RECONCILIATION				
Development costs				
Carrying value at 1 April	35	164	5	158
Capitalised during the year	1	5	-	6
Fair value at first consolidation	-	29	-	-
Impairment for the year (refer note 3) [1]	72	(163)	72	(159)
Transfer to property, plant and equipment (refer note 8)	(5)	-	(5)	-
Carrying value at 31 March	103	35	72	5
Goodwill				
Carrying value at 1 April	259	9	-	-
Acquisition external	-	242	-	-
Business acquired	-	8	-	-
Carrying value at 31 March	259	259	-	-
Software				
Carrying value at 1 April	33	26	23	26
Amortisation for the year (refer note 3)	(11)	(16)	(7)	(12)
Business acquired	-	13	-	-
Capitalised during the year	1	5	1	4
Transfer from property, plant and equipment (refer note 8)	-	5	-	5
Carrying value at 31 March	23	33	17	23
Other				
Carrying value at 1 April	8	8	8	8
Capitalised during the year	-	-	-	-
Carrying value at 31 March	8	8	8	8
Total carrying value at 31 March	393	335	97	36

1. *The Seeker 400 is a multi-mission multi-role ISR System, developed by Denel with its own funds over a seven year period. The total development cost (R159m) was impaired in 2015/16 due to lack of evidence for the recoverability of the asset. The UAVS business entity forms part of Denel Dynamics, an entity within the Denel group. Management reassessed the recoverable amount based on the following:*

   - *Additional interest received from external parties on the Seeker 400 capability.*
   - *Secondly, on the basis of an increase order pipeline according to the marketing efforts; and*
   - *Strengthened market penetration for the product through possible joint efforts with partners.*

   The recoverable amount is its value in use and a discount rate of 9.47% was used in the recalculation. The impairment reversal amount for the 2016/17 financial year is R72m (2015/16: Rnil) and included under Other operating expenses in the profit and loss account. The recoverable amount is R228m (2015/16: Rnil).

	COMPANY	
	2016/17	2015/16
	Rm	Rm
11 INVESTMENTS IN SUBSIDIARIES		
Unlisted shares	2 541	2 541
Net loans (refer note 30.4) [1]	145	191
Amounts due by subsidiaries	601	386
Amounts due to subsidiaries	(456)	(195)
Gross investments	2 686	2 732
Accumulated impairment	(1 391)	(1 391)
Carrying value at 31 March	**1 295**	**1 341**
The accumulated impairment loss on investments in subsidiaries is as follows:		
Unlisted shares	1 055	1 055
Balance at 1 April	1 055	1 055
Impairment for the year	-	-
Loans	336	336
Balance at 1 April	336	336
Impairment for the year	-	-
	1 391	1 391

BAE Land Systems South Africa (Pty) Ltd was acquired on 29 April 2015, subsequent name change to Denel Vehicle Systems (Pty) Ltd.

Denel Asia LLC was established in Hong Kong on 29 January 2016. No transactions took place during the 2016/17 or 2015/16 financial year in this entity.

100% of the shares held in Denel Vehicle Systems (Pty) Ltd have been pledged as security in relation to the loan received from Nedbank (refer note 21.2).

A detailed breakdown of the investments in subsidiaries is contained in note 34.

1. *Net loans, are in actual fact financial instruments that are managed by the group's treasury function. The A&R committee of the board oversees the group's treasury operations and has an established policy for the management of credit risk arising from treasury activities. (Refer note 30.1). The amount comprises:*

   - *Cash managed by the group's treasury function.*
   - *Cash comprises cash on hand and demand deposits.*
   - *Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.*
   - *Cash equivalents that are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes.*
   - *Bank borrowings are generally considered to be financing activities. However, in some countries, bank overdrafts which are repayable on demand form an integral part of an entity's cash management. In these circumstances, bank overdrafts are included as a component of cash and cash equivalents. A characteristic of such banking arrangements is that the bank balance often fluctuates from being positive to overdrawn.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

12 INVESTMENTS IN ASSOCIATED COMPANIES

12.1 ESTABLISHMENT OF ASSOCIATED COMPANIES

As part of the turn-around strategy that was agreed with government, Denel embarked on a process to sought partners to share technology, development cost and funding, access to markets and assist in management. During this process a number of equity partners were identified which would have synergy with specific business entities within Denel. Denel negotiated equity partnership agreements which led to the formation of new companies.

A company is an "associated company" for the group, if Denel has significant influence and which is neither a subsidiary nor a joint venture. Significant influence is their power to participate in the financial and operating policy decisions of the company, but not control or joint control over those policies. Control is the power to govern the financial and operating policies of a company in order to obtain benefits from its activities. Although Denel has significant influence over it's associated companies, it has no control or joint control over its associated companies w.r.t. their financial and operating policy decisions.

Rheinmetall Denel Munition (Pty) Ltd was established on 1 September 2008 when the Denel entities comprising of Somchem (Somerset West and Wellington sites), Swartklip, Boksburg and Naschem became part of the Rheinmetall defence group. The company became known as Rheinmetall Denel Munition with Rheinmetall Waffe Munition GmbH being the 51% majority shareholder, while Denel holds 49% of the shares. In considering control, Denel took into account the following factors:

» Rheinmetall Waffe Munition GmbH holds 51% of the shares in Rheinmetall Denel Munition (Pty) Ltd,and has the right in terms of the shareholders' agreement to appoint three of the five board members;
» Rheinmetall Waffe Munition GmbH manage the day to day activities of the company in terms of the shareholders' agreement; and
» Rheinmetall Waffe Munition GmbH has the right to appoint the CEO and CFO of their choice of the company in terms of the shareholders' agreement.

These matters were initially considered by management in 2008 when the company was established. At that time and subsequently Rheinmetall Denel Munition (Pty) Ltd has been accounted for using the equity method. On adoption of *IFRS 10, Consolidated financial statements*, these same factors enabled management to conclude, without making any significant judgements, that Denel does not have power over Rheinmetall Denel Munition (Pty) Ltd but can exercise significant influence.

The golden share held by Denel is done so on behalf of the SA government who may intervene to veto or change certain strategic decisions such as the closure or relocation of the factory to a foreign country. The Golden Share agreement clearly states that this golden share shall not afford the SA government any right to participate in any profits and in the management of the business. These rights do not confer any decision making rights, but merely the right to veto a disposition of the assets or business of Rheinmetall Denel Munition (Pty) Ltd (IFRS 10.14).

The following facts are significant to the partnerships' agreements for all associated companies:

» Denel has only one equity partner for each of the associated companies and the equity partner holds the majority of the shareholding;
» Denel and the equity partner will fund the company or guarantee funding, if additional funding is needed, in the same ratio as their shareholding;
» The equity partner has the right to appoint the majority of the board members;
» The equity partner has the right to appoint the CEO and CFO with the exception in the case of Turbomeca Africa (Pty) Ltd where Denel appoints the CFO; and
» The equity partners are responsible for the day to day running and performance of the companies.

12 INVESTMENTS IN ASSOCIATED COMPANIES (continued)

12.1 ESTABLISHMENT OF ASSOCIATED COMPANIES (continued)

Airbus DS Optronics (Pty) Ltd [1] is a global supplier in the development and production of optronics, optical and precision-engineered products for military and security applications.

Rheinmetall Denel Munition (Pty) Ltd specialises in the design, development and manufacture of large and medium-calibre ammunition, and is a world leader in the field of artillery, mortar and infantry systems and plant engineering.

Pioneer Land Systems LLC will market, sell and manufacture landward vehicles and weapon systems and supply ancillary services in support of such products.

Tawazun Dynamics LLC is a UAE based global supplier of precision guided munitions.

Turbomeca Africa (Pty) Ltd is a world leader in design, manufacturing and sale of gas turbines for small- and medium-powered helicopters.

		Denel SOC Ltd		Equity partner	
Associated company	Equity partner	Shareholding %	Number of board members	Shareholding %	Number of board members
Airbus DS Optronics (Pty) Ltd [1]	Hensoldt Sensors GmbH [2]	30	1	70	5
Rheinmetall Denel Munition (Pty) Ltd	Rheinmetall Waffe Munition GmbH [1]	49	2	51	3
Pioneer Land Systems LLC	International Golden Group PJSC [3]	49	2	51	3
Tawazun Dynamics LLC	Tawazun Holding [3]	49	2	51	3
Turbomeca Africa (Pty) Ltd	Turbomeca SAS [4] and Safran SA [4]	49	3	51	5

The above mentioned information was used in management's judgement that Denel did not exercise control over these companies and therefor, will disclosed these companies as associate companies.

The financial year-end of all Denel's associated companies is 31 December.

1. *Refer footnote 2, page 201.*
2. *Company is incorporated in Germany.*
3. *Company is incorporated in the UAE.*
4. *Both companies are incorporated in France.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
12 INVESTMENTS IN ASSOCIATED COMPANIES (continued)				
12.2 NET INVESTMENT IN ASSOCIATED COMPANIES				
Cost of investments in associated companies:				
Unlisted shares	500	500	500	500
Net share of results in associated companies	495	340		
Share of current year profit before tax	202	161		
Share of current year tax	(48)	(29)		
Share of current year profit after tax (refer note 26.1) [1]	154	132		
Dividends paid	-	(25)		
Accumulated profit at 1 April	340	233		
Net investments in associated companies	995	840	500	500
The net investments in associated companies are made up as follows:				
Airbus DS Optronics (Pty) Ltd	128	103	56	56
Rheinmetall Denel Munition (Pty) Ltd	735	608	372	372
Pioneer Land Systems LLC	-	-		
Tawazun Dynamics LLC	45	-	23	23
Turbomeca Africa (Pty) Ltd	87	129	49	49
Net investments in associated companies	995	840	500	500

The total comprehensive loss attributable to one of the associated companies for the year-end 31 December 2015 was R100m. As per the company's accounting policy and in accordance with *IAS 28, Investments in associates and joint ventures*, paragraph 38, the associates share of losses is only recognised up to the value of the investment in the associated company which was R23m for 2015/16. The remaining attributable comprehensive loss of R77m for 2015/16 has been offsetted against 2016/17's generated profits of the associate company before the investment was recognised in the group's accounting records. The associated company made a profit in 2016/17.

1. *Refer to the consolidated income statements and statements of comprehensive income, page 121.*

	2016/17 Rm	2015/16 Rm

12 INVESTMENTS IN ASSOCIATED COMPANIES (continued)

12.3 EXTRACTS FROM AUDITED ANNUAL FINANCIAL STATEMENTS

Rheinmetall Denel Munition (Pty) Ltd has elected to designate hedges as cash flow hedges for hedge accounting purposes whereas Denel's accounting policy is to designate hedges as fair value hedges. For disclosure purposes, Rheinmetall Denel Munition (Pty) Ltd's annual financial statements were restated to reflect Denel's accounting policy in this regard.

Rheinmetall Denel Munition (Pty) Ltd is considered to be a material associated company as a result of the quantitative nature of its results and is disclosed separately.

The following amounts represents the summarised restated financial information of Rheinmetall Denel Munition (Pty) Ltd:

	2016/17 Rm	2015/16 Rm
Total assets	2 466	2 563
Non-current assets	637	314
Current assets	1 829	2 249
Total liabilities	1 214	1 946
Non-current liabilities	169	313
Current liabilities	1 045	1 633
Net assets	1 252	617
Group's share of associated company's net assets	613	302
Revenue	2 376	2 136
Group's share of revenue	1 164	1 047
Profit before tax	344	206
Group's share of profit before tax	169	101
Profit after tax	260	156
Group's share of profit after tax	127	76

The other associated companies' figures are not material, thus for disclosure purposes, figures are aggregated. The following represents the summarised financial information of the associated companies other than Rheinmetall Denel Munition (Pty) Ltd:

	2016/17 Rm	2015/16 Rm
Total assets	3 389	3 298
Non-current assets	339	533
Current assets	3 050	2 765
Total liabilities	2 728	2 887
Non-current liabilities	812	1 474
Current liabilities	1 916	1 413
Net assets	661	411
Group's share of associated companies' net assets	245	138
Revenue	3 355	1 185
Group's share of revenue	1 510	473
Profit before tax	110	158
Group's share of profit before tax	34	60
Profit after tax	43	147
Group's share of profit after tax	27	56

A detailed breakdown of the investments in associated companies is contained in note 34.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
13 DEFERRED TAX				
Deferred tax assets	36	48	-	-
Deferred tax liabilities	(1)	(1)	-	-
	35	**47**	**-**	**-**
Movement of deferred tax assets and liabilities:				
Balance at 1 April	47	12	-	-
Business acquired	-	13	-	-
Income statement (refer note 7)	(12)	22	-	-
	35	**47**	**-**	**-**
Net deferred tax asset comprises:				
Advance payments received	1 036	1 014	937	885
Amounts due to customers for work invoiced, not yet performed	92	115	92	115
Capital allowances	35	52	27	49
Limit deferred tax asset to liability	(946)	(950)	(913)	(933)
Provisions	274	313	208	249
Other tax deductible differences	213	270	213	259
	704	**814**	**564**	**624**
Net deferred tax liability comprises:				
Amount due from customers for contract work	(469)	(449)	(413)	(448)
Capital allowances	(171)	(218)	(136)	(163)
Doubtful debt allowance	-	(4)	-	(4)
Pre-payments made	(10)	(3)	(9)	(3)
Section 24 allowance on pre-payments received	(13)	(2)	-	-
Other taxable differences	(6)	(91)	(6)	(6)
	(669)	**(767)**	**(564)**	**(624)**

For certain companies in the group, the deferred tax asset on the calculated tax loss is limited to the amount of the deferred tax liability. For the other companies, depending on future taxable profits, the entire deferred tax asset is recognised. Had a full deferred tax asset been recognised on the calculated tax loss, the value of the deferred tax asset at year-end would have been R1 650m (2015/16: R1 647m) for the group and R1 477m (2015/16: R1 557m) for the company.

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
14 INVENTORIES				
Inventories are valued at the lower of cost or net realisable value and is categorised as follows:				
Consumable inventory	143	128	142	127
Finished products	601	498	571	485
Raw materials and bought-out components	422	498	196	351
Work-in-progress	1 457	1 217	864	722
	2 623	2 341	1 773	1 685
Impairment account reconciliation				
Balance at 1 April	253	141	133	131
Business acquired	-	180	-	-
Impairment for the year (refer note 3)	52	43	6	21
Impairment reversal for the year (refer note 3)	(14)	(100)	(14)	(19)
Realised	(19)	(11)	(4)	-
	272	253	121	133
Amount relating to inventories which was recognised as an expense during the year (refer note 3)	4 032	3 025	3 097	1 868
Inventory purchased during the financial year	4 314	3 855	3 185	3 150
Denel reviewed inventory items that were previously treated as slow moving and identified items that will be used in future projects. This resulted in a reversal of the provision for slow moving inventory.	14	19	14	19

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
15 TRADE AND OTHER RECEIVABLES				
Financial assets (refer note 30.4)	2 325	2 704	1 921	2 258
Trade receivables (refer note 30.1)	2 221	2 647	1 829	2 195
Inter-group trade receivables			49	25
Interest receivables (refer note 30.1)	3	3	1	1
Sundry receivables (refer note 30.1)	101	54	42	37
Non-financial assets	1 993	2 324	1 973	2 284
Work performed not yet invoiced	1 475	1 599	1 475	1 599
Pre-payments and advances made	455	557	451	528
Straight line receivables	21	21	21	21
Sundry receivables	42	147	26	136
	4 318	5 028	3 894	4 542
Accumulated impairment				
Financial assets	44	57	42	57
Impairment account reconciliation				
Balance at 1 April	57	41	57	41
Business acquired	-	3	-	-
Impairment for the year (refer note 3)	2	17	3	16
Impairment reversal for the year (refer note 3)	(4)	(4)	-	(1)
Recovered during the year	-	-	(9)	-
Written off as non-collectible	(11)	-	(9)	1
	44	57	42	57

Trade receivables are non-interest bearing and are generally on 30 to 90 day terms. Specific impairments are made for identified doubtful debts.

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
16 OTHER FINANCIAL ASSETS AND LIABILITIES				
16.1 OTHER FINANCIAL ASSETS				
Derivatives	102	73	34	73
Foreign exchange contracts	102	73	34	73
Firm commitments	107	288	107	288
Foreign exchange contracts designate as fair value hedges	107	138	107	138
Foreign exchange options designate as fair value hedges	-	150	-	150
Refer note 30.4	209	361	141	361
16.2 OTHER FINANCIAL LIABILITIES				
Derivatives	102	272	25	218
Foreign exchange contracts	78	122	25	68
Foreign exchange options	24	150	-	150
Firm commitments	68	59	68	59
Foreign exchange contracts designate as fair value hedges	68	59	68	59
Refer note 30.4	170	331	93	277
17 CASH AND CASH EQUIVALENTS				
17.1 CASH AND CASH EQUIVALENTS COMPRISES				
Cash and short-term deposits (refer note 17.2) [1]	2 021	2 003	1 556	1 788
17.2 CASH AND SHORT-TERM DEPOSITS				
Cash in bank	397	651	252	615
Local banks	65	274	22	249
Local banks (foreign currency)	332	377	230	366
Deposits	797	213	477	34
Local call deposits	797	213	477	34
Cash restricted for use [2]	827	1 139	827	1 139
Local banks	827	1 139	827	1 139
Refer note 17.1, 30.1, 30.3 and 30.4	2 021	2 003	1 556	1 788
18 NON-CURRENT ASSETS HELD FOR SALE				
Balance at 1 April	156	84	156	84
Transfer (from)/to investment properties (refer note 9)	(156)	72	(156)	72
Refer note 30.4	-	156	-	156

The asset held for sale in respect of investment properties as at 31 March 2016 relates to the Philippi facility. The negotiations relating to the selling of the property as at 31 March 2016, were at an advanced stage with a 10% deposit received early 2016/17. The asset held for sale in 2015/16 was subsequently sold for R156m. Final payment was received from the buyer on the 14th October 2016.

1. *Cash and cash equivalents are as per the consolidated statements of cash flows, page 123. The weighted average effective interest rate on call deposits is 6.539% (2015/16: 5.5%). Interest on cash in bank is earned at market rates.*
2. *The funds included in cash and short-term deposits are available on demand, except for the amount relating to the Hoefyster project which is ringfenced, R827m (2015/16: R1 139m).*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
19 SHARE CAPITAL AND SHARE PREMIUM				
19.1 AUTHORISED CAPITAL				
1 000 000 000 Class A ordinary shares of R1 each	1 000	1 000	1 000	1 000
232 455 747 Class B ordinary shares of R1 each	232	232	232	232
	1 232	1 232	1 232	1 232
19.2 ISSUED CAPITAL				
Shares at par value				
Class A ordinary shares	1 000	1 000	1 000	1 000
Class B ordinary shares	225	225	225	225
	1 225	1 225	1 225	1 225
19.3 SHARE PREMIUM				
Balance at 1 April	4 951	4 951	4 951	4 951
Premium on shares issued during the year	-	-	-	-
	4 951	4 951	4 951	4 951

At year-end, the number of issued Class A ordinary shares were 1 000 000 000 (2015/16: 1 000 000 000) and the number of issued Class B ordinary shares were 225 056 663 (2015/16: 225 056 663).

The unissued shares are under the control of the SA government, which is the sole shareholder. The Class B ordinary shares are limited in that any reduction of share capital must first be written off against the Class B ordinary share plus any premium thereon, before any reduction of Class A ordinary shares may occur.

	GROUP 2016/17 Rm	GROUP 2015/16 Rm
20 NON-CONTROLLING INTEREST		
Balance at 1 April	19	3
Share of net (loss)/profit in subsidiary	(12)	17
Preference dividends payable	(3)	(1)
	4	19

For the Denel group, the non-controlling interest in LMT Holdings SOC Ltd (RF) is both quantitatively and qualitatively immaterial.

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
21 LOANS AND BORROWINGS				
Interest bearing loans and borrowings				
Finance lease (refer note 21.1)	8	14	-	-
Secured loan (refer note 21.2)	148	-	-	-
Secured loan (refer note 21.3)	-	400	-	400
Secured mortgage (refer note 21.4)	1	2	-	-
Unsecured bonds (refer note 21.5)	689	1 573	689	1 573
Other	7	6	1	-
Non-current portion of interest bearing loans and borrowings	853	1 995	690	1 973
Current portion of interest bearing loans and borrowings	2 412	1 722	2 315	1 917
Finance lease (refer note 21.1)	3	4	-	-
Secured loan (refer note 21.2)	94	-	-	-
Secured loan (refer note 21.3)	400	455	400	455
Secured mortgage (refer note 21.4)	1	1	1	1
Unsecured bonds (refer note 21.5)	685	315	685	315
Commercial paper (refer note 21.6 and 30.3)	200	200	200	200
Current portion of interest bearing loans and borrowings included under current liabilities	1 029	747	1 029	946
Total interest bearing loans and borrowings	3 265	3 717	3 005	3 890

	GROUP					
	2016/17			2015/16		
	Within one year	One to five years	Total	Within one year	One to five years	Total
21.1 FINANCE LEASE						
Finance lease liabilities are payable as follows:						
Future minimum lease payments	4	10	14	5	16	21
Interest	(1)	(2)	(3)	(1)	(2)	(3)
Present value of minimum lease payments	3	8	11	4	14	18

During the 2015/16 finanical year a decision was made to finance a high-speed five axis milling machine, called "Zimmerman". The total capital amount was €1.3m (R23m). Interest is charged at a fixed rate of 5.75% p.a. (2015/16: 5.75%), with capital payable half yearly and interest quarterly. The lease agreement determined ten capital instalments of €114 750 of which the final capital instalment will be on 4 October 2020, with the final interest payment on 10 December 2020. The total capital amount outstanding as at 31 March 2017 is €0.803m (R11.6m) (2015/16: €1.03m (R17.4m)). The carrying amount of the asset as at 31 March 2017 was R21m. No finance loan existed for the year under review for the company, Denel SOC Ltd.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

21 LOANS AND BORROWINGS (continued)

21.2 SECURED LOAN

Secured loan from Nedbank to Denel Vehicle Systems (Pty) Ltd to the amount of R250m for a four year priod expiring 23 November 2020. Interest is payable every quarter. The interest is linked to JIBAR + 4.35%. The loan is secured against the 100% shareholding of Denel SOC Ltd in Denel Vehicle Systems (Pty) Ltd. Refer note 11.

21.3 SECURED LOAN

Secured loan from ABSA by Denel SOC Ltd for a period of two years to the amount of R400m. Interest is payable quarterly at a JIBAR linked interest rate with a credit spread of 150 basis points. Repayment of loan on 24 June 2017. The interest is linked to JIBAR + 1.5%.

21.4 SECURED MORTGAGE

The secured mortgage relates to a mortgage bond by LMT Holdings SOC Ltd (RF). The carrying value of the asset is R9.5m (2015/16: R9.5m). The bond is repayable in monthly instalments with an interest rate of 9.5% (2015/16: 9.25%) p.a. is directly link to the prime interest rate. The final instalment will be in July 2018.

21.5 UNSECURED BONDS

Denel registered a R3bn (2015/16: R3bn) Domestic Medium Term Note (DMTN) programme with the Johannesburg Stock Exchange (JSE). Under the programme Denel could raise senior and/or subordinated notes up to the facility limit of R2.539bn (2015/16: R3bn). The programme contains cross-default (indebtedness of outstanding amount equals or exceeds 1% (2015/16: 1%) of total asset of issuer) and negative pledge clause (which precludes the company from encumbering any assets or revenue of the company or any subsidiary in favour of any borrowing, without making effective provision whereby all notes shall be directly secured equally and rateable with such relevant borrowings).

The government guarantee, guarantees irrevocably and unconditionally the punctual performance by the issuer of payment of principal and/or interest. In terms of the guarantee, the guarantor waives all rights of subrogation indemnity and subordinates any claims which it may have in favour of the note holders. Therefore, in the event that the issuer cannot honour payment the guarantor will repay the debt. The guarantee expires on 30 September 2017.

The borrowings have been raised through the issuance of one- and eighteen-month bonds totalling R1.6bn (2015/16: R1.4bn). The three-year bond was re-financed on 28 January 2016. Two five-year bonds were issued on 28 January 2013 and 10 June 2013 at interest rates of 6.86% and 7.92% and matures on 29 September 2017 and 10 June 2018 respectively. Of the total borrowings, R1.85bn (2015/16: R1.85bn) are backed by a five-year government guarantee. The interest rate is linked to JIBAR.

21 LOANS AND BORROWINGS (continued)

21.6 COMMERCIAL PAPER

During 2016/17 notes to the value of R964m (2015/16: R650m) were issued as follows:

Rate	Issue date	Maturity date	Rm
2016/17			
3-month JIBAR + 1.20%	27 January 2017	29 August 2017	400
3-month JIBAR + 1.20%	6 February 2017	22 September 2017	262
Fixed rate 8.35%	6 February 2017	5 May 2017	52
3-month JIBAR + 1.20%	27 February 2017	29 August 2017	150
3-month JIBAR + 1.20%	3 March 2017	29 August 2017	100
			964
2015/16			
3-month JIBAR + 0.95%	20 November 2015	19 November 2016	200
Fixed rate 8.75%	28 January 2016	17 January 2017	200
3-month JIBAR + 1.05%	25 February 2016	27 February 2017	150
3-month JIBAR + 1.05%	3 March 2016	3 March 2017	100
			650

The commercial paper programme is a five-year debt instrument issued as part of the DMTN programme. The DMTN is registered for R2.2bn (2015/16: R2.2bn). R1.85bn (2015/16: R1.85bn) of the notes are secured by a government guarantee.

The undrawn borrowing facilities available for future operating activities amount to R134m (2015/16: R275m) and US$50m (2015/16: US$50m). Refer note 30.4 for fair value.

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	%	%	%	%
21.7 WEIGHTED AVERAGE EFFECTIVE INTEREST RATES				
Finance lease (fixed rate, refer note 21.1)	5.8	3.2	-	-
Local secured loans (floating rate, refer note 21.2)	JIBAR + 4.35%	8.5	JIBAR + 4.35%	8.5
Local secured loans (floating rate, refer note 21.3)	JIBAR + 1.2%	-	JIBAR + 1.2%	-
Secured mortgage (floating rate, refer note 21.4)	9.5	9.25	-	-
Local unsecured loans (fixed rate)	8.5	7.6	8.5	7.6
Current bank borrowings (floating rate)	9.2	8.4	9.2	8.4

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP 2016/17 Rm	GROUP 2015/16 Rm	COMPANY 2016/17 Rm	COMPANY 2015/16 Rm
21 LOANS AND BORROWINGS (continued)				
21.8 SUMMARY OF MATURITY OF BORROWINGS				
Maturing:				
Within three months	495	752	477	947
Between three and twelve months	1 917	970	1 838	970
Between one and two years	1	1 976	-	1 955
Between two and three years	699	2	690	1
Between three and five years	153	10	-	10
After five years	-	7	-	7
	3 265	3 717	3 005	3 890
22 ADVANCE PAYMENTS RECEIVED				
Non-current advance payments received	2 060	2 100	2 060	1 937
Current advance payments received	1 562	1 431	1 246	1 224
Total advance payments received	3 622	3 531	3 306	3 161
The carrying amount of the advance payment is expected to be settled as follows:				
Between three and twelve months	132	228	132	228
Less than one year	1 430	1 203	1 114	996
Between one and two years	722	552	722	552
Between two and three years	522	336	522	336
Between three and five years	468	277	468	277
More than five years	348	935	348	772
Refer note 25.1	3 622	3 531	3 306	3 161

Since 2012/13 the group entered into large long-term contracts on which advance payments were received.

These advance payments will be settled over a period of up to 11 years (2015/16: 12 years) and therefore the portion of the liability that will be settled more than twelve months after the reporting period is classified as non-current.

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
23 PROVISIONS				
23.1 NON-CURRENT PROVISIONS				
Contract risks and onerous contracts	1	3	-	-
Product warranty and recall	118	113	95	102
Site restoration	212	207	212	207
Counter trade	54	50	-	-
	385	373	307	309
23.2 CURRENT PROVISIONS				
Contract risks and onerous contracts	56	21	46	11
Performance guarantees (refer note 25.1) [1]	30	55	30	55
Product warranty and recall	143	144	82	91
Site restoration [1]	7	7	7	7
Counter trade	30	71	20	62
Insurance provision [1]	11	9	-	-
Other [1]	144	253	102	186
	421	560	287	412
Total provisions	806	933	594	721

Denel Land Systems was contracted for the excavation and transportation of heavy oil contaminated soil to land fill for an amount of US$7.5m. Since the inception of the project, there has been significant hurdles experienced which included but not limited to the following:

» Securing of visa's for Denel employees deployed to the project;
» Limited access to the areas;
» Weather conditions;
» Project scope creep;
» Statement of work discrepancies; and
» Change in the scope of the geophysics company.

All these hurdles experienced has led to over expenditures on the project. An additional US$3.5m was added to the contract by the client, however this was not sufficient to cover the over expenditure on the contract, thus making this contract onerous.

1. Non-current povision for 2016/17: Rnil (2015/16: Rnil).

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	Contract risks and onerous contracts	Performance guarantees	Product warranty and recall	Site restoration	Counter-trade	Insurance	Other	Total
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
23 PROVISIONS (continued)								
23.3 RECONCILIATION								
GROUP								
2016/17								
Balance at 1 April	24	55	257	214	121	9	253	933
Charged to the income statement	38	-	89	-	-	2	140	269
Realised	(5)	(25)	(51)	(14)	(37)	-	(208)	(340)
Unused amounts reversed	-	-	(38)	-	-	-	(41)	(79)
Unwinding of discount on provisions (refer note 6)	-	-	4	19	-	-	-	23
	57	30	261	219	84	11	144	806
2015/16								
Balance at 1 April	25	44	109	216	49	7	198	648
Business acquired	-	-	69	-	42	-	-	111
Charged to the income statement	22	11	117	-	31	2	251	434
Realised	(24)	-	(29)	-	-	-	(193)	(246)
Unused amounts reversed	(1)	-	(10)	(18)	(1)	-	(3)	(33)
Unwinding of discount on provisions (refer note 6)	2	-	1	16	-	-	-	19
	24	55	257	214	121	9	253	933
COMPANY								
2016/17								
Balance at 1 April	11	55	193	214	62	-	186	721
Charged to the income statement	38	-	57	-	8	-	97	200
Realised	(3)	(25)	(41)	(14)	-	-	(159)	(242)
Unused amounts reversed	-	-	(36)	-	(50)	-	(22)	(108)
Unwinding of discount on provisions (refer note 6)	-	-	4	19	-	-	-	23
	46	30	177	219	20	-	102	594
2015/16								
Balance at 1 April	25	44	100	216	49	-	173	607
Charged to the income statement	9	-	110	-	14	-	190	323
Realised	(24)	11	(13)	-	-	-	(177)	(203)
Unused amounts reversed	(1)	-	(5)	(18)	(1)	-	-	(25)
Unwinding of discount on provisions (refer note 6)	2	-	1	16	-	-	-	19
	11	55	193	214	62	-	186	721

23 PROVISIONS (continued)

Contract risks and onerous contracts

The provision for onerous contracts comprises expected losses on contracts where the expected benefits to be derived from a contract are lower than the unavoidable costs of meeting the obligation. The provision for contract risk comprises potential risks on contracts that are in progress, based on the technical and financial risk profile of each contract.

Performance guarantees

Performance guarantees are issued by the group for contracts that are in progress. These performance guarantees are carried as contingent liabilities and are raised as provisions when the group has a present legal or constructive obligation to settle them.

Product warranty and recall

The provision for product warranty comprises legal and constructive obligations of the group in respect of products delivered that are still under warranty. The provision for product recall comprises the estimated cost that the group will incur in the event of a specific product recall.

Provisions relating to insurance contracts

The provision is in respect of claims that have been incurred but not reported to the insurance subsidiary.

Countertrade

The group has entered into several export sales contracts that give rise to certain countertrade obligations. The obligations vary and are calculated as a percentage of the export sales contract value. A provision for countertrade is raised once the group has a present legal or constructive obligation to settle them.

Site restoration provision

The provision is for estimated costs for decontamination and site restoration. A provision for site restoration is recognised when the obligation arises as a result of the group's activities.

Other provisions

Other provisions comprise the following:

Retrenchment costs
As a result of the restructuring of a particular contract, certain employees have been identified for retrenchment and will be awarded retrenchment packages. The retrenchment provision has been calculated based on the remuneration and the number of years of service of the affected persons, as well as specific terms negotiated with individuals or their labour representatives. The carrying amount included in other provisions is R4m (2015/16: R7m) for both group and company.

Variable remuneration
Provision is made for all employees based on achieving certain performance targets. The amounts provided are based on an agreed percentage of employees' remuneration. The carrying amount included in other provisions is R140m (2015/16: R201m) for the group and R97m (2015/16: R144m) for the company.

Legal costs and disputes
The provision relates to legal costs for disputes, labour issues and damages resulting from alleged non-performances in which the group or entities within the group are involved, also refer to provisions for performance guarantees which relates to legal action. The carrying amount included in other provisions is Rnil (2015/16: Rnil) for both group and company.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
24 TRADE AND OTHER PAYABLES				
Financial liabilities (refer note 30.2 and 30.4)	1 637	1 741	1 292	1 417
Trade payables	1 118	1 277	775	1 032
Inter-group trade payables			87	29
Interest accrued	35	46	35	46
Other accruals	484	418	395	310
Non-financial liabilities	329	413	328	412
Amounts due to customers for work invoiced not yet performed	328	412	328	412
Other non-financial liabilities	1	1	-	-
	1 966	2 154	1 620	1 829

Trade payables are non-interest bearing and are normally settled between 30 and 90 days. Other payables are also non-interest bearing, and are settled as they fall due in accordance with respective agreements. Interest payable is settled in accordance with terms.

25 CONTINGENT LIABILITIES

25.1 GUARANTEES

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
The following guarantees were issued by the group:				
Advance payment guarantees	5 781	5 440	5 460	5 440
Guarantees to banks for credit facilities of subsidiaries	259	629	59	629
Guarantees to local authorities	28	13	15	13
Participating guarantees	4	12	4	12
Performance guarantees	1 268	1 261	1 047	1 261
Other guarantees	145	223	145	223
Total of guarantees issued	7 485	7 578	6 730	7 578
Guarantees issued on behalf of associated companies	(317)	(200)	(117)	(200)
Advance payment guarantees	(13)	-	(13)	-
Guarantees to banks for credit facilities of subsidiaries	(259)	(200)	(59)	(200)
Performance guarantees	(34)	-	(34)	-
Other guarantees	(11)	-	(11)	-
Refer note 30.2	7 168	7 378	6 613	7 378
Recognised in the consolidated annual financial statements	(3 969)	(3 594)	(3 560)	(3 224)
Advance payments received (refer note 22)	(3 621)	(3 531)	(3 307)	(3 161)
Provision for performance guarantees (refer note 23.2)	(30)	(55)	(30)	(55)
Other provisions	(318)	(8)	(223)	(8)
	3 199	3 784	3 053	4 154

25 CONTINGENT LIABILITIES (continued)

25.2 LITIGATION

Litigation comprises legal claims lodged and claims that may be lodged against the group. Owing to the sensitivity of the claims and the measures that will be taken to limit the liabilities, specific disclosure of items may negatively influence the outcome and the group's actions.

The aggregate amount of significant claims lodged against the company not specifically provided for is Rnil (2015/16: Rnil). The directors are of the view that the success of most of the claims against the company is remote and no material losses are expected to materialise from these claims other than that which have already been provided. Details of some of the key issues are provided below:

The group is in dispute with one of its key customers over contractually related matters. This has led to the cancellation of contracts that were in progress and the loss of potential contracts, as well as the call up of related performance guarantees. There are ongoing arbitrations between the parties and indications are that the matters will be resolved. It is not possible at this stage to estimate the potential damages and legal costs involved as the matters are sub judice.

25.3 CONTRACT LOSSES

One of the group's subsidiaries is a programme partner in a design, manufacturing and supply contract for certain aircraft components. The contract has a value of approximately R2.5bn (2015/16: R2.5bn) and an estimated contract loss of approximately R1.4bn (2015/16: R1.4bn). This loss has not been raised as a provision following a written commitments received from the shareholder stating its support including financial for the continuation of the contract despite it being loss making, as it has certain strategic advantages to the country. During 2012 various onerous terms and conditions to the contract was renegotiated to mitigate risk to the company and shareholder.

25.4 SITE RESTORATION

Provision for site restoration has been calculated and raised, based on certain key assumptions, refer to note 1.3. A contingency of 15% (2015/16: 15%) of the estimated cost as recommended by the consultants was not included in determining the site restoration provision. The contingency would have been to cover risks arising from the unknown depth of contamination and the volume of the material to be cleaned up. After an initial clean up, the site will be tested for explosive ordinates to assess whether there should be any further clean up, which may impact the provision. Had the contingency been included, the provision would have been increased by R31.6m (2015/16: R31m) for both, group and company.

25.5 COUNTERTRADE

The group has entered into several export sales contracts that give rise to certain countertrade obligations. The obligations vary between 60% and 100% of the export sales contract value.

These countertrade obligations can be fulfilled in one or a combination of the following ways:

- Production work share and technology transfer.
- Procurement of products and services from suppliers in the buyers' country.
- Participation in a business venture in the buyers' country.

The group is constantly in negotiations to find the best mechanisms to fulfil the outstanding countertrade obligations. The group issued guarantees to the value of R111m (2015/16: R80m) to enable the contracting country to raise penalties on non-fulfilment of countertrade obligations.

The group has entered into local defence contracts which require the group to impose countertrade obligations in favour of SA on all imported content. The group has, therefore, entered into back-to-back agreements with the suppliers to ensure that this obligation is offset. The group received bank guarantees from all the said suppliers which were ceded to the client.

The group provides for the cost to settle countertrade obligations when revenue is recognised on the contracts that give rise to the countertrade obligations.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	2016/17			2015/16		
	Export contracts	Local defence contracts	Total	Export contracts	Local defence contracts	Total
	Rm	Rm	Rm	Rm	Rm	Rm
25 CONTINGENT LIABILITIES (continued)						
25.5 COUNTERTRADE (continued)						
The table below summarises the group's countertrade position:						
Total countertrade obligation	7 134	5 176	12 310	7 370	3 251	10 621
Obligation discharged	(1 181)	(922)	(2 103)	(245)	(541)	(786)
Outstanding obligation	5 953	4 254	10 207	7 125	2 710	9 835
To be settled by third party	-	(2 227)	(2 227)	-	(565)	(565)
Net obligation of the group	5 953	2 027	7 980	7 125	2 145	9 270
Penalties						
Maximum penalty for non-compliance	566	213	779	693	184	877
Third-party obligation	-	(111)	(111)	-	80	80
Net group exposure	566	102	668	693	264	957
Guarantees issued						
Group issued	110	-	110	75	-	75
Third-party guarantees	-	21	21	-	24	24
	110	21	131	75	24	99
Provision to settle obligation	84	-	84	121	-	121

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
26 NOTES TO THE CONSOLIDATED STATEMENTS OF CASH FLOWS				
26.1 RECONCILIATION OF PROFIT WITH CASH RETAINED FROM OPERATIONS				
Net profit before tax	356	434	103	272
Adjusted for:	(13)	368	142	321
Loss on disposal of property, plant and equipment [1]	-	-	-	-
Depreciation [2]	142	131	103	100
Amortisation of intangible assets [2]	11	16	7	12
Remeasurement of derivatives	(199)	48	(154)	1
Remeasurement of firm commitments	186	(54)	190	(54)
Finance costs (refer note 6.1)	352	280	359	289
Finance income (refer note 6.2)	(80)	(77)	(92)	(63)
Dividends received			-	(56)
Decrease in provisions	(151)	155	(151)	95
Impairment raised on intangible assets [2]	(72)	163	(72)	159
Share of profit in associated companies (refer note 12)	(154)	(132)		
Fair value adjustment of Investment properties (refer note 4)	(48)	(162)	(48)	(162)
Operating profit before changes in net current assets	343	802	245	593
Changes in net current assets	207	(1 374)	339	(1 087)
Increase in inventories	(282)	(712)	(88)	(403)
Decrease/(Increase) in trade and other receivables	712	(1 510)	648	(1 406)
(Decrease)/Increase in trade and other payables	(223)	848	(221)	722
Cash utilised in operations	550	(572)	584	(494)

1. *Refer note 3 and 4.*
2. *Refer note 3.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17 Rm	2015/16 Rm	2016/17 Rm	2015/16 Rm
27 CAPITAL COMMITMENTS				
Approved and contracted for				
Property, plant and equipment	19	59	6	52
Land and buildings [1]	1	1	1	-
Computer equipment [1]	2	1	1	-
Machinery and equipment	16	55	4	50
Plant [1]	-	1	-	1
Vehicles [1]	-	1	-	1
Approved but not contracted for				
Property, plant and equipment	50	3	48	3
Land and buildings	12	-	10	-
Machinery and equipment	9	3	9	3
Office furniture and equipment	15	-	15	-
Plant	13	-	13	-
Vehicles	1	-	1	-
	69	62	54	55

There will be no specific financing arrangements made as these will be financed from available funds and interest bearing borrowings. All expenditure will be incurred in the following financial year.

1. No capital commitments approved but not contracted for.

	Buildings	Computer equipment	Office furniture	Plant and machinery	Total
	Rm	Rm	Rm	Rm	Rm

28 NON-CANCELLABLE LEASES

OPERATING LEASES

The group and company have certain property, plant and equipment held under operating leases. Some of the lease agreements provide for minimum annual lease payments which are due as follows:

	Buildings Rm	Computer equipment Rm	Office furniture Rm	Plant and machinery Rm	Total Rm
GROUP					
2016/17					
Less than one year	63	4	3	3	73
Between one and five years	230	1	12	4	247
More than five years	22	-	-	-	22
	315	**5**	**15**	**7**	**342**
2015/16					
Less than one year	77	5	3	2	87
Between one and five years	288	14	10	3	315
More than five years	120	-	-	-	120
	485	**19**	**13**	**5**	**522**
COMPANY					
2016/17					
Less than one year	65	2	3	1	71
Between one and five years	230	1	12	3	246
More than five years	22	-	-	-	22
	317	**3**	**15**	**4**	**339**
2015/16					
Less than one year	65	4	3	1	73
Between one and five years	288	14	10	2	314
More than five years	120	-	-	-	120
	473	**18**	**13**	**3**	**507**

Non-cancellable leases of buildings includes the Kempton Park site which Denel sold during 2007 to ACSA's subsidiary, Precinct 2A, on a sale and leaseback basis. The original lease period was five years with an option to extend for a further two periods of five years each, which Denel exercised during 2012. The lease payments are fixed for the ten-year period and quarterly lease payments are based on the purchase value of the property discounted at a fixed interest rate of 9.25% (2015/16: 9.25%). Should Denel extend the lease beyond the current ten year period, the lease payments will be based on market related rates.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

29 RELATED PARTIES

Related party transactions are disclosed in terms of the requirements of the relevant standard. Materiality has been considered in the disclosure of these transactions. Amounts smaller than R0.5m have not been included in the table.

National government and state controlled units

Denel SOC Ltd is fully controlled by its sole shareholder, the SA government represented by DPE.

The group operates in an economic environment currently dominated by entities directly or indirectly owned by the SA government. As a result of the constitutional independence of all three spheres of government in SA, only parties within the national sphere of government will be considered to be related parties.

The list of public units in the national sphere of SA government was provided by the NT.

Post-employment benefit plans

Other related parties also consist of post retirement benefit plans (refer note 32).

Key management personnel

Key management is defined as individuals with the authority and responsibility for planning, directing and controlling the activities of the entity. All individuals who are members of the Denel executive committee and the board of directors, as well as the entities' executive committees are regarded as key management.

Close family members of key management personnel are considered to be those family members who may influence, or be influenced by key management in their dealings with the entity. There were no material transactions other than the directors' emoluments detailed in the remuneration report, pages 103 to 105.

Entities within the group

Denel SOC Ltd is the ultimate parent company of the group. The company advanced loans to these entities in the group during the current and previous financial years as part of the financing plan. Other transactions within the group were on commercial terms and conditions.

A detailed breakdown of the investments in subsidiaries and associated companies is contained in note 34.

Refer note 11 and 12 for further detail.

Terms and conditions of transactions with related parties

During the year the company and its subsidiaries, in the ordinary course of business, entered into various sales and purchase of goods and services with the other related parties of the group. The effect of these transactions is included in the results of the group. These transactions occurred under terms that are no less favourable than those arranged with third parties.

29 RELATED PARTIES (continued)

The following transactions were carried out with related parties:

	2016/17				2015/16			
	National government	Major national public units	Between the company and its subsidiaries	Associated companies	National government	Major national public units	Between the company and its subsidiaries	Associated companies
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
GROUP								
Purchases of goods	3	102		235	-	14		441
Sales of goods	1 230	723		468	1 625	628		10
Services rendered	331	77		37	512	30		-
Services received	47	15		9	17	15		-
Lease payments	-	-		-	-	48		-
Lease cash received	17	3		71	24	-		-
Guarantees issued to related parties	2 954	109		-	-	-		-
Guarantees issued to third parties on behalf of related parties	-	-		117	-	-		124
Guarantees issued to third parties by related parties	1 850	-		-	-	-		-
Finance costs	-	-		1	-	-		-
Dividends received	-	-		-	-	-		25
Outstanding balances payable	13	5		138	8	1		158
Outstanding balances receivable	86	75		87	52	159		59
Provision for penalties paid	8	-		-	4	-		-
Advance payments received	2 496	63		74	-	-		177
Advance payments made	1	-		35	-	-		51
COMPANY								
Purchases of goods	3	102	69	233	-	14	56	439
Sales of goods	1 117	723	2	467	1 518	628	3	4
Services rendered	-	-	-	-	365	30	65	-
Services received	47	-	-	-	17	15	15	-
Lease payments	-	-	-	-	-	48	-	-
Lease cash received	17	3	12	71	24	-	11	-
Guarantees issued to related parties	2 954	109	-	-	-	-	-	-
Guarantees issued to third parties on behalf of related parties	-	-	-	117	-	-	-	124
Guarantees issued to third parties by related parties	1 850	-	-	-	-	-	-	-
Finance income	-	-	21	-	-	-	1	-
Finance costs	-	-	24	1	-	-	12	-
Dividends received	-	-	-	-	-	-	31	25
Outstanding balances payable	13	5	87	137	8	1	27	158
Outstanding balances receivable	86	75	49	87	52	159	21	53
Provision for penalties paid	8	-	-	-	4	-	-	-
Advance payments received	2 496	63	-	74	-	-	-	177
Advance payments made	1	-	-	35	-	-	31	51

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
29 RELATED PARTIES (continued)				
Compensation paid to key management personnel:				
Short-term employee benefits	61	48	48	45
Post-employee benefits	4	3	3	3
Share-base payments	-	2	-	2
Termination benefits	11	7	11	7
	76	60	62	57

Compensation paid to key management personnel includes information disclosed in the remuneration report, pages 103 to 105.

	2016/17	2015/16
	R'000	R'000
Directors' fees paid or accrued to the non-executive directors of the group:		
Mr LD Mantsha	891	597
Ms M Kgomongoe	367	343
Ms PM Mahlangu	279	187
Mr Mahumapelo	-	278
Ms N Mandindi	96	212
Ms R Mokoena	223	171
Mr NJ Motseki	204	238
Mr TJ Msomi	255	235
Lt Gen TM Nkabinde (rtd)	290	205
Ms KPS Ntshavheni	345	321
	2 950	2 787

29 RELATED PARTIES (continued)

	2016/17								2015/16
	Salaries	Pension fund contribution	Medical aid contribution	Other [8]	Company contribution	Short-term incentive	Loss of office	Total	Total
	R'000	R'000	R'000	R'000	R'000	R'000	R'000	R'000	R'000
Amounts paid or accrued to executives of the group:									
Executive directors									
Mr R Saloojee [1]	3 938	-	-	107	-	-	2 362	6 407	4 725
Mr F Mhlontlo [2]	1 091	-	-	299	155	-	8 282	9 827	3 497
Sub-total	**5 029**	**-**	**-**	**406**	**155**	**-**	**10 644**	**16 234**	**8 222**
Prescribed officers									
Mr ZN Ntshepe	2 074	80	-	604	193	1 470	-	4 421	4 009
Mr ZM Mhlwana	2 840	-	-	640	311	1 723	-	5 514	3 262
Ms N Davies	1 724	67	82	240	118	966	-	3 197	3 142
Mr T Kleynhans [3] Mr	1 063	43	84	169	76	1 344	-	2 779	-
GTT Mbele [4]	1 971	74	75	164	133	1 680	-	4 097	-
Ms NF Msiza [5]	1 357	48	-	113	85	-	-	1 603	-
Ms V Qinga [6]	1 669	62	77	139	109	966	-	3 022	-
Mr JM Wessels [7]	760	30	21	142	53	-	-	1 006	3 365
Sub-total	**13 458**	**404**	**339**	**2 211**	**1 078**	**8 149**	**-**	**25 639**	**13 778**
Total	**18 487**	**404**	**339**	**2 617**	**1 233**	**8 149**	**10 644**	**41 873**	**22 000**

1. *Resigned on 8 November 2016.*
2. *Resigned on 30 August 2016.*
3. *Appointed as executive manager on 1 August 2016.*
4. *Appointed as executive manager on 10 April 2016.*
5. *Appointed as executive manager on 7 April 2016, resigned on 28 February 2017.*
6. *Appointed as executive manager on 1 April 2017.*
7. *Resigned on 30 September 2016.*
8. *Other includes mainly 13th cheques, car, cellphone and other travel allowances.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

30 FINANCIAL RISK MANAGEMENT

The group is exposed to various financial risks due to the nature and diversity of its activities and the use of various financial instruments. These risks include:

» Credit risk
» Liquidity risk
» Market risk

Information about the group's exposure to each of the above risks, its objectives, policies and processes for measuring and managing these risks are included in this note. The group's management of capital is also discussed. Further quantitative disclosures are included throughout the consolidated annual financial statements.

The board of directors has overall responsibility for the establishment and oversight of the group's risk management framework. The board has delegated its responsibility to the A&R committee, who is responsible for the development and monitoring of the group's risk management policies. The committee meets three times a year and regularly reports to the board on its activities. The group's risk management policies are established to identify and analyse the risks faced by the group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the group's activities.

The roles and responsibilities of the A&R committee include:

» Approval of all counter parties;
» Approval of new instruments;
» Approval of foreign exchange transaction company policy;
» Approval of the investment policy;
» Approval of corporate treasury policy and procedure manual; and
» Recommend to the board for approval of the long-term funding requirements.

The A&R committee is assisted in its oversight role by the internal audit department, who undertakes regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the A&R committee.

30.1 CREDIT RISK

Credit risk is the risk of financial loss to the group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. This risk arises principally from the group's receivables from customers (loans receivable, trade and sundry receivables) and its centralised treasury activities (derivative financial instruments and cash and cash equivalents).

Receivables from customers

The A&R committee of the board has an established policy for the management of credit risk arising on receivables from customers. Under this policy the creditworthiness of potential and existing customers is assessed prior to contracting with new or existing customers. Entities are required to review the following before entering into a contract or submitting a proposal to a potential client:

- » The potential client's compliance with statutory and regulatory conditions;
- » The political risk of the potential client's country;
- » The previous business record that the existing client had with entities within the group (includes but is not limited to payment history);
- » Obtain the most recent credit rating from the group's treasury department, of the country that the potential customer operates in. Countries are graded by major international banks and these grading are published on a regular basis. The group uses the international publication, "Institutional investor" as a basis for its country risk assessments; and
- » Whether finance is available to the potential client.

The policy further requires that for specifically identified contracts, the contractual terms must provide for the retention of ownership over goods until full and final payment has been received. Additionally, security for payment must also be contractually stipulated. Security usually takes the form of irrevocable letters of credit, bank guarantees (from first class international banks in acceptable countries)/bonds, promissory notes and credit insurance. In the case of high risk clients who are unable to provide security over future payments, the group may transact with them only on a pre-payment basis.

Overdue amounts are individually assessed and if it is evident that an amount will not be recovered, it is impaired and legal action is instituted to recover the amounts.

Financial instruments managed by the group's treasury function

The A&R committee of the board oversees the group's treasury operations and has an established policy for the management of credit risk arising from treasury activities. Counterparties are assessed based on their official Fitch ratings. Counterparties are approved by the A&R committee. Various rating agency publications and financial news regarding counterparties are regularly monitored by the treasury department. The group limits its exposure by spreading investments over the approved counterparties, as well as by investing with certain counterparties, usually banks with F1 and F1+ short-term ratings, AA long-term ratings and a minimum of R2bn in capital. Treasury is allowed to invest 25% of its portfolio with a counterparty that is F1+ rated and 15% with a counterparty that is F1 rated. Annual bank facilities are negotiated with each bank and is approved by the GCFO.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

30 FINANCIAL RISK MANAGEMENT (continued)

30.1 CREDIT RISK (continued)

Credit exposure and concentration of credit risk

The carrying amount of financial assets represents the maximum credit exposure at the reporting date. The following table represents the concentration of risk for all non-derivative financial assets:

	2016/17			2015/16		
	Domestic	Foreign	Total	Domestic	Foreign	Total
	Rm	Rm	Rm	Rm	Rm	Rm
GROUP						
Trade receivables [1]	237	1 984	2 221	327	2 320	2 647
Government and related units	141	245	386	245	717	962
Non-government units	96	1 739	1 835	82	1 603	1 685
Sundry receivables [1]	100	1	101	53	1	54
Government and related units	57	1	58	3	-	3
Non-government units	43	-	43	50	1	51
Interest receivables [1]	3	-	3	3	-	3
Non-government units	3	-	3	3	-	3
Cash and short-term deposits [2]	1 710	311	2 021	1 626	377	2 003
Non-government units	1 710	311	2 021	1 626	377	2 003
	2 050	2 296	4 346	2 009	2 698	4 707
COMPANY						
Trade receivables [1]	226	1 603	1 829	313	1 882	2 195
Government and related units	134	245	379	232	210	442
Non-government units	92	1 358	1 450	81	1 672	1 753
Sundry receivables [1]	41	1	42	36	1	37
Government and related units	41	1	42	3	-	3
Non-government units	-	-	-	33	1	34
Interest receivables [1]	1	-	1	1	-	1
Non-government units	1	-	1	1	-	1
Cash and short-term deposits [2]	1 326	230	1 556	1 422	366	1 788
Non-government units	1 326	230	1 556	1 422	366	1 788
	1 594	1 834	3 428	1 772	2 249	4 021

1. *Refer note 15.*
2. *Refer note 17.*

30 FINANCIAL RISK MANAGEMENT (continued)

30.1 CREDIT RISK (continued)

Ageing

The ageing of financial assets at the reporting date is included below. The ageing categories include:

	2016/17				2015/16			
	Receivables not impaired	Receivables impaired	Impairment amount	Carrying value	Receivables not impaired	Receivables impaired	Impairment amount	Carrying value
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
GROUP								
Trade receivables [1]	2 221	42	(42)	2 221	2 647	55	(55)	2 647
Not past due	1 173	1	(1)	1 173	2 089	-	-	2 089
Past due								
Less than 30 days	198	-	-	198	98	-	-	98
30 to 60 days	126	-	-	126	228	-	-	228
61 to 90 days	20	-	-	20	16	-	-	16
More than 90 days	704	41	(41)	704	216	55	(55)	216
Sundry receivables [1]	101	1	(1)	101	54	2	(2)	54
Not past due, not impaired	97	-	-	101	54	-	-	54
Past due								
More than 90 days	4	1	(1)	4	-	2	(2)	-
Interest receivables [1]	3	-	-	3	3	-	-	3
Not past due, not impaired	3	-	-	3	3	-	-	3
Cash and short-term deposits [2]	2 021	-	-	2 021	2 003	-	-	2 003
Not past due, not impaired	2 021	-	-	2 021	2 003	-	-	2 003
	4 346	43	(43)	4 346	4 707	57	(57)	4 707
COMPANY								
Trade receivables [1]	1 677	-	152	1 829	2 195	55	(55)	2 195
Not past due	942	-	152	1 029	1 748	-	-	1 748
Past due								
Less than 30 days	119	-	-	119	46	-	-	46
30 to 60 days	9	-	-	9	169	-	-	169
61 to 90 days	-	-	-	-	16	-	-	16
More than 90 days	607	-	-	607	216	55	(55)	216
Sundry receivables [1]	39	-	-	42	37	-	-	37
Not past due, not impaired	39	-	-	39	37	-	-	37
Past due								
More than 90 days	3	-	-	3	-	-	-	-
Interest receivables [1]	1	-	-	1	1	-	-	1
Not past due, not impaired	1	-	-	1	1	-	-	1
Cash and short-term deposits [2]	1 556	-	-	1 556	1 788	-	-	1 788
Not past due, not impaired	1 556	-	-	1 556	1 788	-	-	1 788
	3 273	-	152	3 428	4 021	55	(55)	4 023

1. *Refer note 15.*
2. *Refer note 17.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
30 FINANCIAL RISK MANAGEMENT (continued)				
30.1 CREDIT RISK (continued)				
Security held over non-derivative financial assets				
Irrevocable Letters of Credit confirmed by foreign banks	332	347	332	347

30.2 LIQUIDITY RISK

Liquidity rsk is the risk that the group will not have sufficient financial resources to meet its obligations when they fall due or will have to do so at excessive cost. This risk may arise when there are mismatches between receipts and payments. As well as when where there are limited funds available to fund that gap.

The group has a centralised treasury manages the liquidity of the group taking into account assets, liabilities and commitments to ensure there is sufficient cash within the group as a whole. This ensures that updated cash flow information and projections of future cash flows are received from entities on a daily, weekly and monthly basis (depending on the type of funding required). Measures have been introduced to ensure that the cash flow information received is accurate and complete. Further to that the group maintains a range of funding sources and liquidity contingency plans.

The group received government guarantees of R1.85bn (2015/16: R1.85bn) to raise borrowings. These guarantees expire on 30 September 2017 (refer note 21.5).

Surplus funds are deposited in liquid assets (i.e. negotiable certificates or deposits and call deposits) (refer note 17).

	GROUP 2016/17 Rm	GROUP 2015/16 Rm	COMPANY 2016/17 Rm	COMPANY 2015/16 Rm
Undrawn credit facilities				
SA Rand (Rm)	134	275	134	275
US Dollar ($m)	50	50	50	50

The credit banking facilities are unsecured, bear interest at a rate linked to prime and are subject to annual review. The facilities are in place to ensure liquidity.

	Contractual undiscounted cash flows					
	Carrying amount	Total cash flows	Less than three months	Between three and twelve months	Between one and five years	More than five years
	Rm	Rm	Rm	Rm	Rm	Rm

30 FINANCIAL RISK MANAGEMENT (continued)

30.2 LIQUIDITY RISK (continued)

Exposure to liquidity risk

The following are the contractual maturities of financial liabilities, including interest payments and excluding the impact of netting agreements:

	Carrying amount Rm	Total cash flows Rm	Less than three months Rm	Between three and twelve months Rm	Between one and five years Rm	More than five years Rm
GROUP						
2016/17						
Interest bearing loans and borrowings (refer note 21)	3 265	3 426	534	1 946	946	-
Trade and other payables (refer note 24)	1 612	1 612	899	713	-	-
Derivative financial liabilities (refer note 16.2)	102	102	16	86	-	-
Guarantees (refer note 25.1)	7 168	7 168	7 168	-	-	-
	12 147	**12 269**	**8 578**	**2 745**	**946**	**-**
2015/16						
Interest bearing loans and borrowings (refer note 21)	3 717	4 104	807	1 031	2 259	7
Trade and other payables (refer note 24)	1 741	1 741	1 535	206	-	-
Derivative financial liabilities (refer note 16.2)	272	272	43	187	42	-
Guarantees (refer note 25.1)	7 502	7 502	1 065	1 279	3 404	1 754
	13 232	**13 619**	**3 450**	**2 703**	**5 705**	**1 761**
COMPANY						
2016/17						
Interest bearing loans and borrowings (refer note 21)	3 005	3 155	515	1 867	773	-
Trade and other payables (refer note 24)	1 292	1 292	659	633	-	-
Derivative financial liabilities (refer note 16.2)	25	25	15	10	-	-
Guarantees (refer note 25.1)	6 613	6 613	6 613	-	-	-
	10 935	**11 085**	**7 802**	**2 510**	**773**	**-**
2015/16						
Interest bearing loans and borrowings (refer note 21)	3 890	4 246	977	1 027	2 242	-
Trade and other payables (refer note 24)	1 417	1 417	1 256	161	-	-
Derivative financial liabilities (refer note 16.2)	218	218	60	158	-	-
Guarantees (refer note 25.1)	6 325	6 325	865	1 155	2 552	1 753
	11 850	**12 206**	**3 158**	**2 501**	**4 794**	**1 753**

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

30 FINANCIAL RISK MANAGEMENT (continued)

30.3 MARKET RISK

Market risk is the risk that movements in market risk factors, including foreign exchange rates, interest rates and commodity prices will affect the group's revenue and operational costs, as well as the value of its holdings of financial instruments. The objective of the group's market risk management policy is to manage and control market risk exposures to minimise the impact of adverse market movements with respect to revenue protection and to optimise the funding of the business operations.

Entities

Business entities, including subsidiaries are responsible for the preparation and presentation of market risk information as it affects the relevant entity. Information will be submitted to treasury where it is monitored and further analysed to be used in the decision making process. In certain instances an entity will prepare and use market risk information for its own purposes.

Treasury

Treasury is responsible for reporting to the A&R committee on market risk elements on a quarterly basis. The report submitted includes important positional and hedge information on currency, interest rate and commodities, and is used by the committee to determine the market risk strategy going forward. In addition, key market risk information is reported to the GCFO and executive committee on a weekly and monthly basis respectively.

A significant element of the market risk encountered arises from financial instruments that are managed centrally within the Treasury function of the group. These include more complex instruments used for hedging purposes.

Interest rate risk

Interest rate risk arises due to adverse movements in domestic and foreign interest rates. The group is primarily exposed to upward interest rate movements on loans and borrowings. There is no other exposure to fair value interest rate risk as all fixed rate financial instruments are measured at amortised cost.

The A&R committee determines the interest rate risk strategy based on economic expectations and reports received from the treasury department. Treasury department monitors interest rates on a daily basis and the policy is to maintain short-term cash surpluses at floating rates of interest. Interest rate and funding transactions are governed by the authorised treasury procedures manual.

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
30 FINANCIAL RISK MANAGEMENT (continued)				
30.3 MARKET RISK (continued)				
At the reporting date the interest rate profile of the group's interest bearing financial instruments was as follows:				
Fixed rate instruments				
Cash and short-term deposits (refer note 17.1)	49	74	49	14
Commercial paper (refer note 21 and 21.6)	52	200	52	200
Loans and borrowings (refer note 21)	603	613	585	587
Fair value sensitivity analysis for fixed rate instruments				
The group does not account for any fixed rate financial-assets and liabilities at fair value through profit and loss therefore a change in interest rates at the reporting date would not affect profit and loss.				
Variable rate instruments				
Cash and short-term deposits (refer note 17.1)	1 972	1 929	1 507	1 774
Commercial paper (refer note 21 and 21.6)	148	-	148	-
Loans and borrowings (refer note 21)	2 662	3 104	2 419	3 303
Cash flow sensitivity analysis for variable rate instruments				
A change of 50 basis points in interest rates at the reporting date would have increased or decreased profit and loss by the amounts shown below. This assumes that all other variables remain constant. The impact on the group's equity is equal to the impact on the profit and loss.				
Cash and cash equivalents				
Net effect on profit and loss is equal but opposite for a 50 basis points increase on the financial instruments listed above.	4	11	4	11

CURRENCY RISK

Currency risk arises from the movement in foreign exchange rates. The group's currency exposures result primarily from the import of raw materials, foreign sales of goods and services, as well as foreign bank account holdings. Foreign exchange embedded derivatives are recognised when the group has entered into contracts denominated in foreign currencies, which are neither the measurement currencies of parties to the contract, nor the currencies in which those commodities are routinely traded in international commerce. Foreign exchange embedded derivatives are not recognised for contracts denominated in a common currency. No speculating in foreign currency is allowed within the group.

Treasury is responsible for the hedging of foreign currency exposure in terms of information received from the business entities. Currency exposures are hedged based on an 18 month rolling period, which requires any currency exposure forecast for the next 18 months to be covered. Hedging instruments consists of forward exchange contracts and, to a limited extent, currency options. Revaluations of hedged positions are performed on a daily basis to check that these are in line with the underlying Foreign Exchange Policy. The hedging instrument is entered into once the exposure is firm and ascertainable, i.e. there is an underlying contract in place. Currency exposures are reported to the GCFO on a weekly basis and to the exco on a monthly basis.

Bank accounts of foreign offices are not hedged. Proceeds received from export contracts that would be used to pay foreign suppliers on the same contract are natural hedged by keeping funds in the controlled foreign currency (CFC) accounts.

A CFC account is a transactional account denominated in a foreign currency, i.e. any currency other than Rand. It is available in all major currencies and is a useful mechanism for managing foreign currency receipts and payments.

Net gains/(loss) on financial instruments are disclosed in notes 3, 4 and 5.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	2016/17		2015/16	
	USD	EUR	USD	EUR
	m	m	m	m
30 FINANCIAL RISK MANAGEMENT (continued)				
30.3 MARKET RISK (continued)				
CURRENCY RISK (continue)				
The group's exposure to currency risk was as follows based on the foreign currency notional amounts:				
GROUP				
Assets	101	92	533	307
Trade receivables	48	77	42	81
Controlled foreign currency accounts (CFC)	17	6	2	5
Firm commitments (export revenue)	36	9	489	221
Liabilities	(15)	(28)	(27)	163
Trade payables	(7)	(1)	(11)	(12)
Firm commitments (import)	(8)	(27)	(16)	175
Gross balance sheet exposure	86	64	506	470
Forecast transactions (revenue)	38	7	358	208
Forecast transactions (purchases)	(16)	(19)	(16)	(175)
Gross balance sheet exposure	108	52	848	503
Forward exchange contracts				
Export revenue	(36)	(9)	(489)	(221)
Imports	8	19	16	175
Net exposure	80	62	375	457

	2016/17		2015/16	
	USD	EUR	USD	EUR
	m	m	m	m
30 FINANCIAL RISK MANAGEMENT (continued)				
30.3 MARKET RISK (continued)				
CURRENCY RISK (continue)				
COMPANY				
Assets	77	80	533	307
Trade receivables	42	69	42	81
Controlled foreign currency accounts (CFC)	6	1	2	5
Firm commitments (export revenue)	29	10	489	221
Liabilities	(12)	(13)	(27)	163
Trade payables	(4)	(6)	(11)	(12)
Firm commitments (import)	(8)	(7)	(16)	175
Gross balance sheet exposure	65	67	506	470
Forecast transactions (revenue)	27	8	358	208
Forecast transactions (purchases)	(7)	(7)	(16)	(175)
Gross balance sheet exposure	85	68	848	503
Forward exchange contracts				
Export revenue	(29)	(10)	(489)	(221)
Import	8	7	16	175
Net exposure	64	65	375	457
Strengthening of the Rand				
Group	39	63	24	62
Company	29	44	24	62

A 5% strengthening of the Rand against the above currencies at 31 March would have increased/(decreased) profit and loss by the above mentioned amounts.

A 5% weakening of the Rand against the above currencies at 31 March would have had an equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant. The impact on the group's equity is equal to the impact on the profit and loss.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	2016/17			2015/16		
	Foreign currency notional amount	Local currency	Fair value	Foreign currency notional amount	Local currency	Fair value
		Rm	Rm		Rm	Rm
30 FINANCIAL RISK MANAGEMENT (continued)						
30.3 MARKET RISK (continued)						
CURRENCY RISK (continue)						
Foreign currency derivatives						
The fair value of foreign currency derivatives are disclosed in note 16. The following foreign exchange contracts existed at 31 March:						
GROUP						
Foreign currency derivatives						
Revenue contracts						
Euro (EUR)	8 785 769	87	78	221 311 733	6 042	6 177
Sterling (GBP)	57 977	1	-	360 144	8	8
Switzerland (CHF)	513 143	7	6	5 934 796	92	93
US Dollar (USD)	36 033 191	8 960	9 889	489 128 520	18 786	19 830
		9 055	9 973		24 928	26 108
Purchase contracts						
Euro (EUR)	19 147 023	453	506	175 128 868	3 896	3 941
Australian Dollar (AUD) [1]	-	-	-	87 600	-	-
Sterling (GBP)	2 315 530	25	31	7 450 919	714	732
Switzerland (CHF)	191 678	1	1	13 410 216	206	206
US Dollar (USD)	8 447 633	139	161	15 620 439	244	258
		618	699		5 060	5 137
COMPANY						
Foreign currency derivatives						
Revenue contracts						
Euro (EUR)	9 902 618	140	146	214 440 296	4 789	4 805
Sterling (GBP)	79 700	1	1	360 144	8	8
Switzerland (CHF)	513 413	7	6	5 934 796	92	93
US Dollar (USD)	2 863 527	400	401	423 787 592	6 342	6 348
		548	554		11 231	11 254
Purchase contracts						
Euro (EUR)	7 164 023	106	106	169 783 973	2 873	2 895
Australian Dollar (AUD) [1]	-	-	-	87 600	-	-
Sterling (GBP)	487 401	8	8	4 242 349	92	93
Switzerland (CHF)	191 678	1	1	13 410 216	206	206
US Dollar (USD)	7 530 173	125	125	14 966 801	221	225
		240	240		3 392	3 419

1. *2015/16: Purchase contracts: Foreign currency notial amount AUD87 600, Local currency R8 287, Fair value R108 879.*

30 FINANCIAL RISK MANAGEMENT (continued)

30.3 MARKET RISK (continued)

CURRENCY RISK (continue)

Maturity table

	Foreign currency notional amount							
	2016/17				2015/16			
	One year	Two years	Three to five years	Total	One year	Two years	Three to five years	Total
GROUP								
Foreign currency derivatives								
Revenue contracts								
Euro (EUR)	8 785 769	-	-	8 785 769	221 311 733	-	-	221 311 733
Sterling (GBP)	57 977	-	-	57 977	360 144	-	-	360 144
Switzerland (CHF)	513 143	-	-	513 143	5 934 796	-	-	5 934 796
US Dollar (USD)	33 490 757	2 542 434	-	36 033 191	459 400 487	29 728 033	-	489 128 520
Purchase contracts								
Euro (EUR)	19 147 023	-	-	19 147 023	171 235 033	2 688 548	1 205 287	175 128 868
Australian Dollar (AUD)	-	-	-	-	87 600	-	-	87 600
Sterling (GBP)	2 315 530	-	-	2 315 530	6 092 139	1 358 780	-	7 450 919
Switzerland (CHF)	191 678	-	-	191 678	13 318 838	-	91 378	13 410 216
US Dollar (USD)	8 447 633	-	-	8 447 633	15 620 439	-	-	15 620 439
COMPANY								
Foreign currency derivatives								
Revenue contracts								
Euro (EUR)	9 902 618	-	-	9 902 618	214 440 296	-	-	214 440 296
Sterling (GBP)	79 700	-	-	79 700	360 144	-	-	360 144
Switzerland (CHF)	513 413	-	-	513 413	5 934 796	-	-	5 934 796
US Dollar (USD)	2 863 527	-	-	2 863 527	423 787 592	-	-	423 787 592
Purchase contracts								
Euro (EUR)	7 164 023	-	-	7 164 023	168 252 931	325 755	1 205 287	169 783 973
Australian Dollar (AUD)	-	-	-	-	87 600	-	-	87 600
Sterling (GBP)	487 401	-	-	487 401	4 109 139	133 210	-	4 242 349
Switzerland (CHF)	191 678	-	-	191 678	13 318 838	-	91 378	13 410 216
US Dollar (USD)	7 530 173	-	-	7 530 173	14 966 801	-	-	14 966 801

Firm commitments

Contracts (sale or purchase) denominated in a foreign currency, which is neither a common currency, the measurement currency of any party to the contract, nor the currency in which the commodity is routinely traded in international commerce, contains a foreign exchange embedded derivative (to sell or buy the equivalent amount of foreign currency), is separated and accounted for at fair value even though the contract is not recognised. Denel view the USD, GBP and EUR as common currencies.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	2016/17			2015/16		
	Foreign currency notional amount	Local currency	Fair value	Foreign currency notional amount	Local currency	Fair value
	m	Rm	Rm	m	Rm	Rm
30 FINANCIAL RISK MANAGEMENT (continued)						
30.3 MARKET RISK (continued)						
FOREIGN CURRENCIES						
Export transactions						
Firm commitments relating to foreign exchange contracts						
Euro (EUR) [1]	-	5	5	5	77	84
Sterling (GBP) [2]	-	-	-	1	11	10
Switzerland (CHF)	-	-	-	1	4	4
US Dollar (USD)	21	289	292	46	705	705
		294	297		797	803
Firm commitments relating to foreign exchange options						
Euro (EUR)	-	-	-	10	170	177
US Dollar (USD)	-	-	-	59	729	572
		-	-		899	749
Import transactions						
Firm commitments relating to foreign exchange contracts						
Euro (EUR)	6	91	90	13	196	212
Sterling (GBP) [3]	-	2	2	1	3	3
Switzerland (CHF) [4]	-	1	1	1	15	14
US Dollar (USD) [5]	-	5	5	1	7	7
		99	98		221	236

1. *2016/17: Purchase contracts: €381 014, Local currency R5 287 986, Fair value R5 570 805.*
2. *2016/17: Purchase contracts: £27 800, Local currency R450 060, Fair value R471 827.*
3. *2016/17: Revenue contracts: £133 210, Local currency R2 222 209, Fair value R2 2295 315.*
4. *2016/17: Revenue contracts: CHF91 378, Local currency R1 215 133, Fair value R1 239 864.*
5. *2016/17: Revenue contracts: US$382 534, Local currency R5 033 246, Fair value R5 308 488.*

	Foreign currency notional amount (m)							
	2016/17				2015/16			
	One year	Two years	Three to five years	Total	One year	Two years	Three to five years	Total
30 FINANCIAL RISK MANAGEMENT (continued)								
30.3 MARKET RISK (continued)								
FOREIGN CURRENCIES (continued)								
Maturity table								
Export contracts								
Firm commitments relating to foreign exchange contracts								
Euro (EUR) [1]	-	-	-	-	5	-	-	5
Sterling (GBP) [2]	-	-	-	-	1	-	-	1
Switzerland (CHF)	-	-	-	-	1	-	-	1
US Dollar (USD)	21	-	-	21	46	-	-	46
Firm commitments relating to foreign exchange options								
Euro (EUR)	-	-	-	-	10	-	-	10
US Dollar (USD)	-	-	-	-	59	-	-	59

Export transactions

Firm commitments relating to foreign exchange contracts

The maturity of all export transaction firm commitments is within one year.

Import transactions

Firm commitments relating to foreign exchange contracts

The maturity of all import transaction firm commitments is within one year.

Commodity risk

As at 31 March 2017 the group had no commodity swap contracts (2015/16: Rnil).

1. *2016/17: Export contracts: €381 014 matures within one year.*
2. *2016/17: Exports contracts: £27 800 matures within one year.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	Loans and receivables Rm	Liabilities at amortised cost Rm	At fair value through profit and loss Rm	Carrying amount Rm	Fair value Rm
30 FINANCIAL RISK MANAGEMENT (continued)					
30.4 FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES					
GROUP					
2016/17					
Financial assets					
Cash and cash equivalents (refer note 17.1 and 17.2)	2 021			2 021	2 021
Other financial assets (refer note 16.1)			209	209	209
Trade and other receivables (refer note 15)	2 325			2 325	2 325
	4 346		209	4 555	4 555
Financial liabilities					
Interest bearing borrowings (refer note 21)		(3 265)		(3 265)	(3 265)
Other financial liabilities (refer note 16.2)			(170)	(170)	(170)
Preference dividends payable		(6)		(6)	(6)
Trade and other payables (refer note 24)		(1 612)		(1 612)	(1 612)
		(4 883)	(170)	(5 053)	(5 053)
Net financial assets/(liabilities)	4 346	(4 883)	39	(498)	(498)
2015/16					
Financial assets					
Cash and cash equivalents (refer note 17.1 and 17.2)	2 003			2 003	2 003
Other financial assets (refer note 16.1)			361	361	361
Trade and other receivables (refer note 15)	2 704			2 704	2 704
	4 707		361	5 068	5 068
Financial liabilities					
Interest bearing borrowings (refer note 21)		(3 717)		(3 717)	(3 717)
Other financial liabilities (refer note 16.2)			(331)	(331)	(331)
Preference dividends payable		(3)		(3)	(3)
Trade and other payables (refer note 24)		(1 741)		(1 741)	(1 741)
		(5 461)	(331)	(5 792)	(5 792)
Net financial assets/(liabilities)	4 707	(5 461)	30	(724)	(724)

	Loans and receivables Rm	Liabilities at amortised cost Rm	At fair value through profit and loss Rm	Carrying amount Rm	Fair value Rm
30 FINANCIAL RISK MANAGEMENT (continued)					
30.4 FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES (continued)					
COMPANY					
2016/17					
Financial assets					
Cash and cash equivalents (refer note 17.1 and 17.2)	1 556			1 556	1 556
Other financial assets (refer note 16.1)			141	141	141
Trade and other receivables (refer note 15)	1 921			1 921	1 921
Subsidiaries: Loans and receivables (refer note 11)	601			601	601
	4 078		141	4 219	4 219
Financial liabilities					
Loans and borrowings (refer note 21)		(3 005)		(3 005)	(3 005)
Other financial liabilities (refer note 16.2)			(93)	(93)	(93)
Trade and other payables (refer note 24)		(1 292)		(1 292)	(1 292)
Subsidiaries: Loans and borrowings (refer note 11)		(456)		(456)	(456)
		(4 753)	(93)	(4 846)	(4 846)
Net financial assets/(liabilities)	4 114	(4 753)	48	(627)	(627)
2015/16					
Financial assets					
Cash and cash equivalents (refer note 17.1 and 17.2)	1 788			1 788	1 788
Other financial assets (refer note 16.1)			361	361	361
Trade and other receivables (refer note 15)	2 258			2 258	2 258
Subsidiaries: Loans and receivables (refer note 11)	386			386	386
	4 432		361	4 793	4 793
Financial liabilities					
Interest bearing borrowings (refer note 21)		(3 890)		(3 890)	(3 890)
Other financial liabilities (refer note 16.2)			(277)	(277)	(277)
Trade and other payables (refer note 24)		(1 417)		(1 417)	(1 417)
Subsidiaries: Loans and borrowings (refer note 11)		(195)		(195)	(195)
		(5 502)	(277)	(5 779)	(5 779)
Net financial assets/(liabilities)	4 432	(5 502)	84	(986)	(986)

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

30 FINANCIAL RISK MANAGEMENT (continued)

30.3 FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES (continued)

The group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

Various valuation techniques and assumptions are utilised for the purpose of calculating fair value. The group does not hold any financial instruments traded in an active market, except for the investment in listed equity instruments. Fair value is determined using valuation techniques as outlined below. Where possible, inputs are based on quoted prices and other market determined variables. The calculation of fair value requires various inputs into the valuation methodologies used.

The source of the inputs used affects the reliability and accuracy of the valuations. Significant inputs have been classified into the hierarchical levels in line with *IFRS 13, Fair value measurement* as shown below.

» Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities.
» Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.
» Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

Currently the only financial assets and liabilities that are measured at fair value are the financial assets and liabilities disclosed in note 16. During the year there were no transfers between any of the levels of fair value measurements. Transfers between levels are considered to have occurred at the date of the event or change in circumstances.

Financial instrument	Valuation method	Significant inputs	Fair value hierarchy of inputs
Financial assets			
Investment properties (refer note 9)	Refer note 1.4.6.	Refer note 1.4.6.	Level 3
Derivative financial assets (refer note 16.1)	Market comparison technique: The fair value of foreign currency contracts is marked-to-market by comparing the contracted forward rate to the present value of the current forward rate of an equivalent contract with the same maturity date.	Forward exchange contracted rates, market foreign exchange rates, forward contract rates, market commodity prices.	Level 2
Non-current assets held for sale (refer note 18)	Refer note 1.4.18.	Refer note 1.4.18.	Level 3
Cash and cash equivalents (refer note 17)	Refer note 1.4.4.	Refer note 1.4.4.	Level 2
Trade and other receivables (refer note 15)	Refer note 1.4.4. *	Refer note 1.4.4. *	Level 2
Financial liabilities			
Derivative financial liabilities (refer note 16.2)	Refer derivative financial assets in this table.	Derivative financial assets in this table.	Level 2
Loans and borrowings (refer note 21)	Refer note 1.4.4.	Refer note 1.4.4.	Level 2
Preference dividends payable	**	**	Level 2
Trade and other payables (refer note 24)	Refer note 1.4.4. *	Refer note 1.4.4. *	Level 2

All other financial assets and liabilities carrying amount approximates fair value.

* *The fair value of these instruments approximates their carrying value, due to their short-term nature.*
** *The carrying value is considered to reflect its fair value.*

	Carrying amount	Fair value	Level 1	Level 2	Level 3	Total
	Rm	Rm	Rm	Rm	Rm	Rm

30 FINANCIAL RISK MANAGEMENT (continued)

30.4 FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES (continued)

The categorisation of each class of financial asset and liability, including their fair values, are included below:

	Carrying amount Rm	Fair value Rm	Level 1 Rm	Level 2 Rm	Level 3 Rm	Total Rm
GROUP						
2016/17						
Assets measured at fair value						
Investment properties (refer note 9)	728	728	-	-	728	728
Other financial assets (refer note 16.1)	209	209	-	209	-	209
Non-current assets held for sale (refer note 18)	-	-	-	-	-	-
Assets not measured at fair value						
Cash and cash equivalents (refer note 17.1 and 17.2)	2 021	2 021	-	2 021	-	2 021
Trade and other receivables (refer note 15)	2 325	2 325	-	2 325	-	2 325
	5 283	5 283	-	4 555	728	5 283
Liabilities measured at fair value						
Other financial liabilities (refer note 16.2)	(170)	(170)	-	(170)	-	(170)
Liabilities not measured at fair value						
Loans and borrowings (refer note 21)	(3 265)	(3 265)	-	(3 265)	-	(3 265)
Preference dividends payable	(6)	(6)	-	(6)	-	(6)
Trade and other payables (refer note 24)	(1 612)	(1 612)	-	(1 612)	-	(1 612)
	(5 053)	(5 053)	-	(5 053)	-	(5 053)
Net value	230	230	-	(498)	728	230
2015/16						
Assets measured at fair value						
Investment properties (refer note 9)	680	680	-	-	680	680
Other financial assets (refer note 16.1)	361	361	-	361	-	361
Non-current assets held for sale (refer note 18)	156	156	-	-	156	156
Assets not measured at fair value						
Cash and cash equivalents (refer note 17.1 and 17.2)	2 003	2 003	-	2 003	-	2 003
Trade and other receivables (refer note 15)	2 704	2 704	-	2 704	-	2 704
	5 904	5 904	-	5 068	836	5 904
Liabilities measured at fair value						
Other financial liabilities (refer note 16.2)	(331)	(331)	-	(331)	-	(331)
Liabilities not measured at fair value						
Loans and borrowings (refer note 21)	(3 717)	(3 717)	-	(3 717)	-	(3 717)
Preference dividends payable	(3)	(3)	-	(3)	-	(3)
Trade and other payables (refer note 24)	(1 741)	(1 741)	-	(1 741)	-	(1 741)
	(5 792)	(5 792)	-	(5 792)	-	(5 792)
Net value	112	112	-	(724)	836	112

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	Carrying amount Rm	Fair value Rm	Level 1 Rm	Level 2 Rm	Level 3 Rm	Total Rm
30 FINANCIAL RISK MANAGEMENT (continued)						
30.4 FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES (continued)						
COMPANY						
2016/17						
Assets measured at fair value						
Investment properties (refer note 9)	719	719	-	-	719	719
Other financial assets (refer note 16.1)	141	141	-	141	-	141
Assets not measured at fair value						
Cash and cash equivalents (refer note 17.1 and 17.2)	1 556	1 556	-	1 556	-	1 556
Subsidiaries: Loans and receivables (refer note 11)	601	601	-	601	-	601
Trade and other receivables (refer note 15)	1 921	1 921	-	1 921	-	1 921
	4 938	4 938	-	4 219	719	4 938
Liabilities measured at fair value						
Other financial liabilities (refer note 16.2)	(93)	(93)	-	(93)	-	(93)
Liabilities not measured at fair value						
Loans and borrowings (refer note 21)	(3 005)	(3 005)	-	(3 005)	-	(3 005)
Subsidiaries: Loans and borrowings (refer note 11)	(456)	(456)	-	(456)	-	(456)
Trade and other payables (refer note 24)	(1 292)	(1 292)	-	(1 292)	-	(1 292)
	(4 846)	(4 846)	-	(4 846)	-	(4 846)
Net value	92	92	-	(627)	719	92
2015/16						
Assets measured at fair value						
Investment properties (refer note 9)	671	671	-	-	671	671
Other financial assets (refer note 16.1)	361	361	-	361	-	361
Non-current assets held for sale (refer note 18)	156	156	-	-	156	156
Assets not measured at fair value						
Cash and cash equivalents (refer note 17.1 and 17.2)	1 788	1 788	-	1 788	-	1 788
Subsidiaries: Loans and receivables (refer note 11)	386	386	-	386	-	386
Trade and other receivables (refer note 15)	2 258	2 258	-	2 258	-	2 258
	5 620	5 620	-	4 793	827	5 620
Liabilities measured at fair value						
Other financial liabilities (refer note 16.2)	(277)	(277)	-	(277)	-	(277)
Liabilities not measured at fair value						
Loans and borrowings (refer note 21)	(3 890)	(3 890)	-	(3 890)	-	(3 890)
Subsidiaries: Loans and borrowings (refer note 11)	(195)	(195)	-	(195)	-	(195)
Trade and other payables (refer note 24)	(1 417)	(1 417)	-	(1 417)	-	(1 417)
	(5 779)	(5 779)	-	(5 779)	-	(5 779)
Net value	(159)	(159)	-	(986)	827	(159)

31 CAPITAL MANAGEMENT

The board's policy is to maintain a strong capital base to maintain stakeholder confidence and to sustain future development of the business. The group considers its capital to comprise of total equity. The group may adjust its capital structure by way of issuing new shares and is dependent on its shareholder for additional capital, as required. The group manages its capital structure in light of changes in economic conditions and the board of directors monitors the capital adequacy, solvency and liquidity of the group on a continuous basis. Refer directors' report, pages 116 to 119 for more information.

The capital resources of the group has been depleted during the past years as a result of loss making contracts and inadequate orders to optimise the labour and capital intensive operations throughout the group. A turnaround strategy was developed during 2006 which was approved by the key stakeholders, including the Executive Authority and the Cabinet. This required the shareholder to inject R5.2bn for the successful implementation of the strategy.

Since the approval of the strategy, the group has been recapitalised by a total of R4.2bn. The shareholder has also provided a government guarantee totalling R1.85bn to enable the group to raise borrowings.

The group further strives to negotiate advance payments from clients in business transactions that require high investment in working capital over a long delivery lead times.

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

The company is not subject to externally imposed capital requirements. However, one of the company's subsidiaries, Densecure SOC Ltd, is a wholly owned captive insurer and therefore, has certain externally imposed capital requirements.

The minimum capital requirements applicable to Densecure SOC Ltd were maintained at all times during the year. In accordance with SA insurance legislation and regulations, the company is required to maintain a minimum Capital Adequacy Requirement (CAR) ratio of 1. This means the company is required to hold regulatory admissible net assets of greater than 1 to the solvency capital requirement, as at the reporting date, the company has a CAR ratio of 7.11 (2015/16: 6.6).

For detail on the quantitative data of what Denel manages as capital (total equity), please refer to the consolidated statements of changes in equity, page 122.

32 POST-RETIREMENT OBLIGATIONS

The group offers pension and post-retirement benefits through a defined contribution plan and a defined benefit plan.

32.1 DENEL MEDICAL BENEFIT TRUST

The group provides post-retirement medical aid contribution subsidies to qualifying retirees. The subsidies are funded by contributions made into a separate trustee administrated fund. Denel does not make annual contributions as the trust is fully funded. However, R26m (2015/16: R26m) was contributed during the year under review to reimburse the trust for the impact of early retirements.

The fund is valued annually by independent actuaries using the projected unit credit method. The result of the valuation carried out at 31 March 2017 indicated the trust is over-funded. There are currently no unrecognised actuarial losses, past services cost and contribution holidays due to the group. Therefore, there is no actuarial surplus recognised on the statement of financial position and no plan assets are recognised due to statutory requirements. The DMBT's expected long-term investment return was based on the yields of the R186 South African government bond plus a risk premium of 1.25% p.a.

The group has longevity and investment risk exposure as it is expected to fund actuarial losses that may arise and is exploring the possibility of limiting its exposure through a voluntary settlement process. For further detail refer to the directors' report, page 118.

The net asset cannot be recognised by Denel according to *IAS 19, Employee benefits* given that Denel cannot acces the assets from the Trust to derive economic benefit, as this belong to the beneficiaries of the DMBT.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	2016/17 R'000	2015/16 R'000
32 POST-RETIREMENT OBLIGATIONS (continued)		
32.1 DENEL MEDICAL BENEFIT TRUST (continued)		
The actuarially calculated liability compared to assets is as follows for the defined benefit plans:		
Change in defined benefit funded obligation		
Present value of funded obligations at 1 April	481	521
Service cost benefits earned during the year	1	3
Interest cost on projected benefit obligation	46	41
Remeasurement	3	(6)
Benefits paid	(28)	(26)
Liability buy-out	-	(52)
Present value of funded obligations at 31 March	**503**	**481**
Change in plan assets		
Fair value of plan assets at 1 April	1 288	1 314
Expected return on plan assets	125	104
Remeasurement	(50)	(53)
Benefits paid	(28)	(26)
Member voluntary payout exits from scheme	-	(51)
Fair value of plan assets at 31 March	**1 335**	**1 288**
Fund excess	832	807
Excess not recognised	(832)	(807)
Unrecognised actuarial gains	**-**	**-**
Net benefit expenses		
Service cost	1	3
Interest cost	46	41
Expected return on plan assets	125	104
Net actuarial loss recognised during the year	-	6
Income	**172**	**154**

	%	%
The principal actuarial assumptions used for accounting purposes were:		
Expected return on plan assets	9.5	9.9
Expected medical inflation	8.7	9.4

	Number	Number
The beneficiary members from the funds are as follows:		
Active members	72	82
Retired members	839	845

	2016/17		2015/16	
	Increase	Decrease	Increase	Decrease
	%	%	%	%
32 POST-RETIREMENT OBLIGATIONS (continued)				
32.1 DENEL MEDICAL BENEFIT TRUST (continued)				
A 1% change in assumed healthcare cost trend rates would have the following effects on the defined benefit obligation	11	9	11	9

	2016/17	2015/16	2014/15	2013/14	2012/13	2011/12
	Rm	Rm	Rm	Rm	Rm	Rm
Amounts for the current and previous five years are as follows:						
Defined benefit obligation	(503)	(481)	(611)	(759)	(755)	(674)
Plan assets	1 335	1 288	1 328	1 168	1 057	1 151
Surplus	832	807	717	409	302	477
Experience adjustments on plan liabilities	3	(5)	(35)	(25)	(25)	(4)

32.2 DENEL RETIREMENT FUND

The group has established a retirement fund scheme that covers all qualifying employees. This fund is a defined contribution plan and is governed by the Pension Funds Act no. 24 of 1956. The contributions are charged to the income statement as incurred.

33 SEGMENT REPORTING

Segment information is presented in respect of the group's operating segments. These operating segments are based on the group's management and reporting structure. Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

Unallocated items are shown as reconciling items between the segments and the consolidated information. Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one period.

Transfer price between operating segments is set at cost plus 10% of segment revenue, and segment results include transfers between operating segments and these transfers are eliminated on consolidation.

Business segments

The group comprises the following main operating segments:

- Aerostructures: Denel Aerostructures SOC Ltd;
- Aerospace Systems: Denel Dynamics, Denel Overberg Test Range and Denel Asia LLC;
- Aviation: Denel Aviation;
- Land Solutions: Denel Land Systems, Denel Vehicle Systems (Pty) Ltd and LMT Holdings SOC Ltd (RF);
- Munitions: Pretoria Metal Pressings; and
- Non-core, mainly consist of corporate office, treasury functions as well as property management and are not directly related to the business segments identified. This segment also includes segments that are not separated due to their immateriality, e.g. Densecure SOC Ltd.

The results of business entities with revenue less than 10% (2015/16: 10%) of the group revenue are aggregated within an operating segment which products and services closest relates to that of the specific business entity.

More detail on the business entities is stated in the operational overview section, pages 67 to 74.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	Aerostructures	Aerospace Systems	Aviation	Land Solutions	Munitions	Non-core	Consolidation entries	Total
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
33 SEGMENT REPORTING (continued)								
2016/17								
Segment revenue	553	1 863	1 092	3 998	582	411	(442)	8 057
Revenue from external customers	541	1 771	1 070	3 934	574	167		8 057
Inter-group revenue	12	92	22	64	8	244	(442)	-
Contribution	7%	22%	13%	49%	7%	2%		100%
Segment result	(7)	6	90	281	(44)	138	10	474
Net finance income/(costs)	10	(15)	11	22	(33)	(267)	-	(272)
Finance income	11	6	12	84	-	95	(128)	80
Finance cost	(1)	(21)	(1)	(62)	(33)	(362)	128	(352)
Share of results in associated companies							154	154
Income tax expense	-	-	-	(21)	-	(2)		(23)
Net profit/(loss) for the year	13	(24)	112	304	(110)	(398)	164	333
Segment assets	845	2 122	893	6 220	903	7 147	(5 703)	12 427
Deferred tax assets								36
Total assets								12 463
Segment liabilities	510	1 519	390	4 957	499	5 015	(3 079)	9 811
Deferred tax liabilities								1
Total liabilities								9 812
Cash flows from:								
Operating activities	7	(104)	122	569	70	(279)	(9)	376
Investing activities	(1)	(88)	(121)	(585)	(12)	413	487	93
Financing activities	(6)	182	(1)	(48)	(58)	(47)	(473)	(451)
Capital expenditure	8	22	10	23	-	7	(5)	65
Impairment losses raised/(reversed)	9	-	3	41	1	(90)		(36)
Depreciation/amortisation i.r.o. segment assets	24	36	14	39	18	22		153
Revenue from SA government	-	553	-	786	223	16		1 578
Significant non-cash items								
Fair value adjustment	-	-	-	-	-	48		48

33 SEGMENT REPORTING (continued)

	Aerostructures	Aerospace Systems	Aviation	Land Solutions	Munitions	Non-core	Consolidation entries	Total
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
2015/16								
Segment revenue	621	1 937	1 407	3 846	503	378	(464)	8 228
Revenue from external customers	596	1 824	1 388	3 809	460	151		8 228
Inter-group revenue	25	113	19	37	43	227	(464)	-
Contribution	7%	22%	17%	46%	6%	2%		100%
Segment result	7	134	89	256	(61)	223	(143)	505
Net finance income/(costs)	9	(20)	6	39	(9)	(228)	-	(203)
Finance income	10	6	8	71	-	69	(87)	77
Finance cost	(1)	(26)	(2)	(32)	(9)	(297)	87	(280)
Share of results in associated companies							132	132
Income tax expense	-	-	-	(38)	-	(1)		(39)
Net profit/(loss) for the year	16	114	95	257	(70)	(6)	(11)	395
Segment assets	852	2 496	931	4 340	1 044	7 369	(4 078)	12 954
Deferred tax assets								48
Total assets								13 002
Segment liabilities	520	1 890	530	3 787	563	5 103	(1 713)	10 680
Deferred tax liabilities								1
Total liabilities								10 681
Cash flows from:								
Operating activities	(13)	186	(2)	(57)	(331)	(82)	(402)	(701)
Investing activities	(4)	(46)	4	(557)	24	(1 501)	1 085	(995)
Financing activities	17	(130)	(2)	531	307	1 721	(885)	1 559
Capital expenditure	38	36	15	35	17	27	-	168
Impairment losses raised/(reversed)	5	149	2	46	-	(83)		119
Depreciation/amortisation i.r.o. segment assets	18	44	14	37	12	22		147
Revenue from SA government	33	55	1 021	965	63	24		2 161
Significant non-cash items								
Fair value adjustment	-	-	-	-	-	162		162

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	2016/17				2015/16			
	Share capital issued [1]	Share investment by Denel SOC Ltd [1]	Amounts owing to/(by) Denel SOC Ltd [1]	Effective percentage shareholding	Share capital issued [1]	Share investment by Denel SOC Ltd [1]	Amounts owing to/(by) Denel SOC Ltd [1]	Effective percentage shareholding
	Rm	Rm	Rm	%	Rm	Rm	Rm	%
34 SUBSIDIARIES AND ASSOCIATED COMPANIES								
The following unlisted companies are subsidiaries of Denel SOC Ltd and its subsidiaries:								
Denel Aerostructures SOC Ltd	1 689	1 689	(148)	100	1 689	1 689	191	100
Densecure SOC Ltd	8	8	-	100	8	8	-	100
LMT Holdings SOC Ltd (RF) [2]	27	16	(265)	51	27	16	-	51
Denel Vehicle Systems (Pty) Ltd	25	828	268	100	25	828	-	100
Aggregated amounts less than R0.5m [1 and 3]	-	-	-		-	-	-	
Total investment		2 541	145			1 713	191	
Less: Accumulated impairment of investment (refer note 11)		(1 055)	(336)			(1 055)	(336)	
Net investment of Denel SOC Ltd (refer note 11)		1 486	(191)			1 486	(145)	
Subsidiary shareholding by LMT Holdings SOC Ltd (RF), a subsidiary of Denel SOC Ltd [4]								
LMT Products SOC Ltd	-	-	-	51	-	-	-	51
LMT Engineering SOC Ltd	-	7	-	51	-	7	-	51
LMT Properties SOC Ltd	-	-	-	51	-	-	-	51
Net investment of LMT Holdings SOC Ltd (RF)		7	-			7	-	

The country of incorporation of subsidiaries are not different from Denel, except for Denel Asia LLC which is a Hong Kong based company.

Non-controlling interest voting rights are not different from % shareholding.

1. *Amounts smaller than R0.5m due to rounding are not reflected against the units but in aggregate on this page.*
2. *This includes R16m (2015/16: R16m) preference shares.*
3. *The invesment made in Denel Asia LLC, was less than R0.5m (refer note 11).*
4. *Shares are not held by the group but effective management control is exercised in these entities.*

	2016/17				2015/16			
	Share capital issued [1]	Share investment by Denel SOC Ltd [1]	Amounts owing to/(by) Denel SOC Ltd [1]	Effective percentage shareholding	Share capital issued [1]	Share investment by Denel SOC Ltd [1]	Amounts owing to/(by) Denel SOC Ltd [1]	Effective percentage shareholding
	Rm	Rm	Rm	%	Rm	Rm	Rm	%
34 SUBSIDIARIES AND ASSOCIATED COMPANIES (continued)								
The following unlisted companies are associated companies of Denel SOC Ltd and its subsidiaries:								
Turbomeca Africa (Pty) Ltd	-	49	-	49	-	49	-	49
Airbus DS Optronics (Pty) Ltd [2]	-	57	-	30	-	57	-	30
Rheinmetal Denel Munition (Pty) Ltd	-	371	-	49	-	371	-	49
Tawazun Dynamics LLC	-	23	-	49	-	23	-	49
Net investment of Denel SOC Ltd (refer note 12.2)		**500**	**-**			**500**	**-**	
Associated company shareholding by Denel Vehicle Systems (Pty) Ltd, a subsidiary of Denel SOC Ltd:								
Pioneer Land Systems LLC [3]	-	-	-	49		-	-	49
Net investment of Denel Vehicle Systems (Pty) Ltd		**-**	**-**			-	-	

	2016/17	2015/16
	Rm	Rm
Aggregated net profit of subsidiaries	74	47

The country of incorporation of associated companies are not different from Denel, except for Tawazun Dynamics LLC and Pioneer Land Systems LLC which are both UAE based companies.

All associated companies are strategic to the business activities of Denel.

1. *Amounts smaller than R0.5m due to rounding are not reflected against the units but in aggregate on this page.*
2. *70% shareholding by Airbus DS Optronics GmbH was sold to Hensoldt Sensors GmbH on 28 February 2017. Airbus DS Optronics (Pty) Ltd's name was subsequently change (after 31 March 2017) to Hensoldt Optronics (Pty) Ltd. This has not altered the shareholding of Denel.*
3. *Equity partnership was established between International Golden Group PJSC and Denel Vehicle Systems (Pty) Ltd. The agreement was entered into on 5 February 2014. Apart from the issuing of 100 non-dividible non-negotiable shares @ UAE$3 000 per share in 2014, no other transactions to date took place. International Golden Group PJSC holds 51% in Pioneer Land Systems LLC whilst Denel Vehicle Systems (Pty) Ltd holds 49% of the shares issued.*

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2017

	GROUP		COMPANY	
	2016/17	2015/16	2016/17	2015/16
	Rm	Rm	Rm	Rm
35 IRREGULAR EXPENDITURE				
Balance at 1 April	49	-	47	-
Add: Irregular expenditure incurred in the prior year identified in the current year	7	5	-	5
Deviations from the procurement process not adequately approved [1]	2	-	-	
Tax clearance certificates not obtained [2]	5	5	-	5
Add: Irregular expenditure incurred in current year	139	44	35	42
Suppliers not registered on the central supplier database [3]	8	-	2	-
Evaluation criteria not adequately specified [4]	4	-	2	
Tax clearance certificates not obtained [5]	5	2	-	2
Bids not adequately approved [6]	8	-	-	-
Deviations from the procurement process not adequately approved [7]	106	42	25	40
Contract extension not adequately approved [8]	7	-	7	-
Less : Amounts condoned [9]	(79)	-	(39)	-
Less : Amounts recoverable (not condoned)				
Less: Amounts not recoverable (not condoned)	-	-	-	-
Irregular expenditure awaiting condonation	116	49	43	47

Details of irregular expenditure:

1. *Seven (7) cases [no cases relating to Denel SOC Ltd] instances have been incurred where expenditure has been incurred on bids in which deviations were undertaken from the procurement process which were not adequately approved in terms of the supply chain management policy. Based on investigations undertaken by management it was noted that although the deviations from the procurement process were reasonable as these were due to instances of suppliers which are sole suppliers or due to the initial design of the products incorporating certain products which cannot be substituted at a later stage, the deviation from a transparent procurement process was not adequately documented and approved as is required in terms of National Treasury Regulations and the supply chain management policy which have resulted in irregular expenditure.*
2. *Fourteen (14) cases [no cases relating to Denel SOC Ltd] instances have been incurred in which bids were issued to suppliers without the entity adequately evaluating valid tax clearance certificates as is required in the group supply chain policy and the Preferential Procurement Regulations.*
3. *Fifty three (53) cases [two cases (2) relating to Denel SOC Ltd] instances have been incurred where expenditure has been incurred on bids with suppliers which were not registered on the central supplier database as is required in terms of National Treasury SCM Instruction 4A of 2016/17.*
4. *Six cases (6) [four (4) cases relating to Denel SOC Ltd] cases instances have been incurred in which the evaluation criteria in the bids were not adequately specified in line with the requirements of the Preferential Procurement Regulations.*
5. *Fifty one (51) cases [no cases relating to Denel SOC Ltd] instances have been incurred in which bids were issued to suppliers without the entity adequately evaluating valid tax clearance certificates as is required in the group supply chain policy and the Preferential Procurement Regulations.*
6. *One hundred and twenty eight (128) cases [no cases relating to Denel SOC Ltd] instances have been incurred where expenditure has been incurred on bids which were not adequately approved in terms of the delegation.*
7. *Eighty nine (89) cases [thirty two (32) cases relating to Denel SOC Ltd] instances have been incurred where expenditure has been incurred on bids in which deviations were undertaken from the procurement process which were not adequately approved in terms of the supply chain management policy. Based on investigations undertaken by management it was noted that although the deviations from the procurement process were reasonable as these were due to instances of suppliers which are sole suppliers or due to the initial design of the products incorporating certain products which cannot be substituted at a later stage, the deviation from a transparent procurement process was not adequately documented and approved as is required in terms of National Treasury Regulations and the supply chain management policy which have resulted in irregular expenditure.*
8. *One (1) case [one (1) case relating to Denel SOC Ltd] instances has been incurred where expenditure has been incurred on a contract which was extended without following an adequate procurement process or obtaining adequate authorisation as is required in terms of the delegation of authority.*
9. *Sixty two (62) cases [thirty nine (39) cases relating to Denel SOC Ltd] instances have been condoned by the Group Supply Chain Executive who has been delegated the authority to condone the cases.*

35 IRREGULAR EXPENDITURE (continued)

Denel acquired all the shares in BAE Systems Land Systems South Africa (Pty) Ltd on 29 April 2015, resulting in Denel Vehicle Systems (Pty) Ltd being a Schedule 2 entity in terms of the PFMA Act from the date of acquisition. As a Schedule 2 entity, Denel Vehicle Systems (Pty) Ltd was required to comply with the requirements of both the PFMA and PPPFA Acts, as well as the National Treasury Regulations in relation to procurement and contract management from 29 April 2015 onwards. Management of Denel have applied to the Minister of Finance to exempt Denel Vehicle Systems (Pty) Ltd from the requirements of the legislation and regulations relating to procurement and contract management for a period to enable the management of the entity to develop internal control systems to ensure compliance with all the relevant requirements. As at the reporting date of the consolidated annual financial statements, engagements with the Minister of Finance were still on going.

Due to the entity becoming a Schedule 2 entity and not being previously required to comply with requirements of the legislation and regulations relating to procurement and contract management, management has embarked on a process to align the businesses operations and control environment to ensure compliance, although this could not be achieved in a manner which ensured that irregular expenditure was not incurred by the entity. Management have also set up controls to identify irregular expenditure incurred to ensure prioritisation of the most significant risk areas first. In the current year of the total irregular expenditure incurred by the group, R83m related to Denel Vehicle Systems (Pty) Ltd.

Possible irregular expenditure

This relates to expenditure under investigation regarding the confirmation of the tax compliance status for foreign suppliers – the PPPFA regulations require that tenders may only be awarded to a person whose tax matters have been declared to be in order by SARS. SARS is only able to provide a taxpayer with confirmation of the taxpayer's tax compliance status as compliant if the taxpayer is registered for tax in SA. Altogether 17 bids (six for Denel SOC Ltd) awarded to foreign suppliers, amounting to R22m (R2m for Denel SOC Ltd) have been identified where SARS is not in a position to confirm the foreign suppliers' tax compliance status. Clarity is being sought on the reporting of these contracts.

It should be noted that these bids relate to suppliers which are original equipment manufacturers which are utilised in the service or repair of aircrafts or which have previously been designed into products manufactured by Denel.

	Greater than 12 months Rm	Less than 12 months Rm	Total Rm
Ageing of 2016/17 irregular expenditure not condoned:			
Deviations from the procurement process not adequately approved	-	93	93
Tax clearance certificates not obtained	5	5	10
Evaluation criteria not adequately specified	-	4	4
Suppliers not registered on the central supplier database	-	8	8
	5	111	116

Disciplinary steps taken/criminal proceedings

Internal disciplinary hearings have been held for 144 case instances of irregular expenditure incurred and no instances of criminal proceedings have been instituted.


A7
A5
DENEL

PART 7

INFORMATION SERVICE

GRI CONTENT INDEX

We have provided some GRI disclosures in the 2016/17 integrated report. The disclosures provided are set out in the table below, with a reference to where in the document the information may be found.

REFERENCE	DESCRIPTION	INTEGRATED REPORT REFERENCE/COMMENT	PAGE
STRATEGY AND ANALYSIS			
G4-1	Statement from the most senior decision-makers of the organisation about the relevance of sustainability to the organisation and the organisation's strategy for addressing sustainability.	Group chief executive officer's report	62 to 65
G4-2	Description of key impacts, risks, and opportunities, including rights as defined by national laws and relevant internationally recognized standards.	Risk management	56 to 59
ORGANISATIONAL PROFILE			
G4-3	Report the name of the organisational.	About this report	Inside cover
G4-4	Report the primary brands, products, and services.	What we do	08
G4-5	Report the location of the organisation's headquarters.	Corporate contact details	212
G4-6	Report the number of countries where the organisation operates, and names of countries where either the organisation has significant operations or that are specifically relevant to the sustainability topics covered in the report.	Organisational structure	09
G4-7	Report the nature of ownership and legal form	Organisational structure	09
G4-9	Report the scale of the organisation (including total number of employees, operations, net sales).	Performance indicators Organisational structure Human capital	07 09 24 to 40
G4-10	Report the total number of employees by employment contract and gender and the total number of permanent employees by employment type and gender.	Human capital	24 to 40
G4-11	Report the percentage of total employees covered by collective bargaining agreements.	Human capital	24 to 40
G4-12	Describe the organisation's supply chain.	Supply chain	40
G4-13	Report any significant changes during the reporting period regarding the organisation's size, structure, ownership, or its supply chain including expansions.	Not applicable	
G4-14	Report whether and how the precautionary approach or principle is addressed by the organisation.	We do not currently apply the precautionary approach	
IDENTIFIED MATERIAL ASPECTS AND BOUNDARIES			
G4-17	List all entities included in the organisation's consolidated financial statements.	Organisational structure Note 34 of the consolidated annual financial statements	09 200 to 201
G4-18	Explain the process for defining the report content and the Aspect Boundaries and how the organisation has implemented the Reporting Principles for Defining Report Content.	About this report	Inside cover
G4-20	For each material Aspect, report the Aspect Boundary within the organisation.	Material issues	54 to 55
G4-21	For each material Aspect, report the Aspect Boundary outside the organisation.	Material issues	54 to 55
G4-22	Report the effect of any restatements of information provided in previous reports, and the reasons for such restatements.	Not applicable	
G4-23	Report significant changes from previous reporting periods in the Scope and Aspect Boundaries.	Not applicable	

REFERENCE	DESCRIPTION	INTEGRATED REPORT REFERENCE/COMMENT	PAGE
STAKEHOLDER ENGAGEMENTS			
G4-24	Provide a list of stakeholder groups engaged by the organisation	Stakeholder engagements	20 to 23
G4-25	Report the basis for identification and selection of stakeholders with whom to engage.	Stakeholder engagements	20 to 23
G4-26	Report the organisation's approach to stakeholder engagement, including frequency of engagement by type and by stakeholder group, and an indication of whether any of the engagement was undertaken specifically as part of the report preparation process.	Stakeholder engagements	20 to 23
G4-27	Report key topics and concerns that have been raised through stakeholder engagement, and how the organisation has responded to those key topics and concerns, including through its reporting. Report the stakeholder groups that raised each of the key topics and concerns.	Stakeholder engagements	20 to 23
REPORT PROFILE			
G4-28	Reporting period for information provided.	About this report	Inside cover
G4-29	Date of most recent previous report.	31 March 2016	
G4-30	Reporting cycle.	We report annually	
G4-31	Provide the contact point for questions regarding the report or its contents.	Corporate contacts details	212
G4-32	Report the 'in accordance' option the organisation has chosen, the GRI Content Index for the chosen option and the reference to the External Assurance Report, if the report has been externally assured.	Not applicable. This report contains some GRI disclosure.	
G4-33	Report the organisation's policy and current practice with regard to seeking external assurance for the report, report the scope and basis of any external assurance provided, the relationship between the organisation and the assurance providers and whether the highest governance body or senior executives are involved in seeking assurance for the organisation's sustainability report.	About this report Report of the Audit and Risk committee	Inside cover 108 to 109
GOVERNANCE			
G4-34	Report the governance structure of the organisation, including committees of the highest governance body. Identify any committees responsible for decision-making on economic, environmental and social impacts.	Corporate governance	84 to 102
G4-35	Report the process for delegating authority for economic, environmental and social topics from the highest governance body to senior executives and other employees.	Corporate governance	84 to 102
G4-36	Report whether the organisation has appointed an executive-level position or positions with responsibility for economic, environmental and social topics, and whether post holders report directly to the highest governance body.	Corporate governance	84 to 102

REFERENCE	DESCRIPTION	INTEGRATED REPORT REFERENCE/COMMENT	PAGE
G4-37	Report processes for consultation between stakeholders and the highest governance body on economic, environmental and social topics. If consultation is delegated, describe to whom and any feedback processes to the highest governance body.	Corporate governance Stakeholder engagement	84 to 102 20 tot 23
G4-38	Report the composition of the highest governance body and its committees including executive and non-executive directors, independence, tenure, number of each individual's other significant positions and commitments, the nature of the commitments and gender.	Corporate governance	84 to 102
G4-39	Report whether the Chair of the highest governance body is also an executive officer (and, if so, his or her function within the organisation's management and the reasons for this arrangement).	The Chairman is a non-executive director. Denel board of directors	85
G4-40	Report the nomination and selection processes for the highest governance body and its committees, and the criteria used for nominating and selecting highest governance body members (including diversity, independence, expertise and experience relating to economic, environmental and social topics)	Corporate governance	84 to 102
G4-41	Report processes for the highest governance body to ensure that conflicts of interest are avoided and managed and whether conflicts of interest are disclosed to stakeholders (including cross board membership and related party disclosure)	Corporate governance Note 29 of the consolidated annual financial statements	84 to 102 172 to 175
G4-42	Report the highest governance body's and senior executives' roles in the development, approval, and updating of the organisation's purpose, value or mission statements, strategies, policies, and goals related to economic, environmental and social impacts.	Corporate governance	84 to 102
G4-43	Report the measures taken to develop and enhance the highest governance body's collective knowledge of economic, environmental and social topics.	Corporate governance	84 to 102
G4-44	Report the processes for evaluation of the highest governance body's performance with respect to governance of economic, environmental and social topics and whether such evaluation is independent or not, and its frequency. Report whether such evaluation is a self-assessment	Corporate governance	84 to 102
G4-45	Report the highest governance body's role in the identification and management of economic, environmental and social impacts, risks, and opportunities. Include the highest governance body's role in the implementation of due diligence processes	Corporate governance	84 to 102
G4-46	Report the highest governance body's role in reviewing the effectiveness of the organisation's risk management processes for economic, environmental and social topics.	Risk management Corporate governance	56 to 59 84 to 120
G4-47	Report the frequency of the highest governance body's review of economic, environmental and social impacts, risks, and opportunities.	Risk management Corporate governance	56 to 59 84 to 120

REFERENCE	DESCRIPTION	INTEGRATED REPORT REFERENCE/COMMENT	PAGE
G4-48	Report the highest committee or position that formally reviews and approves the organisation's sustainability report and ensures that all material Aspects are covered.	The Audit and Risk committee is responsible to ensure the integrity of the information presented. Corporate governance, Audit and Risk committee Report of the Audit and Risk committee	 91 108 to 109
G4-49	Report the process for communicating critical concerns to the highest governance body.	Risk management	56 to 59
G4-50	Report the nature and total number of critical concerns that were communicated to the highest governance body and the mechanism(s) used to address and resolve them.	Risk management	56 to 59
G4-51	Report the remuneration policies for the highest governance body and senior executives (including performance pay, equity based pay, bonuses, deferred or vested shares, sign on bonuses, termination payments and clawbacks)	Remuneration report	103 to 105
G4-52	Report the process for determining remuneration.	Remuneration report	103 to 105
	ETHICS AND INTEGRITY		
G4-56	Describe the organisation's values, principles, standards and norms of behaviour such as codes of conduct and codes of ethics	Vision and values Corporate governance	06 84 to 102
G4-57	Report the internal and external mechanisms for seeking advice on ethical and lawful behaviour, and matters related to organisational integrity, such as helplines or advice lines	Corporate governance	84 to 102
G4-58	Report the internal and external mechanisms for reporting concerns about unethical or unlawful behaviour, and matters related to organisational integrity, such as escalation through line management, whistleblowing mechanisms or hotlines.	Corporate governance	84 to 102

GLOSSARY

ACRONYM	FULL DESCRIPTION
(Pty) Ltd	(Proprietary) Limited
A&R committee	Audit and Risk committee
AAD 2016	Africa Aerospace and Defence Exhibition 2016
ACI	African, Coloured and Indian
ACSA	Airports Company South Africa
AGM	Annual general meeting
Airbus	Airbus DS Optronics (Pty) Ltd
AISI	Aerospace Industry Support Initiative
AMD	South African Aerospace, Maritime and Defence Industries Association
AMO	Aircraft Maintenance Organisation
APC	Armoured personnel carriers
ARMSCOR	Armaments Corporation of South Africa
AS	Aerospace Standard
ATWG	Anti-tank guided weapon
B-BBEE	Broad-based black economic empowerment
BI	Black Industrialist
Board	Denel board of directors
BRICS	Brazil, Russia, India, China and South Africa
BVR	Beyond visual range
C4ISR	Command, Control, Communications, Computers, Intelligence, Surveillance and Reconnaissance
CAE	Chier audit executive
CAR	Capital Adequacy Requirement
CCM	Continuous control monitoring
CEO	Chief executive officer
CFC	Controlled foreign currency
CFO	Chief financial officer
CGVR	Central guide vertical restraint
CHF	Swiss Franc
CIL	Centre of Innovation and Learning
Companies Act	South African Companies Act, no. 71 of 2008
COSO	Committee of Sponsoring Organisations of the Treadway Commission
C-RAM	Counter-rocket, artillery and mortar system
CSI	Corporate social investment
CSIR	Council for Scientific and Industrial Research
CVO	Contract variation order
DAe	Denel Aerostructures SOC Ltd
DAv	Denel Aviation
DCAC	Directorate of Conventional Arms Control
DD	Denel Dynamics
Dekra	German Motor Vehicle Inspections Association
Denel Asia	Denel Asia LLC
Denel ISM	Denel Integrated Systems and Maritime
Denel OTR	Denel Overberg Test Range
Denel S3	Denel Sovereign Security Solutions
Deniprop	Denel Industrial Properties
DenRet	Denel retirement fund
DIRCO	Department of International Relations and Cooperation

ACRONYM	FULL DESCRIPTION
DLS	Denel Land Systems
DMBT	Denel Medical Benefit Trust
DMG	Denel machine gun
DMTN	Domestic Medium Term Note
DoD	Department of Defence
DoD&MV	Department of Defence and Military Veterans
DPE	Department of Public Enterprises
DPS	Damage per second
DRC	Democratic Republic of the Congo
DTA	Denel Technical Academy
DTC3	Denel Technical Cyber Command Centre
dti	Department of Trade and Industry
DVS	Denel Vehicle Systems (Pty) Ltd
EASA	European Aviation Safety Agency
EBIT	Earnings before interest and taxation
EC	Eurocopter
ED	Enterprise development
EE	Employment equity
Entity/(ies)	Denel's operating divisions or subsidiary
ERW	Explosive remnants of war
ESD	Enterprise supplier development
EUR	Euro
EXCO	Group executive committee of Denel
FIFO	First-in-first-out
G5	A towed howitzer of 155 mm calibre
G6	A 155mm self-propelled howitzer
GBADS	Ground-based air defence system
GBP	British Pound Sterling
GCEO	Group chief executive officer
GCFO	Group chief financial officer
GDP	Gross domestic product
GHG	Greenhouse gas
government	South African government, unless otherwise stated
GRI	Global Reporting Initiative
ha	hectare
Hensoldt	Hensoldt Optronics (Pty) Ltd, previously known as Airbus DS Optronics (Pty) Ltd (Airbus)
HR	Human resources
HVAC	heating, ventilation and air-conditioning
IAS	International accounting standards
IBSA	India, Brazil and South Africa
ICT	Information communication technology
ICV	Infantary combat vehicle
IDEX2017	UAE International Defence Exhibition 2017
IED	Improvised explosive device
IESBA	International Ethics Standards Board for Accountants
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standards

ACRONYM	FULL DESCRIPTION
IGG	International Golden Group (GG) PJSC
IIR	Imaging Infrared
IIRC Framework	International Integrated Reporting Council Framework
IP	Intellectual property
IPAP	Industrial Policy Action Plan
IR Framework	Integrated Reporting Framework
IRBA	Independent Regulatory Board for Auditors
ISA	International Standards on Auditing
ISO	International Standards Organisation
IT	Information technology
JARIC	Joint Air Reconnaissance Intelligence
JSE	Johannesburg stock exchange
KG	Kilogram
King III	King Code of Governance Principles and the King Report on Governance in South Africa 2009
King IV	King Code of Governance Principles and the King Report on Governance in South Africa 2016
KL	Kilolitre
kWh	Kilowatt-hour
L	litres
LCT	Light combat turren
LED	Light Emitting Diode
LEO	Law enforcement officers
LLC	LLC Limited liability company
LMT	LMT Holdings SOC Ltd (RF)
m3	cubic metre
MEDDS	Mechem explosives and drug detection system
MMP	Mobile Mortar Platform
MoD	Ministry of Defence
MOI	Memorandum of Incorporation
MPV	Mine-protected vehicles
MRAP	Mine-resistant ambush protected
MRO	Maintenance, repair and overhaul
NCPF	National Cybersecurity Policy Framework
NEMA	National Electrical Manufacturers Association
NIMR	NIMR Automotive LLC
NT	National Treasury
OCI	Other comprehensive income
OEM	Original equipment manufacturer
OHS	Occupational health and safety
OHSAS	Occupational Health Safety Assessment Series
PAA	Public Audit Act, no. 25 of 2004
PAW	Personal Assault Weapon
PFMA	Public Finance Management Act, no. 1 of 1999
PLCM	Product lifecycle management
PLS	Pioneer Land Systems LLC
PMP	Pretoria Metal Pressings
PPPFA	Preferenctial Procurement Policy Framework Act
PR&T	Personnel, remuneration and transformation
PWD	People with disability
R&D	Research and development
R/Rand/ZAR	South African Rand
RAF	Road Accident Fund

ACRONYM	FULL DESCRIPTION
RDM	Rheinmetall Denel Munition (Pty) Ltd
RF	Ring-fenced
RG-vehicle	Family of mine-resistant 4x4 light armoured vehicles
Rm	South African Rand million
RSA	Republic of South Africa
RSS	Ribs, spars and sword
RTD	Retired
S&E committee	Social and Ethics committee
SA	South Africa(n)
SA government	South African Government
SAAF	South African Air Force
SABS	South African Bureau of Standards
SACAA	South African Civil Aviation Authority
SANAS	South African National Accreditation System
SANDF	South African National Defence Force
SANParks	South African National Parks
SANSA	South African National Space Agency
SAPS	South African Police Services
SARA	Small African Regional Aircraft
SARS	South African Revenue Services
SCM	Supply chain management
SDROW	Self-defence remotely-operated weapon
SEAFAR	Deep sea monitoring system
SED	Socio-economic development
SETA	Sector Education and Training Authority
SGD	Singapore Dollar
Shareholder	South African government
SHE	Safety, health and environment
SHEQ	Safety, health, environment and quality
SMME	Small, medium and micro enterprise
SOC	State-owned company
SOE	State-owned entity
SOP	Schools Outreach Programme
SS77	762x51mm machine gun
STEM	Science, Technology, Engineering and Mathematics
t	tons
TD	Tawazun Dynamics LLC
TGP	Total guaranteed package
TMA	Turbomeca Africa (Pty) Ltd
TS	Top shells
UAE	United Arab Emirates
UAV	Unmanned aerial vehicle
UAVS	Unmanned aerial vehicle systems
UN	United Nations
URS	User requirement specification
US	United States
USA	United States of America
USD	United States Dollar
VAT	Value added tax
WFF	Wing-to-fuselage fairing

CORPORATE CONTACT DETAILS

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Registration number 1992/001337/30

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