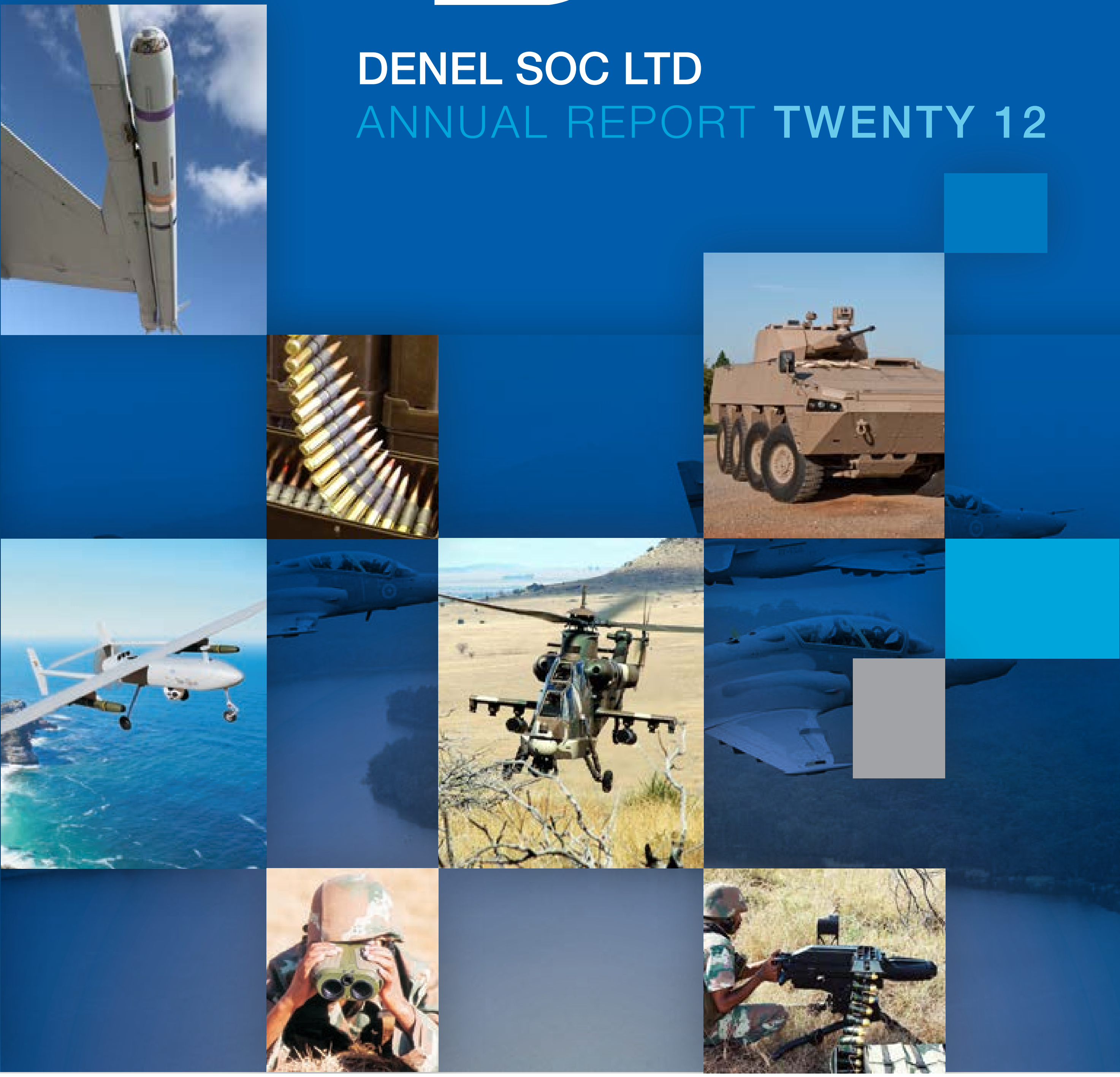
DENEL SOC LTD

ANNUAL REPORT TWENTY 12



A RELIABLE DEFENCE, SECURITY AND TECHNOLOGY SOLUTIONS PARTNER

About this report

This annual report presents Denel's financial, economic, operating, social and sustainability performance for the year ended 31 March 2012. It aims to provide a transparent, comprehensive and comparable view of the group's turnaround, operational and financial performance and outlook to a broad range of stakeholders. This report further aims to highlight significant opportunities, challenges faced by the group and planned actions to address issues. The planned actions take into account business priorities, risks and recommendations made by stakeholders.

This annual report takes cognisance of the integrated reporting requirements of the King III report on Corporate Governance, as is expected of a responsible organisation committed to good governance and accountability. The sustainability and governance section is based on the requirements of one of the globally recognised best reporting practices' framework, the Global Reporting Initiative (GRI). The annual report is available on Denel's website (www.denel.co.za)

To further enhance readability, a list of abbreviations and acronyms is provided on pages 202 to 204. In line with Denel's inclusive approach, corporate contact details are provided on the inside back cover.

CONTENT

GROUP **OVERVIEW**

NATURE OF BUSINESS

The Government of South Africa (Government) is the sole shareholder of Denel and the company reports to the Minister of Public Enterprises. The Minister appoints an independent board of directors to provide strategic direction and oversight to the Denel group. The executive management team is responsible for the day-to-day management of the company.

Denel provides turn-key solutions of defence equipment to its clients by designing, developing, integrating and supporting artillery, munitions, missiles, aircraft sub-assembly manufacturing, aircraft maintenance, unmanned aerial vehicle systems (UAVS) and optical payloads based on high-end technology. It further provides product and logistical support, including testing and qualification, maintenance, upgrades and decommissioning, as and when required. Denel's products and solutions are designed and developed to meet unique end-user requirements of its clients including full lifecycle support, thereby reducing the cost of ownership. Programmes that are being executed include landward systems projects, missiles, command and control, avionics upgrades, development and design of aerostructures components, as well as demining operations. In addition to specific development and production capabilities, Denel is a prime contractor in a number of the South African National Defence Force (SANDF) programmes, which positions Denel as a specialist contractor to global defence suppliers.

Denel plays a significant role in industrial development via key conventional technologies, diverse quality products and operational capacity through its active research and development programmes, product development, manufacturing and maintenance activities, well-defined infrastructure and strong human capital base. As such, investment in research and development (R&D) has a special economic significance in extending Denel's global footprint, apart from its conventional association with scientific and technological development. The research, design, development, integration, qualification, certification and industrialisation are done primarily in-house with selected specialised items outsourced to strategic partner companies. Significant elements of production are outsourced to the broader South Africa (SA) manufacturing industry whilst some of the Denel businesses are vertically integrated with production commencing from raw materials through to final products. Denel also supports the local commercial market by supplying non-defence products. Further details of Denel's activities, products and services are provided in the business unit overview section on pages 30 to 41. It is a fact that by leveraging the defence technology base, innovative applications have been found to increase rail safety, crime protection, surveillance, protection of assets, mine safety management, as well as in the manufacturing of mining drill bits, commercial brass strips, amongst others.

Denel delivers technologically advanced and efficient products to the global market, together with a wide range of sophisticated services and solutions to its customers. Denel is also contributing to creating safer environments with products that have been tailor-made for clients, including SANDF, the United Nations (UN), other international agencies, governments and commercial customers globally.

Denel's mandate includes contributing to national priorities as set out in the New Growth Path (NGP) and Industrial Policy Action Plan (IPAP2), particularly regarding skills and supplier development, maintaining advanced manufacturing and aerospace capabilities, optimising existing technology and exploring diversification to increase revenue and job creation. Global studies in the industry indicate that this sector has a multiplier effect of no less than four. This means that for every job in Denel there are at least four downstream jobs created in the economy. The Denel group including the associates' employs 6 787 direct personnel with circa 30 000 indirect jobs maintained and/or supported in the economy. Denel is actively involved in artisan training, internships, apprenticeships and maths and science student support. Denel provides military independence and security of supply, advanced manufacturing, technology development and R&D to the country.

Denel's future activities will be significantly influenced by the outcomes of the Defence Review undertaken during the year. The Defence Review will also inform policy and strategy of companies in the industry. The review was completed and a first draft report issued during April 2012. The report discusses a number of issues, and recommendations that could contribute to creating a vibrant defence industry. The Defence Review process will play a significant role in growing the industry.

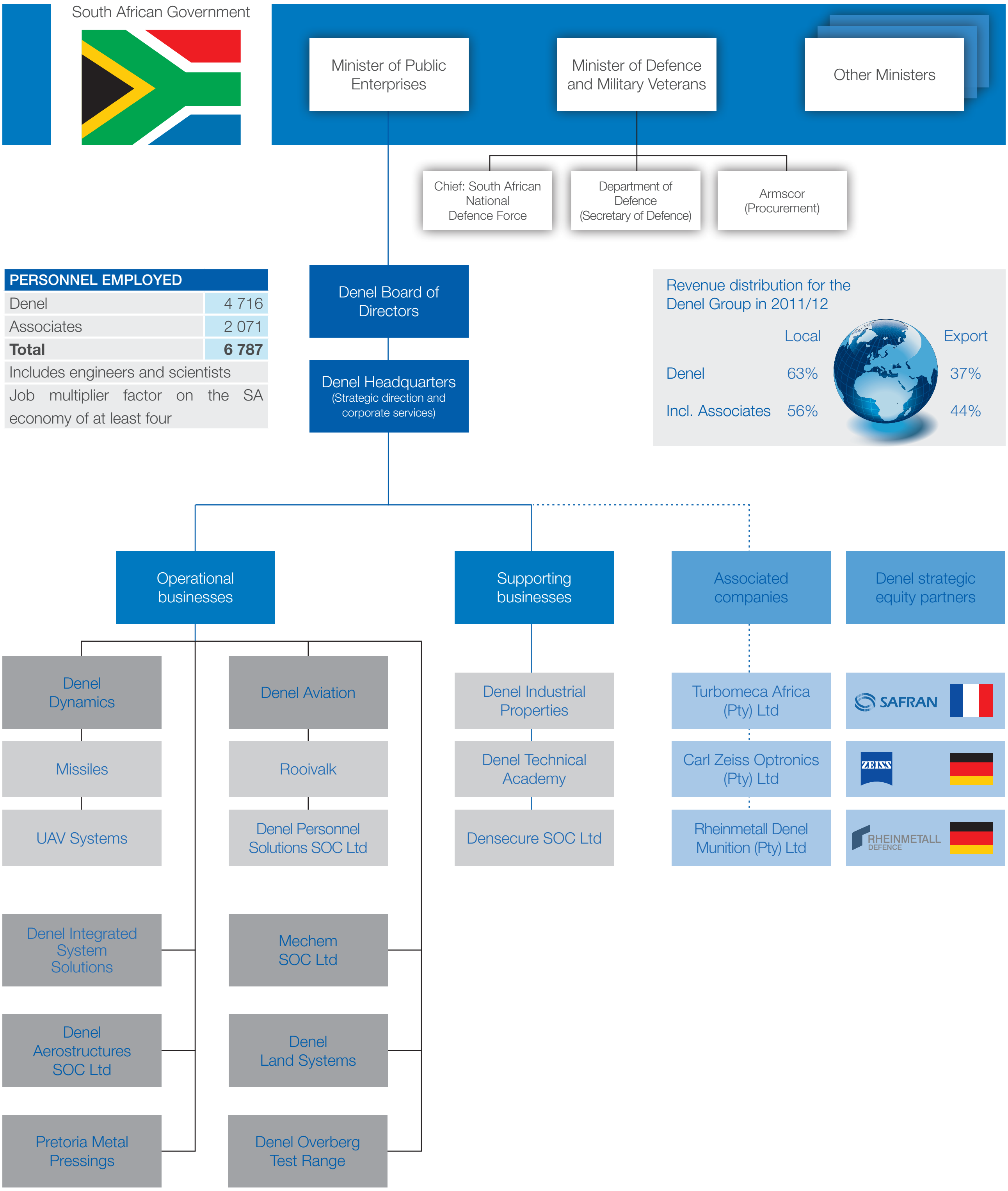
Denel is a group of companies and its organisational structure is provided on page 06, reflecting its business units, associates and reporting hierarchy.

STRATEGIC OBJECTIVES, VISION AND VALUES

Denel's primary objective is to be a supplier of defence, security and related technology solutions in a financially sustainable manner, whilst simultaneously fulfilling the objective of being a responsible South African corporate citizen.

STRATEGIC OBJECTIVES, VISION AND VALUES	
VISION	WHAT DENEL STANDS FOR
The credible state-owned South African strategic partner for innovative, security and related technology solutions.	Denel is committed to operational excellence, openness and integrity as it engages with its customers and stakeholders. Denel believes in its people who are skilled innovators and who take responsibility for their actions. We also acknowledge that we have a broader responsibility in terms of communities, countries and the environment in which we operate.
PURPOSE	VALUES
Denel's purpose is to:	
• Supply South Africa's (SA) defence and security environment with strategic technology capability, products, services and support.	**Performance** We embrace operational excellence.
• Leverage indigenous capability to access selected export markets.	
• Contribute to socioeconomic imperatives of government such as:	**Integrity** We are honest, truthful and ethical.
- Job creation, skills development and social investment.	
- Enhancing the local technology and manufacturing base.	**Innovation** We create sustainable, innovative solutions.
- Supplier development.	
- Exploiting commercial use of technology.	**Caring** We care for people, customers, communities and the environment.
- Foreign policy and regional security objectives.	
• Be a responsible corporate citizen to ensure: - Good governance. - Transformation and employee well-being.	**Accountability** We take responsibility for our actions.
DENEL STRATEGIC FOCUS AREAS	
• Growing revenue and improve customer relationships.	
• Improving productivity, efficiency and profitability.	
• Creating a vibrant organisation through human resource development and transformation.	
• Improving capabilities to deliver systems and solutions through innovation.	

ORGANISATIONAL STRUCTURE



PERSONNEL EMPLOYED	
Denel	4 716
Associates	2 071
Total	**6 787**
Includes engineers and scientists	
Job multiplier factor on the SA economy of at least four	

Revenue distribution for the Denel Group in 2011/12

	Local	Export
Denel	63%	37%
Incl. Associates	56%	44%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HISTORICAL OVERVIEW

1938
Denel's roots are established

The South African Royal Mint is converted to an ammunition factory. This is the start of the Pretoria Metal Pressings (PMP) division.

1948
South African DoD establishes a defence advisory committee

The South African Department of Defence (DoD) establishes an advisory committee on the equipment requirements for the Union Defence Force.

1949-1951
DoD establishes a defence production office and resources board

DoD establishes a defence production office and resources board to support its defence production and resource requirements.

1961-1977
DoD establishes a munitions production board

There is a substantial effort in SA to set-up an indigenous state-owned and private defence industry. A munitions production board is established in terms of Act no. 37 of 1964, reporting to the Minister of Defence.

1968
Armscor is established

Armscor Act no. 57 of 1968 establishes Armscor to act as the manufacturer and procurement agency of defence equipment for the DoD.

1977-1990
SA becomes a defence technology leader

SA becomes a defence technology leader in many areas.

1990-1992
Decision to separate Armscor's procurement and manufacturing

The position of Armscor as the manufacturer and procurement agency is reconsidered, with a decision to separate production and procurement functions.

1992
Denel is incorporated in terms of the Companies Act

Denel is established to be responsible for all previous Armscor production facilities. The company is incorporated in terms of the Companies Act.

The manufacturing business units within Armscor are transferred to Denel:

- Denel Aviation (DAv) (previously Atlas Aircraft Corporation, which included at its inception gearbox and engine activities, now assigned to the associated company, Turbomeca Africa (Pty) Ltd (TMA), as well as aerostructures manufacturing assigned to Denel Aerostructures (DAe)
- Denel Dynamics (previously Kentron, later Denel Aerospace Systems (DAS)), with ground-based air defence activities initially included and now split off into Denel Integrated Systems Solutions (DISS)
- Denel Land Systems (DLS) (previously Lyttelton Engineering Works, which separated into Lyttelton Ingenierswerke (LIW) and Vektor for some time before amalgamating again)
- PMP (a division of Denel)
- Mechem (incorporated into Denel)
- Overberg Test Range (OTR) (previously known as OTB), a test range facility established in the early 1980s. With the termination of the then space programme OTR was transferred to Denel)

There is a significant reduction in personnel, from 25 000 employees to 14 000 within the consolidated Denel manufacturing units.
Details of other units that were transferred from Armscor and subsequently transferred into standalone units, outside of the Denel group, or closed, are not provided.

Centralisation of core activities

2001-2004

A strategy of centralising core activities is pursued to improve financial performance. Denel experiences a loss of critical markets, encounters increased financial losses and solvency problems.

A turnaround strategy aimed at bringing Denel to profitability is launched. It includes rightsizing and managed decentralisation to improve financial performance and accountability. Selected equity partnerships are entered into with the aim of accessing funding, best practice business processes, new technology and securing new markets. Non-core, loss-making assets and businesses are disposed of. Rheinmetall Denel Munition (RDM) becomes an associate (previously comprising the individual Swartklip, Somchem, Wellington and Naschem facilities). Carl Zeiss Optronics (Pty) Ltd (CZO) became an associate in 2008.

2005-2009

Implementation of turnaround strategy, restructuring and decentralisation

Certain facilities are closed. The 1998 White Paper on Defence is promulgated with the aim of directing the restructuring and equipping of the SANDF. In this era, approximately 70% of SA's defence acquisitions are imported. Loss-making contracts are entered into just to maintain capacity, resulting in legacy obligations that continue to impact Denel's performance. R&D spend is reduced. There are unsuccessful attempts to enter commercial markets with nonmilitary products.

1992-2000

Unsuccessful attempts to counter difficult trading conditions

Ongoing drive to improve operations

2010-2012

Losses are substantially reduced and new strategies are implemented to continue the turnaround of the group. These initiatives include strategies focused on significantly improving revenue, optimising efficiency and costs, as well as leadership and transformation. Greater emphasis is placed on improving business development and ensuring better conversion of opportunities to sales. Denel secures orders in excess of R5bn to supply defence systems to various countries over a five to seven year period. The SA government (shareholder) strongly demonstrates its support for Denel, including its marketing efforts and in accessing funding.

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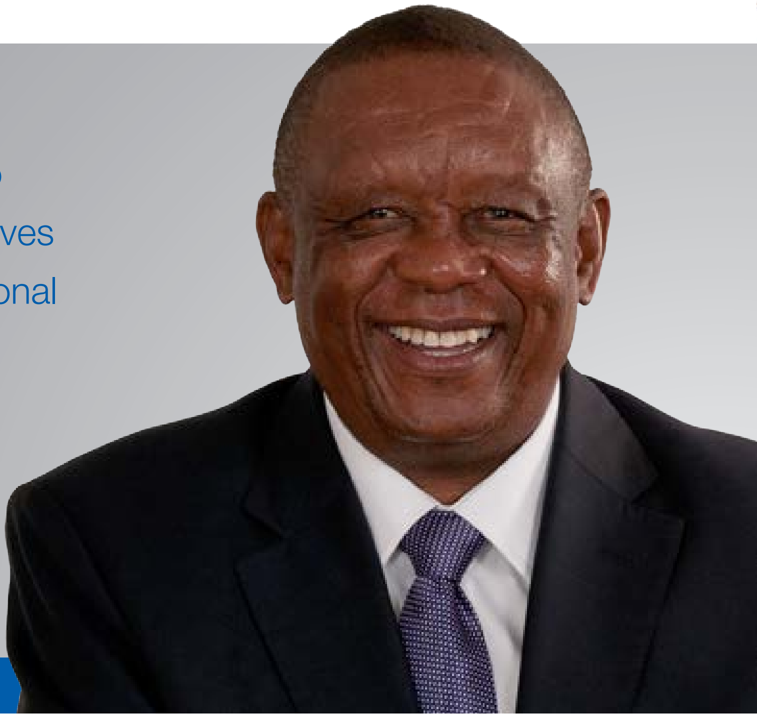
DIRECTORS' AND **EXECUTIVE REPORTS**

CHAIRMAN'S REPORT

The improvement in financial results is also attributable to the implementation of initiatives enhancing internal efficiencies and operational performance. We will continue to entrench operational excellence in the execution of key programmes and contracts as this is a critical intervention to ensure improved performance.

Zoli N R Kunene



INTRODUCTION

I am pleased to present my first annual report as chairman of the board. I am grateful for the confidence placed in me, entrusted to chair and work with the board, to provide oversight and strategic direction to a complex company like Denel.

This annual report provides a broad overview to Denel stakeholders of what we do, how Denel has performed against targets, key achievements for the year, sustainable development, governance and the detailed annual financial statements.

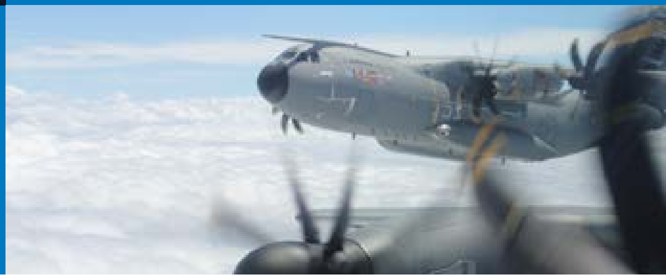
The release of this annual report coincides with the completion of the draft Defence Review report which articulates the role, composition and structure of defence in our democracy, and importantly, describes the strategic role of Denel as a national asset in providing sovereign and strategic capabilities to the SANDF.

FINANCIAL PERFORMANCE REVIEW

Considering that Denel has been operating under difficult conditions, both locally and internationally, it is pleasing that Denel has posted a marginal profit of R41m. Denel continues to successfully manage operations, despite limited cashflows. As opposed to the prior year's financial results, which were positive primarily due to once-off accounting gains, the current year results are based on improved operational performance. This financial year's improvement is also attributable to better financial performance by the aerostructures business, which in the past contributed significantly to losses posted by the group.

Whilst welcoming the financial improvements, the balance sheet remains highly geared. Notwithstanding this, we have managed to maintain debt levels at R1,85bn and reduced annual interest charges to less than R100m. Government, as the shareholder, has continued to support Denel in addressing the renewal of the government guarantees backing the debt. As a result, the notes underlying the debt have been rolled over as they fell due. We view this as a demonstration of confidence, the shareholder and the participating investors have in Denel. In addition, there are ongoing constructive engagements with investors and financial institutions, regarding the future bank facility requirements.

The sustainable turnaround of Denel is integrally linked to securing new revenue streams, accessing bank facilities to be able to execute new orders and ensuring improvements in operations. Together with the shareholder, we are exploring sustainable funding mechanisms to strengthen the company's balance sheet.



We are pleased that R700m was allocated to Denel during the 2012 National Budget Speech by the Minister of Finance, to support the aerostructures business. We view this recapitalisation as a reinforcement of the government's commitment to developing a viable and sustainable aerostructures business. This cash injection will enable DAe to fund its working capital requirements, as it is preparing for the serial manufacturing phase of its major programmes. The allocation has not been included in these financial results as funds will only be disbursed during the 2012/13 financial year.

OPERATIONAL REVIEW

The improvement in financial results is also attributable to the implementation of initiatives enhancing internal efficiencies and operational performance. We will continue to entrench operational excellence in the execution of key programmes and contracts as this is a critical intervention to ensure improved performance.

The new corporate business plan is focused on achieving a positive bottom line, improved operational performance and financial sustainability. We, however, recognise the constraints caused by the current national defence spending level.

Therefore, a key element of the strategy going forward is to ensure a more export driven revenue stream, and this vision is supported by the strong order opportunity pipeline. Denel has already secured some key export orders. We believe that these orders will contribute to creating a more dynamic business model, in terms of technology development, skills development and long term sustainability.

We are expecting in the short to medium term to conclude orders in respect of key local programmes, some of which will contribute to maintaining certain strategic capabilities for the future, as well as greater investment in R&D.

Denel executes a number of defence programmes with varying levels of complexity, with stringent performance targets, milestone targets and technical requirements. This requires ongoing performance evaluation, taking into account the understanding of the user requirements. The nature of these evaluations require a strong customer focus and sound stakeholder relationships. I am confident that Denel is making strides towards establishing a dynamic relationship with its customer environment, so as to better deliver on its contractual obligations, which in the past has led to underperformance and financial losses.

In order to realise the opportunity pipeline that Denel has identified locally and internationally, a special effort is being made to enhance the marketing, business development and sales function so as to ensure the conversion of opportunities into firm contracts. In addition, the company is concurrently instituting cost optimisation measures, operational efficiencies, addressing duplication on the business support side and instilling a culture of excellence.

CONTRIBUTION TO DEVELOPMENT IMPERATIVES

Denel has continued to fulfil its primary mandate of being a custodian of key strategic defence capabilities whilst contributing to national developmental priorities as set out in the NGP and IPAP2. These national priorities include skills development, enterprise development and maintaining advanced manufacturing and aerospace capabilities. Denel is actively involved in artisan training, internships, apprenticeships and maths and science student support, which are key to building human capital. Denel's contribution to the country includes military independence and security of supply, advanced manufacturing, technology development, R&D and earning foreign currency.

Denel recognises that there are key areas requiring specific attention, namely, employment equity, skills development and preferential procurement. The board has committed itself to ensuring that these issues are addressed from the highest level in order to ensure that progress is achieved. In addition, we operate in an industry that has a job multiplier effect of no less than four. This means that for every job in Denel there are at least four downstream jobs created in the economy. The Denel group including the associates employs 6 787 direct personnel with circa 30 000 indirect jobs maintained and/or supported in the SA economy. In addition, Denel will engage with the Ministry of DoD&MV to discuss how we can utilise the capabilities and training facilities in Denel to improve the quality of life of our military veterans.

The details of Denel's contribution to socioeconomic priorities are provided in the *economic impact section* page 56.

GOVERNANCE

During the 2011/12 financial year, the shareholder reconstituted and broadened the board to align the company to statutory requirements and to continue adhering to good governance. I take this opportunity to welcome the new members of the board, Mr Mavuso Msimang, Prof Stella Nkomo, Mr Bafana Ngwenya, Mr Ghandi Badela, Ms Ziphozethu Mathenjwa, Mr Nkopane Motseki, Adv Melissa Ntshikila, Mr Matodzi Ratshimbilani and Ms Sonja Sebotsa. I wish them well as they discharge their responsibilities as members of the board. I wish to express my sincere gratitude to the outgoing board members, namely Dr Sibusiso Sibisi (previous chairman), Ms Seadimo Chaba, Mr Llewellyn Jones and Mr Alan Hirsch, for their dedication and significant contribution to the turnaround of the group.

Please join me in welcoming the new group chief executive officer (GCEO), Mr Riaz Saloojee, who was appointed following the resignation of Mr Talib Sadik. Mr Saloojee comes with a strong background in the defence environment and has an established record as a leader in the defence industry. We have given Mr Saloojee a broad mandate to address significant challenges confronting the group, by the same token have every confidence that he will execute the task at hand.

APPRECIATION

I thank the Minister of Public Enterprises, Mr Malusi Gigaba, his previous Deputy Minister, Mr Dikobe Martins, Director-General, Mr Tshediso Matona and the Department of Public Enterprises (DPE) officials for their commitment and support to Denel during the current financial year.

I wish to recognise the previous Minister of DoD&MV, Ms Lindiwe Sisulu, Deputy Minister, Mr Thabang Makwetla, the Secretary of Defence, Dr Sam Gulube and officials of the DoD&MV, the SANDF and Armscor for their continued support, guidance and commitment to Denel throughout the year. I welcome the new Minister of DoD&MV, Ms Nosiviwe Mapisa-Nqakula and the Deputy Minister of DPE, Mr Bulelani Magwanishe, and assure them of our support and commitment.

I wish to acknowledge the support received from the National Treasury (NT) during the year. I thank the chairman of the Portfolio Committees on Public Enterprises, Mr Peter Maluleka, the chairman of the select committee on Labour and Public Enterprises, Ms Priscilla Themba, as well as the chairman of the Defence Portfolio Committee, Mr Malusi Motimele.

I extend my heartfelt thanks to my fellow board members for robust engagements and for their sacrifice as they availed themselves to address various matters during the financial year under review.

Denel's executive management team is congratulated on the progress made during the year under review. The executives in the business units and all employees, similarly, deserve a huge 'thank you' for their efforts, loyalty and commitment. The board acknowledges that the success of any business is built on the hard work, creativity and commitment of its employees.

CONCLUSION

Acknowledging that there are huge challenges that we need to collectively resolve, I am confident that with the measures being implemented, a clear strategic vision, underpinned by sound leadership, we will turnaround the company thus securing a sustainable future for the benefit of our country and its people.

Zoli N R Kunene
Chairman

GROUP CHIEF EXECUTIVE OFFICER'S REPORT

The company's strategy is premised on achieving, in a three-year period, significant increase in revenue, optimised cost and efficiency, strong balance sheet, modernised technology and transformation.

Riaz Saloojee

INTRODUCTION

As part of familiarising myself with the organisation during the last three months of the financial year, I have been engaging with key clients, potential clients, financial institutions, employees, the shareholder community, as well as visiting our key operations. In these engagements we discussed material issues that Denel must address going forward. All stakeholders expressed strong support for a successful Denel. I am particularly impressed as Denel appears to occupy a key position in both the defence environment and the SA economy. This confirms that Denel is a strategic national asset. I will continue to engage the stakeholders of Denel, especially in looking at ways in which we can build a stronger organisation.

I have been reviewing the overall financial performance of the organisation. The group's financial performance has been improving, but there are real challenges that must be addressed as we go forward. The current state of the world economy, which is largely subdued and not favouring business, is not helping.

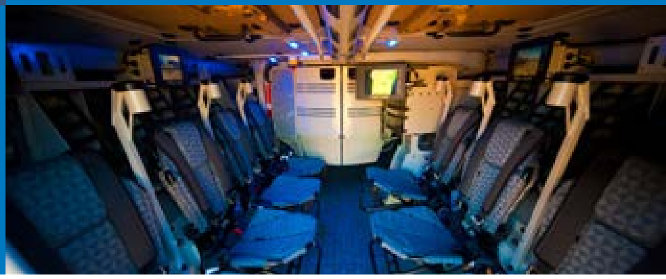
FINANCIAL REVIEW

A close study of the group's financial performance reveals a year-on-year improvement, which is commendable. The group has achieved 10% improvement at revenue level and this modest achievement is attributable to more maintenance, repair and overhaul (MRO) services, aerostructures and landmine clearance work undertaken during the year. The revenue improvement at an overall level has come largely from outside of SA. Considering the current defence spend in the country, this improvement is in line with our strategy to grow our presence in foreign markets. We see future growth opportunities largely in landward and missile systems.

The company's cash utilisation is linked to how the organisation is managing its balance sheet in areas such as timing of debtor collection, spend on items already provided for, prepayments made or received and funding business costs. Our objectives are to turn the organisation around in terms of profitability and generate positive operating cash flows. Denel's operations require high investment in working capital and therefore, we continue to implement stringent cash flow management processes. We are also challenging and improving the related internal control measures on an on-going basis.

We held road shows with key financial institutions that focused on strengthening relationships, a better understanding of Denel's business requirements and how these important partners could improve their support to Denel, as it accesses new markets over the next five years.





OPERATIONAL REVIEW

Denel has delivered on a number of projects as listed under the *key achievements* detailed on page 26. As part of tightening operations, we have held a number of urgent engagements with the local client during January to March, taking the form of workshops focused on fast-tracking specific orders and/or resolving specific project issues. In particular, the orders that needed to be finalised that could have negatively impacted our year-end financial performance. I have no doubt that both organisations will benefit by ensuring the continuation of standing joint forums involving the GCEO, executives and programme managers. We have addressed the issues that were confronting us at the time, but due to the complexity of the projects, ensuring that all issues are resolved, will remain a challenge. For example, one such issue is minimising, for the benefit of both the client and Denel, the extent to which committed funds to Denel projects are rolled-over back to the fiscus. We will focus our energies on finding solutions starting by addressing the "hockey-stick" effect that impacts the extent of roll-over of funds and by establishing a better mechanism to communicate technical issues on projects.

I am proud of the achievements made to date on a number of projects. Whilst these have been outlined on page 26, I would like to highlight a few of these:

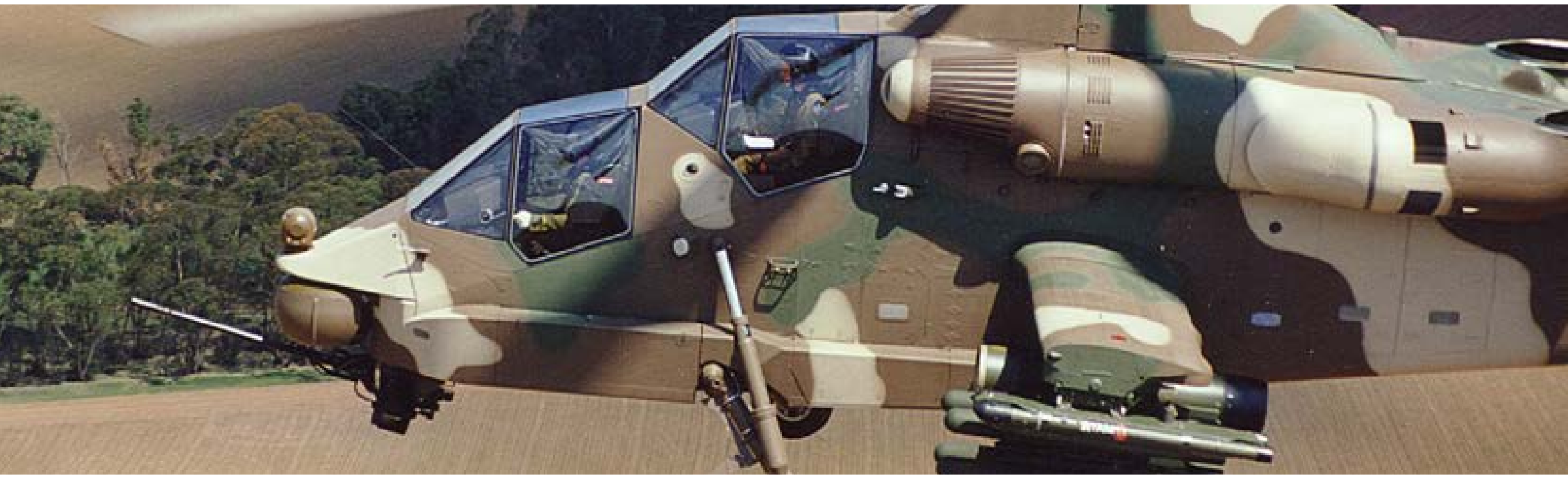
- DLS successfully completed certain milestones of the development phase of the Hoefyster project, which in our view initiate negotiations for the placement of the production order. Despite a delay in awarding the Hoefyster production contract, Denel is looking forward to being involved in the production phase of this programme.
- DAv has delivered eight certified Rooivalk combat support helicopters to the South African Air Force (SAAF); the remaining three will be delivered during the second quarter of 2012/13. The Rooivalk is the first combat support helicopter to be designed, built, qualified and certified on the African continent. This bears testimony to the kind of capability and skills this country has.
- The development of A-Darter, a highly sophisticated missile, which is a collaboration programme between the governments of SA and Brazil, is substantially on track. The flight clearance and integration programmes for carrying and firing the A-Darter from the Gripen fighter have been successfully completed. The success of this joint development with Brazil provides evidence of the benefits of multinational collaboration.

Comprehensive details of significant contracts are provided in the directors' report.

Denel spends a significant amount on R&D, but the concern is the extent of the self-funded portion in comparison to industry bench-marks, as it is fairly low. Despite the group's current financial performance and the overall financial position, I am pleased that we are investing in R&D. For example, the development of the Seeker 400, a UAV that is an improvement from the existing portfolio of UAVS and can stay airborne for up to 16 hours gathering relevant surveillance data against various threats, is encouraging. Investing in R&D is critical to ensuring that we stay ahead of the game, and remain competitive and relevant. It is our strategic focus going forward to modernise technology and continue to improve our capabilities through innovation. The details on R&D are provided on pages 56 to 57.

STRATEGY

The group is faced with a challenge regarding generating positive cash flows in the short- to medium-term. In addition, the group continues to have high debt of approximately R1,85bn before taking into account other short-term liabilities arising from prepayments received. I am satisfied that there are adequate risk mitigations as there is a strong business case covering the next five years showing strong growth prospects and increasing profitability on a sustainable basis. Denel has not in the past been so close to turning around, bearing in mind that it has been loss making for over ten years. We are exploring a number of funding



mechanisms with both financial institutions and the shareholder. Indications are that in future, there will be a hybrid funding model in place for Denel comprising a combination of recapitalisation, loans and government guarantees aimed at strengthening the balance sheet.

The strategy review session held during March 2012 focused on key issues impacting the operating environment, identifying the focus areas and canvassing ideas to fast track the attainment of our strategic objectives. We emerged with a strategic intent to make Denel a dynamic, vibrant, financially sustainable, and profitable organisation, which has empowered its employees with regard to skills development, technology innovation, people retention and reflects the transformation imperatives of government. This forms the foundation from which we will build a long-term sustainable company. The strategic intent is underpinned by Denel's revised vision, mission and values.

The company's strategy is premised on achieving, in a three-year period, significant increase in revenue, optimised cost and efficiency, strong balance sheet, transformed workforce as well as modernised technology. Therefore, our strategy, amongst others is aimed at addressing financial performance challenges based on a two-pronged approach focusing on improving business development and reducing business costs. We shall on the one hand, focus on implementing strategies aimed at ensuring quicker conversion of the opportunity pipeline to orders. Considering the level of defence spend in SA, specific attention will be given to securing export orders. On the other hand, we shall develop and implement measures aimed at optimising and reducing business costs. The latter will comprise a combination of continuous improvement in terms of efficiencies and taking out some of the costs. We see this as the way to ensure that we stay competitive and in business.

The strategy of all defence companies operating in SA will no doubt be influenced by the implementation of the recommendations of the Defence Review. We see the following areas as likely to have a significant impact on Denel, the intent to:

- Maintain and further develop the SA defence industry as a key national asset encompassing state organs utilising the industry's capabilities.
- Develop a healthy partnership between the SANDF and its supporting industry, with the local industry in principle enjoying preference.
- Have strong government support for export sales, technology transfers and joint ventures, provided such transactions do not compromise national security.
- Enhance acquisition policy focussed on timely and efficient equipment acquisition in order to sustain and further develop the defence industry. These will include developing long-term acquisition plans to avoid boom and bust problems.

I am confident that Denel has been refocused on the right strategic course aimed at ensuring a sustainable turnaround of the group.

PEOPLE MANAGEMENT

Market conditions require that defence contractors be both agile and efficient, with human capital development being a critical success factor. We are focussed on the implementation of skills attraction, development and retention strategy in order to ensure that current and future human resources needs are met. Denel has achieved a level 3 B-BBEE rating in the 2011/12 financial year. We have been partnering with the UNISA School of Business Leadership for over two years on a leadership development programme. The leadership development programme is informed by the organisational leadership needs identified by the Denel leadership framework. Denel is also committed to

creating an environment conducive to all employees realising their full potential. A process has been implemented to continue improving the organisational climate.

Denel has continued to transform the organisation by focussing on B-BBEE. Meeting employment equity and enterprise development targets has remained a challenge due to a number of reasons, including the skills set requirements and the fact that Denel is not growing. Regardless of the historic reasons, employment equity and effective succession planning will be our focus going forward. I am pleased that Denel continues to contribute to the requirements of the NGP in terms of skills development and is delivering on its commitments regarding artisan training and development.

SUSTAINABLE DEVELOPMENT

Denel is committed to sustainable development and ensuring a sustainable future. The group also subscribes to the principles of the UN Global Compact. Denel recognises that sustainability is dependent on making positive contributions to its economic, social and natural environments. Specific measures have been implemented to ensure the responsible use of scarce natural resources and caring for the environment. Denel believes that there is always room for improvement, and is steadily integrating all material sustainability concerns into its governance practices.

The aspects of sustainable development, including corporate strategy, effective risk management, human resources and transformation, occupational health and safety, targeted socioeconomic development (SED), governance and environmental management are provided in the *sustainability and governance section* on pages 54 to 99.

APPRECIATION

I would like to extend my appreciation to the executive team and all Denel employees for their contribution during my short period at the helm of the company. I wish to express my sincere gratitude for the support I received from my executives, my predecessor Mr Talib Sadik, board members, the Minister, the previous Deputy Minister and the Director General of the DPE. I extend my appreciation to the previous Minister of DoD&MV, Deputy Minister, Secretary of Defence, SANDF, Armscor, organised labour and industry partners for their support and contribution. We welcome the new Minister of DoD&MV and the Deputy Minister of DPE, they can be assured of our support and commitment.

The real value of the company is to be found in its human capital. I would, therefore like to call on all Denel employees to continue living the values of integrity, performance, caring, accountability and innovation, as well as making 2012/13 a year in which the group focuses on operational excellence, improved cash management and sustainable financial turnaround.

Riaz Saloojee
Group chief executive officer

BUSINESS **REVIEW**

FINANCIAL HIGHLIGHTS

Despite the economic crunch and fragile world economy, Denel managed to achieve positive results albeit marginal. Key contributors to this performance are the reduced losses, specifically in the aerostructures business, and improved revenues.

Various aspects of business which include governance that support financial performance are detailed elsewhere in this report, in line with the requirements of integrated reporting.


Fikile Mhlontlo

Revenue
R3 568m
improved 10%

Cash utilised
(before prepayments)
R297m

Share of earnings from associates
R33m declined 59%

Net profit
(before interest, tax, non-recurring items and DAe)
R99m

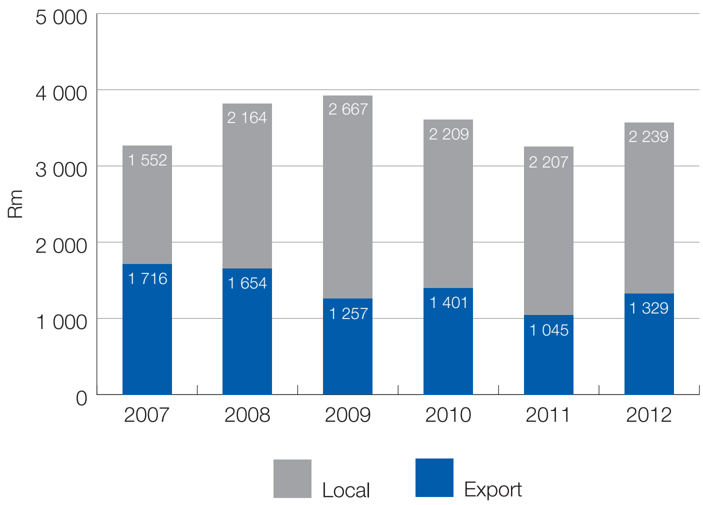
Significant R&D spend
R752m

Equity position
R695m
improved 6%

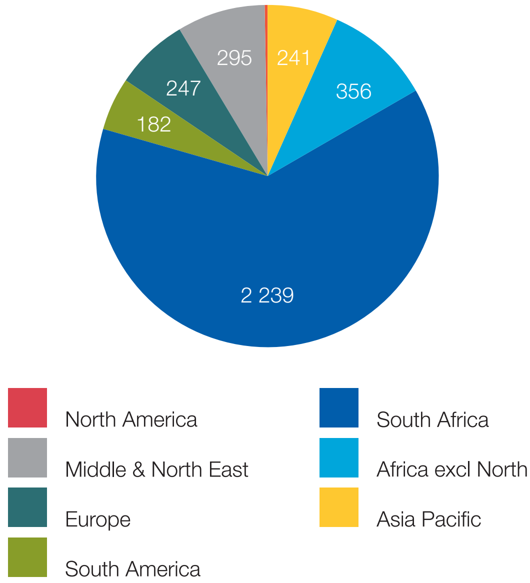
Net loss posted by DAe R78m reduces 67%

Key areas	2012 Rm	2011 Rm	Variance Rm	
Income statement				
Turnover	3 568	3 252	316	↑
Gross profit	862	503	359	↑
Non-recurring items	(141)	(357)	216	↑
Net loss before once-off items	(100)	(246)	146	↑
Net profit for the year	41	111	(70)	↓
Balance sheet				
Equity	695	654	41	↑
Cash and short-term deposits	1 074	920	154	↑
Interest-bearing borrowings	1 966	1 946	20	↑
Ratios	%	%	%	
Gross margin	24	15	9	↑
Exports as a % of turnover	37	32	5	↑

REVENUE

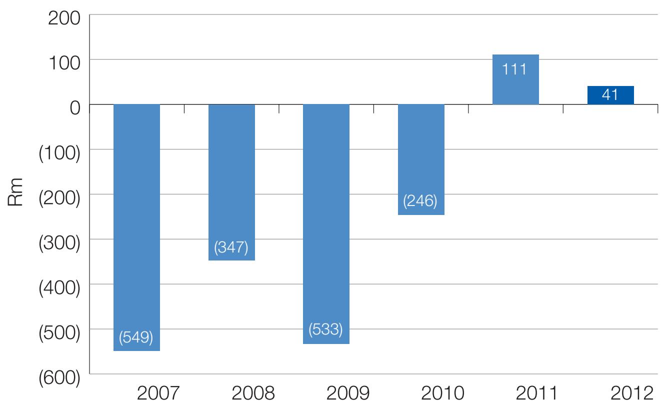


REVENUE BY REGION (Rm)



Revenue has improved by 10% from the prior year to R3 568m, mainly due to increased activities in MRO of aircraft, aerostructures and demining. The current year revenue improved compared to the prior year due to an increase in export revenue.

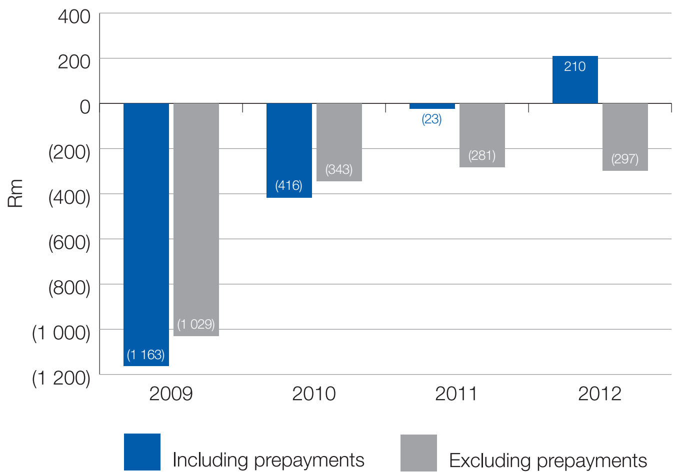
NET PROFIT/(LOSS)



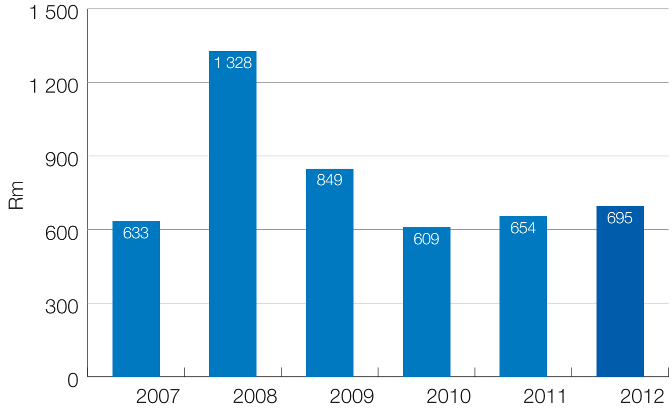
Denel posted R41m (2010/11: R111m) profit, which is lower than the prior year's results. This year's financial results should be understood within the context that last year's results included a number of once-off items, among others an accounting gain of R463m arising from the restructuring of one of the pension funds. This year's financial results are largely attributable to a lower loss posted by the aerostructures business, and more aviation and demining activities undertaken. In analysing these results it should be noted that there are some once-off items without which a normalised loss of R100m (2010/11: R246m) would have been posted. More detail is provided in the *directors' report* on page 114. The group's results continue to be influenced by the financial losses that are posted by DAe R78m (2010/11: R237m) and interest on external borrowings of R84m (2010/11: R120m).

Denel R&D spend:
For the current year totalled R752m (2010/11: R789m) with self-funded R178m (2010/11: R127m) and client-funded R574m (2010/11: R662m), an investment of immeasurable value to the country.

NET CASH FLOWS

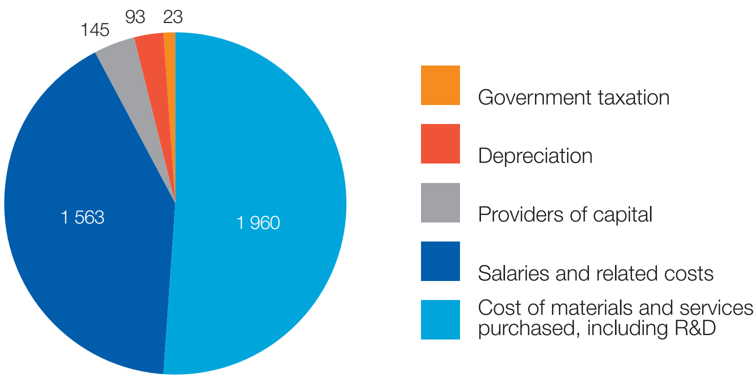


EQUITY



Whilst the group generated positive cash inflows, if prepayments are excluded the group shows negative cash inflows. This indicates that there will need to be more focus on positive cash generation going forward. The net equity increased to R695m (2010/11: R654m), due to positive financial results. The equity position is projected to increase in excess of R1bn following the allocation of R700m to Denel to support its aerostructures business, announced by the Minister of Finance during the 2012 National Budget Speech.

ECONOMIC VALUE DISTRIBUTION (Rm)



The group continues to contribute positively to the economic environment. Details are provided in the economic impact section of the *sustainability and governance section* on pages 56 to 57.

PERFORMANCE AGAINST THE SHAREHOLDER'S COMPACT

Denel agrees its key performance areas with the shareholder's representative, the Minister of Public Enterprises, on an annual basis. The group's strategy is implemented and progress against the contracted targets is continuously monitored by the board. This is reported to the shareholder's representative on a quarterly basis.

The actual performance achieved by the group for the year under review, compared to the contracted targets, is provided in the table below:

Strategic intent	Key performance area	Key performance indicator	Achieved	Contracted
Strategic role in the provision of defence capabilities	Retention of capabilities in areas required by the DoD&MV	Retained strategic capabilities in support of the DoD&MV's requirements	100% of the core capabilities required by DoD&MV were retained	Maintain all or 100% of key strategic capabilities required of Denel by DoD&MV
	Maximise access to local markets	Local sales as a % of turnover	63%	60%
	Contracted SANDF/ DoD&MV programmes	Invoiced sales as a % of SANDF/DoD&MV orders placed (roll-over of funds)	84%	85%
Strategic economic role in promoting advanced manufacturing	Promote advanced manufacturing goals of the country	The value of the development type work as a % of turnover (client-funded)	16%	10%
	Investment in R&D	Self-funded R&D as a % of turnover	5%	0.5%
Business sustainability	Profitability management	Earnings before interest and tax (EBIT) as a % of turnover	4%	(0.5%)
	Debt and gearing	Debt/equity ratio	2.8:1	2.8:1
	Cash management	Cash flow from operations as a % of turnover	10%	(7%)
	Healthy sales pipeline	Orders concluded in respect of the coming year as a % of sales budget for that year (order cover)	53%	55%
Business efficiency	Productivity improvement	Turnover per employee	R757k	R938k
	Operating expenditure (OPEX)	OPEX as a % of revenue	27%	23%
Developmental contribution	Contribution to economic transformation (including attainment of key supplier development)	B-BBEE contributor level	Level 3	Level 4

KEY ACHIEVEMENTS

Received a letter of offer and acceptance for the production of turret systems for ± R3,5bn. The signing ceremony is scheduled for later in the 2012/13 financial year.

Received a contract for the production of missiles for R1,2bn for a period of five years. Execution of the contract is progressing according to plan.

Following from five fully certified Rooivalk helicopters delivered last year, three additional helicopters were delivered to SAAF. The remaining three will be delivered during the 2012/13 financial year.

A-Darter 5th generation short-range air-to-air missile development, collaboration between Brazil and South Africa, had a successful series of guided launches in January 2012. The programme of this highly sophisticated missile entered its qualification phase, to be completed during 2012/13.

Successfully resolved technical issues and completed phase one of the Ground-based Air Defence System (GBADS), culminating in delivery of the system during March 2012.

Successfully completed the enhancement of Umkhonto missile for delivery to the client.

Recapitalisation of Denel for R700m to support the aerostructures business was announced by the shareholder.

Contracts relating to Airbus work packages were renegotiated specifically on issues of price, penalties and guarantees. The agreed terms will be formalised during the 2012/13 financial year.

A project entailing the recommissioning to operational service of 12 Cheetah fighter aircraft completed and delivered to the client.

Seeker 400 nearing completion and will make its maiden flight during the 3rd quarter of 2012. This UAV has been designed to stay airborne for 16 hours whilst simultaneously operating two payloads. It is suitable for surveillances against various threats.

The group is addressing transformation and has maintained its level 3 B-BBEE rating.

The ammunition and explosives division has maintained its record of two million accident-free hours, putting it amongst the top safest companies involved in dangerous goods to work for.

Secured a vehicle manufacturing capability through acquiring a majority stake in LMT Holdings (Pty) Ltd, enabling Denel to produce a local version of a combat vehicle.

Recognised by Nkonki Inc. SOC Integrated Reporting Awards for excellence in corporate reporting. Achieved top position in annual report disclosures for 2011, for ethical leadership and corporate citizenship as well as in boards, directors and remuneration including independence.

BUSINESS OUTLOOK

The defence budget in SA remains under pressure. SA's draft strategic defence review has, however, shed some light on the future direction of the defence industry, which will enable Denel to adjust its long-term plans and strategy. The steady increase in Africa's GDP, as well as the requirement for peacekeeping activities creates opportunities for Denel. SA's membership of the BRICS economic community creates potential opportunities in these developing markets. However, the economic challenges in Europe are expected to increase competition in Denel's traditional markets.

Notwithstanding these challenges, Denel has managed to increase its order cover and concluded two major export contracts worth R5bn. In addition, the awarding of local orders such as GBADS II, A-Darter and the Hoefyster production contract are expected during the 2012/13 financial year. The announced R700m recapitalisation by the shareholder will substantially strengthen our solvency and cash position. Although encouraged by these positive events, the group is still facing challenges regarding the loss-making status of the aerostructures business, high debt levels, cost structure and the ramp-up of new projects.

Denel has prioritised the following initiatives to address the above:

- Revenue growth is the cornerstone and a top priority to ensure long-term sustainability. Actions include enhanced business development function focussing on closing key opportunities and penetrating niche markets, as well as closer cooperation between Denel and various state departments to support conversion of export opportunities.

- Process and efficiency optimisation, materials management, quality management at source and clear performance contracting with applicable accountability will continue to be driven across all units. In addition, inter-company synergies will be maximised from a market, product and supply chain point of view.

- The focus will be on developing a funding model for the company to strengthen the balance sheet and ensure liquidity at all times.

- Negotiations have taken place between DAe and Airbus, aimed at improving prices of the A400M work packages to ensure the long-term sustainability of this company. Restructuring at DAe will continue, including exiting non-viable contracts, space optimisation and growing the order book.

- Denel will continue its transformation journey. Most notably the B-BBEE level 3 rating was maintained. The focus will also be on employment equity and skills development.


6
ZEISS

BUSINESS UNIT **OVERVIEW**

DENEL BUSINESS UNITS

DENEL DYNAMICS MISSILES

Denel Dynamics Missiles is a leader in advanced systems technology. Its core business covers tactical missiles and precision-guided weapons. A wide range of products along with world-class facilities, excellent customer support record and a formalised quality control system (e.g. ISO 9001 and 14000), add up to an impressive capability in the design, development, manufacture, supply and provision of services.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	619	729	(110)
Export turnover	194	192	2
EBIT	11	5	6
Confirmed order book	598	715	(117)
Workforce complement - head count	732	718	14

Note: The financial indicators above represent the unit's performance, including intergroup activities.

Main activities include the following:
SA is one of the few countries in the southern hemisphere to house the specialised technological capabilities required to be a proud innovator of sophisticated missiles – a competitive advantage honed by over 45 years of experience. Products are designed to meet the needs of the government, but always with profitable export opportunities in mind. Local customer remains the best possible ‘launch customer’ from where further unique product solutions can be developed for the export market.

The business unit also serves as a high-tech development institution for young engineers and technicians, developing human capital for both the defence and high-tech manufacturing sectors in SA. The current range of products and systems includes the A-Darter air-to-air missile system, the Umkhonto-IR air defence missile systems, the Ingwe and Mokopa anti-armour missile systems, precision-guided munitions and the Raptor II stand-off weapons.

Key highlights and successes include the following:

- Posting a nominal profit associated with a positive cash balance, with a continued year-on-year improvement in the overall inherent business performance in accordance with the “Voyage to Excellence” programme launched in 2007.
- Umkhonto missile deliveries to a European country completed in 2011/12 – a major success.
- The development of the A-Darter missile is on track for production to commence in 2014. Final missile qualification and performance validation is under way to achieve critical technical milestones in 2012/13 and 2013/14. As part of this evaluation the first two successful guided missile firings from a Gripen aircraft have been successfully completed during February 2012.
- In May 2011, Denel Dynamics Missiles concluded a contract for the sale of Umbani to an export customer. This contract is a prime example of how the substantial investment in intellectual property over a number of years has been afforded an opportunity to yield a return for SA.
- Denel Dynamics Missiles participated in the 2011 International Astronautical Congress. Denel Dynamics Missiles has the capability to add real value to the SA national space programme and thus will be able to play an active role in the exploration of exciting opportunities in this regard.
- Ingwe was not only successfully integrated and flight tested on the EC635 helicopter, but the first flight test with an alternative multipurpose warhead also took place.
- The latest configuration of the Raptor stand-off weapon was introduced as a “fire-and-forget” weapon. This full autonomous flight was a first for the Raptor weapon system.
- Creating a little bit of history! In 2011 a SA smart weapon developed by Denel Dynamics Missiles and integrated by a broader SA industry team was launched from a SAAF Hawk fighter aircraft at OTR for the very first time: a great display of local industry talent and capability.
- Denel Dynamics Missiles was voted 3rd top graduate employer in the SA graduate recruitment association candidate survey (engineering & industrial category), and employer of choice by 60 students from 34 high schools at the University of Pretoria's engineering week held recently.

DENEL DYNAMICS UAVS

The UAVS business unit is a proud innovator of competitive tactical unmanned aerial vehicles and high-speed target systems. This business unit is involved in the design, development and manufacture of world-class unmanned aerial systems (UAS).

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	124	185	(61)
Export turnover	56	160	(104)
EBIT	19	31	(12)
Confirmed order book	116	333	(217)
Workforce complement - head count	99	90	9

Note: The financial indicators above represent the unit's performance, including intergroup activities.

Denel UAVS range of products and systems include:

- Seeker II and Skua high-speed target drone systems.
- Seeker 400 tactical UAS is currently under development.

Key highlights and successes include the following:

- Managed to achieve profitability despite a decline in revenue due to some of the orders not realising.
- Exceptional programme management skills that resulted in excellent profitability on support contracts.
- Continued progress on the Seeker 400 development programme, despite expected challenges on a programme of this magnitude. This UAV has been designed to stay airborne for 16 hours whilst simultaneously operating two payloads.
- Planned development of a small UAV (Hungwe), in order to diversify the portfolio away from only tactical UAVS, but into commercial (non-military) markets, as well as price-sensitive markets.

DENEL AVIATION

DAv is the original equipment manufacturer of the SAAF Rooivalk combat support helicopter and design authority of the SAAF Oryx medium transport helicopter. DAv is also an accredited and certified provider of MRO solutions (including upgrades and systems integration) for both fixed and rotary wing aircraft, and associated components and ground support equipment.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	1 047	736	311
Export turnover	226	37	189
EBIT	60	(159)	219
Confirmed order book	330	2 213	(1 883)
Workforce complement - head count	1 146	1 175	(29)

Note: The financial indicators above represent the unit's performance, including intergroup activities.

Main activities include the following:

- Eurocopter-accredited MRO service centre for the following Eurocopter military and civilian rotary wing aircraft: Super Puma AS332; Puma SA330; Squirrel AS350; Bo105; Alouette SE3160. Also a primary MRO provider for the SAAF Oryx and SAAF Rooivalk helicopters.
- The Rooivalk OEM, Oryx and Cheetah design authority and further provides MRO engineering support, upgrade solutions and systems integration and design, development, certification and flight testing competence.
- Lockheed Martin-accredited Hercules Service Centre for C130 and L100 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 platforms.
- Accredited Eurocopter dynamic component repair and overhaul centre offering depot-level maintenance of avionics, electrical, oxygen and hydro mechanical components. The facility is also accredited to carry out repairs and calibration of ground support and test equipment.
- Sourcing and securing of technical skills for clients in the execution of client business objectives, including labour recruitment, remuneration management, training, administration and interaction with labour unions on behalf of clients.

Key highlights and successes include the following:

- Completed retrofit of eight Rooivalk aircraft to the certified Mark 1F baseline and delivered the aircraft to the SAAF. Got formal confirmation that the current 1F baseline has been accepted and that a formal process to initiate development contract closure is underway.
- An agreement was concluded between the SAAF and DAv that formalises the SAAF/DAv collaborative efforts and secures a multi-year base load business for DAv on the SAAF assigned platforms.
- On the back of the SAAF/DAv agreement and based on the success of the C130 MRO at Air Force Base Waterkloof, an air transport MRO was launched at Air Force Base Waterkloof expanding the types to be supported beyond C130 to include Cessna Caravan and CASA aircraft.
- Despite the setback experienced during delivery of the first batch of Cheetah aircraft to an export customer, the project has recovered and all aircraft delivered and accepted by the customer, thus instilling much confidence in the customer's mind.

DENEL LAND SYSTEMS

DLS is the primary landwards defence systems integrator in SA. It designs, develops, integrates, supplies and supports landward based high-mobility, high-firepower product systems, combat turrets, rapid-fire small and medium calibre weapons, new generation combat vehicle systems, as well as artillery systems. DLS's combat proven systems are in service in several countries. The unit is currently executing the largest landward system export contract in SA's history.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	546	554	(8)
Export turnover	262	73	189
EBIT	23	9	14
Confirmed order book	402	680	(278)
Workforce complement - head count	420	391	29

Note: The financial indicators above represent the unit's performance, including intergroup activities.

Main activities, including key products and services, are the following:

- Taking high-end technology and engineering capabilities in complex systems and/or products through their entire lifecycle, from conceptualisation to production and in-service support. Key product areas are infantry systems, artillery systems, infantry weapons and vehicles.
- Providing product and logistical support, including testing and qualification, maintenance, upgrades and eventual decommissioning, as and whenever required.
- The development and ultimate production of the 'Badger' family of new generation infantry combat vehicles (ICV), under project 'Hoefyster'. The development of variants continues apace, with a significant milestone of the product baseline for the 'section variant' achieved on 10 September 2010. This simultaneously kick-started a countdown process towards the much anticipated production order, with another four variants following closely behind the lead prototype vehicle. Project Hoefyster is utilising five state-of-the-art modular combat turret variants, armed with the home-grown GI-30 (30mm CamGun) and 60mm breech-loading long-range mortar system. Ingwe anti-tank missile system is integrated into the anti-tank variant of the 8x8 armoured modular vehicle platforms. The aim of project Hoefyster is to replace the SA Army's ageing fleet of Ratel ICVs in a phased approach, whilst also creating specific export potential.
- Other products and systems include several artillery systems, combat turrets and rapid-fire small and medium-calibre weapons, for which a wide range of highly competitive, unparalleled world-class products are available.

Key highlights and successes include the following:

- The successful business turnaround and the steady growth over the past five years.
- The future outlook in terms of potential prospects being pursued will double DLS's turnover within the next three years.
- The contract was received on the 17 May 2011 for the production of turret systems. The contract value amounts to an approximate figure of R3,5bn.
- There is good progress in terms of alignment between the user requirements and the Denel offering for the Hoefyster programme.
- Obtained a vehicle capability through taking a majority stake in LMT Holdings (Pty) Ltd. This will enable DLS to produce a local version of the Patria combat vehicle with a dramatic impact on job creation.
- DLS received an award as finalist for the second year running from the Department of Trade and Industry (DTI) for its "Best Enterprise Quality Award", as well as platinum membership by the SA Quality Institute.
- DLS listed on the "Best Employer" awards for 2011/12, which is one of the CRF Institute's projects known as Top Employers (locally known as Best Employers South Africa)
- DLS had successful demonstrations of the new weapon management system for artillery to international clients which hold significant potential for export business.
- The unit had a number of successful socioeconomic development initiatives that included, among others, bursaries, community out-reach programmes, as well as, adopting Philadelphia High School for students with disabilities.

PRETORIA METAL PRESSINGS

PMP is an integrated mass-manufacturer of small- and medium-calibre ammunition and technology-related products for military and commercial use.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	499	501	(2)
Export turnover	130	141	(11)
EBIT	8	14	(6)
Confirmed order book	254	361	(107)
Workforce complement - head count	1 424	1 350	74

Note: The financial indicators above represent the unit's performance, including intergroup activities.

PMP's products are widely used by many clients, including within the SANDF, the South African Police Services (SAPS) and other security agencies, locally and abroad. These include small- and medium-calibre ammunition for soldiers, air defence systems, fighting vehicles, helicopters, fighter aircraft and navy vessels. It also manufactures crew escape systems and power cartridges for local and international clients.

The company supplies handgun and rifle ammunition to the commercial sector, with its hunting ammunition being acclaimed by local and international users. It also provides the mining industry with drill bits and the electrical manufacturing sector with brass strip. These are commercial products that are derived from defence technology. Lead styphnate and lead azide are supplied to the chemical industry for the manufacture of detonators for the mining industry.

Main range of products includes the following:

- Small-calibre ammunition ranging from 5.56mm to 12.7mm and medium-calibre ranges of ammunition from 20mm to 35mm that 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.
- Probit rock drill bits 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 80 tons of brass strip daily. A major portion is used for the manufacture of ammunition by PMP itself or by international clients procuring brass cups and discs from SA, with the remainder of the brass strip sold to the SA commercial market.
- Pro-Amm, Standard, Super and African Elite ranges of hunting ammunition have established a reputation for quality, accuracy and reliability in SA, as well as in the European and United States (US) markets. The company's apt slogan is 'Masters of the Ammunition Art'.

Key highlights and achievements include the following:

- Although the business environment continued to be tough due to the world economic climate and the Rand that is still strong against other currencies, PMP did well to maintain reasonable profits and positive cash generation.
- The unit continued to invest in new-technology manufacturing equipment with a positive effect on manufacturing costs. R18m was spent on additions/replacements, and a state-of-the-art modern primary explosive facility was completed during the year.
- Accident-free hours totalled 2 458 702 hours on 19 March 2012. The LTIFR is 0,06 which puts PMP amongst the top 5% of the safest companies involved in dangerous goods in the world.
- The product development of the PRAC-T, APCI-T and SAPHEI-T of the 30 x 173mm rounds for Project Hoefyster has been completed. Attention during 2012 will be to also complete a HEI-T round. The product development of the ammunition for the 20 x 42mm NEOPUP weapon has also been completed.
- Although the usage of small- and medium-calibre ammunition by the SANDF is estimated to be more than R200m per year, sales to the SANDF were approximately R125m, emphasising the need for earlier planning.

DENEL AEROSTRUCTURES

DAe uses advanced manufacturing technologies to design and produce complex composite and metallic aircraft structures. DAe is positioned as a Tier 1 and 2 supplier in the global aerospace supply chain, supplying aerostructures to OEM's and Super Tier 1 customers such as Airbus. DAe is working with local Tier 3 and 4 parts manufacturing suppliers as part of developing and growing the domestic national aerospace supply chain.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	260	281	(21)
Export turnover	122	254	(132)
EBIT	(74)	(223)	149
Confirmed order book	191	1 278	(1 087)
Workforce complement - head count	382	453	(71)

Note: The financial indicators above represent the unit's performance, including intergroup activities.

Main range of products, services and activities include the following:

- The design, qualification, industrialisation, detail manufacture and assembly of the Airbus A400M wing-to-fuselage fairing and fuselage top shells, providing DAe with a long-term base load order cover.
- The manufacture and assembly of the Empennage for the Gulfstream G150 aircraft.
- The manufacture of components and fuselage assemblies, as well as main rotor heads and blades for the AgustaWestland A109 LUH helicopter.
- Major structures for the Saab Gripen programme, including North Atlantic Treaty Organization (NATO) specification pylons, as well as the main landing gear fuselage unit and rear fuselage.
- Providing engineering support and parts manufacture for the Rooivalk combat support helicopter programme.

Key highlights and achievements include the following:

- DAe has undertaken restructuring in the past two years which has resulted in improved financial and delivery performance. The strategy going forward is to scale capabilities to Airbus A400M technology related requirements upon which further orders in line with the technology strategy can be secured.
- An important restructuring priority for the year under review was the renegotiation of the A400M contractual terms and conditions as well as price. Airbus and Denel concluded a term sheet on 24 November 2011 whereby amendments to the contracts were agreed. The term sheet included changing legal conditions from the existing contracts for DAe, as well as improved contractual prices. The amendment of the current contracts is in progress and is anticipated for completion in the second quarter of 2012.
- DAe achieved an in-principle agreement with Airbus to transfer the A400M 'Ribs, Spars and Sword'-packages for approximately R200m to DAe during the 2012/13 financial year with serial production commencing in 2014.
- Various other restructuring activities took place during the year under review such as the footprint consolidation project whereby the rental footprint will be reduced from 54 000m^2 to 25 000m^2. This will reduce DAe's footprint by December 2012 to ensure more sustainable rental and a lean organisation going forward. The project involves a major reorganisation of DAe's industrial capabilities.
- Government's NGP and IPAP2 mandate a structurally new path and movement to a knowledge based economy to obtain sustained economic growth and social development. In terms of IPAP2 various sector development plans (SDPs) have to be developed. DAe actively supported the development of a draft Aerospace SDP. Government review and evaluation of Aerospace SDP has been initiated.

MECHEM

Mechem is a global leader in creating a safer environment through the provision of clearance solutions of explosive remnants of war (ERW), canine services, related skills development, mine and ballistic protected vehicle design and manufacture, ancillary equipment and remote camp management and maintenance services to the UN, other international agencies, governments and commercial customers globally.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	302	151	151
Export turnover	285	149	136
EBIT	20	17	3
Confirmed order book	57	131	(74)
Workforce complement - head count	62	65	(3)

Note: The financial indicators above represent the unit's performance, including intergroup activities.

Main activities include the following:

- A range of technologies, services and products in its ERW clearance applications. The technologies employed include manual demining, battle area clearance (BAC), stockpile destruction and explosive ordnance disposal (EOD), vehicle-mounted demining, mechanised demining, landmine surveys, range clearance, quality assurance and victim assistance.
- Mechem Explosives and Drug Detection System (MEDDS), a unique remote scent detection capability, used in the identification of mines, explosives, drugs and other contraband, thus significantly improving the success of detecting banned and dangerous substances, while vastly reducing the time required to clear large facilities and vehicle queues.
- Specialist canine services, including the breeding and sale of trained detection and patrol dogs, screening of cargo, as well as training of dogs and dog handlers.
- The Casspir mine protected vehicle is rated as the world standard for such vehicles.
- Operational support of commercial activities, such as major events.
- Range clearance of military and other firing ranges contaminated by unexploded ordnance.
- Afrifoot, a programme launched to facilitate the manufacture and supply of low-cost leg prostheses to landmine survivors.
- Skills development in related fields, through an in-house fully equipped training centre, where demining, demining management, detection dog handling and other related courses are offered.
- The management and maintenance of camps in remote post-conflict areas.

Key highlights and successes include the following:

- Completion of various demining or mine clearing projects in Afghanistan, Sudan, DRC, Angola and Mozambique, delivering large tracts of land and thousands of kilometres of roads clear of mines and other ERW. This supports these countries and their citizens in returning to normality.
- Trained dogs are used in cargo screening for the detection of narcotics and contraband as required by part 108 of the International Civil Aviation Authority's prescriptions on handling cargo. Trained Mechem detection dogs have also been supplied to Namibia, Benin and South African game parks where they have been successful in various large drug busts, as well as apprehending rhino poachers.
- The supply of a large quantity of demining equipment and vehicles, as well as related training to the Executive Demining Commission in Angola.
- The company's skills development expanded internationally and students from Mozambique, Egypt, Benin and Namibia have been trained in demining and dog handling related fields.
- The company was successfully audited on ISO 9001, ISO 14001 and OSHS 18001 in October 2011 and retained these accreditations.
- The company received its DH5 accreditation from the SASSETA and can now accredit the students who complete the dog handlers' courses to this level.

DENEL INTEGRATED SYSTEMS SOLUTIONS

DISS is the business unit within Denel that specialises in higher order, complex systems such as GBADS.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	48	5	43
Export turnover	-	-	-
EBIT	10	(85)	95
Confirmed order book	-	70	(70)
Workforce complement - head count	57	53	4

Note: The financial indicators above represent the unit's performance, including intergroup activities.

Main activities, products and services include the following:

- Designated as single-source supplier of the GBADS capability to the SANDF.
- Extensive modelling and simulation experience in the conceptualisation and design of systems.
- Design, develop, produce, integrate and qualify complex systems.
- Lifecycle support of systems, including the ability to coordinate and manage changes to the system baseline.

Key highlights and successes include the following:

- Completion of the GBADS LWS programme has positioned the company to continue with the follow-on phases of the programme.
- The foundation that has been created will enable the company to branch into other complex systems environments, such as border safeguarding, maritime systems and other related security focused domains.

DENEL OVERBERG TEST RANGE

OTR is a versatile missile and aircraft test range that specialises in rendering 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 military systems. Its primary business goal is to meet the strategic flight test and wider system qualification requirements of SA's military-industrial users, as well as international defence forces and armament industries.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	102	83	19
Export turnover	47	35	12
EBIT	6	1	5
Confirmed order book	45	145	(100)
Workforce complement - head count	166	163	3

Note: The financial indicators above represent the unit's performance, including intergroup activities.

The test range provides turnkey flight test, system certification and performance evaluation services that include:

- Flight tests on 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, as well as electronic warfare tests.
- Mobile telemetry launch support services in remote locations during space missions, as well as operating a ground station for the transfer of data to and from satellites.

Key highlights and achievements include the following:

- The unit's branding was aligned with the overarching Denel group brand to maximise the advantage of being part of SA's leading defence and aerospace group.
- Excellent service was once again provided to the test range's main client, the SANDF. A three-year contract with the DoD&MV (2011/12 to 2013/14) secures approximately 45% of the range's projected income for the period.
- For the domestic market further test campaigns on the 5th generation A-Darter development programme were supported. One of the firings against a Skua high-speed target drone was confirmed to be the most complex dynamic set up used to date in an air-to-air scenario at the range.
- Three international test campaigns involving testing of advanced missile and air defence systems were conducted, offsetting the negative effect of the cancellation of the planned joint SA-German Cape of Good Hope exercise. Clients were satisfied with the test and support services rendered, confirming again the range's suitability and convenience for a wide range of weapon system evaluations.
- Remote telemetry support was provided from Invercargill, New Zealand, for National Centre for Space Studies (CNES) during the successful launch of the ATV3 spacecraft. This was the second launch supported under the frame contract with CNES.
- The test range maintained its ISO 9001 and ISO 14001 (2008 and 2004 respectively) certification, which underlines its commitment to quality service delivery within the bounds of prevailing legislation and agreed environmental management principles.

ASSOCIATES

RHEINMETALL DENEL MUNITION (PTY) LTD

RDM is an integrated producer of energetic materials, ammunition and related products. Its product portfolio includes large-calibre ammunition (76mm to 155mm), artillery projectiles, propellant, charges and pyrotechnic carriers, mortar bombs, 40mm grenades, rocket motors, SADs and various missile sub-systems.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	963	1 124	(161)
EBIT	33	162	(129)
Workforce complement - head count*	1 554	1 440	114

**Including external contract labour and labour brokers*

Key highlights and achievements include the following:

- The integration of RWM's business approach into RDM to achieve a turnaround from an EBIT loss of R117m in 2008 to a sustainable profit of R93m for their financial year ending 31 December 2011.
- RDM implemented an aggressive savings programme to counter the Rand exchange rate fluctuations.
- Securing new orders from international clients (e.g. 105mm PFF ammunition for the US Government) has resulted in strong increase of the order backlog, with further growth in sales anticipated in the future.
- Capital investment projects of R513m to upgrade and modernise all of RDM's facilities is well on track with positive results on safety, environment, productivity and decrease of maintenance.
- The Philippi site has been successfully relocated to Somerset West with minor elements to finalise.
- RDM is centre of excellence for all 60mm, 81mm and 120mm mortar, as well as 155mm artillery systems worldwide.

TURBOMECA AFRICA (PTY) LTD

TMA is the world leader in design, manufacturing and sale of gas turbines for small and medium powered helicopters and has 50 years experience of cooperation in SA since the first Artouste II engine for an Alouette II in 1960.

In both civilian and military aviation a substantial number of turbine helicopters are fitted with Turbomeca turbo-shaft engines. In military aviation, in particular, turbine helicopters are fitted with Turbomeca turbo-shaft engines like Oryx, Rooivalk and A109 LUH.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	345	303	42
EBIT	53	73	(20)
Workforce complement - head count	240	233	7

TMA has extensive capabilities for:

- Manufacturing of:
  - Gears and shafts, either spur helical or spiral-bevel.
  - Five-axis high-speed machining for gearbox casings, either magnesium or aluminium.
  - For Safran group and Rolls-Royce mainly.
- MRO of:
  - Makila, Turmo and Arrius engines.
  - Parts Repair for Makila, Turmo and Arrius.
  - Repair and overhaul for Makila and Turmo accessories, as well as Arrius HMU.
  - Sole engineering centre of excellence for Artouste and Turmo engines.
  - Engine test facilities for Makila, Turmo and Arrius.
- TMA maintenance centre renders a 24-hour customer service over sub-Saharan Africa.

Key highlights and achievements include the following:

- Major efficiency improvements in maintenance and repair activities of engines and accessories, resulting in a minimum turnaround time for customers.
- Continued delivery of Rolls-Royce gearboxes as single-source supplier.
- Improvements in internal efficiencies, ensuring continued profitability despite the impact of the global recession.
- Acquired the heat treatment facility, therefore, the integration of the heat treatment and surface treatment by mid-2012 will help TMA to raise its profile in manufacturing and MRO parts repair.

The business unit has had a successful turnaround and continued to post positive financial results due to good order cover and world-class industrial systems and processes.

CARL ZEISS OPTRONICS (PTY) LTD

CZO is a global supplier involved in the development and production of optronics, optical and precision-engineered products for military and security applications.

Key areas	2012 Rm	2011 Rm	Variance Rm
Turnover	431	393	38
EBIT	27	15	12
Workforce complement - head count	277	286	(9)

The company's main activities include the supply of optical sensors, optical head trackers, laser rangefinders, as well as targeting surveillance and sighting systems, to a spectrum of domestic and international defence and security clients.

Key highlights and achievements include:

- Continuing improvement in skills base achieved through training interventions.
- Continuous improvements in manufacturing efficiencies.
- Certification according to EN 9100-2009 for design and manufacture of products for airborne applications.
- Centre of excellence established for design and production of submarine periscopes.

DIRECTOR AND EXECUTIVE **PROFILES**

DENEL BOARD OF DIRECTORS


Zoli Kunene (59)

Studies in law, Certificate in Industrial Relations and attended various leadership courses.

INDEPENDENT NON-EXECUTIVE DIRECTOR AND CHAIRMAN OF THE DENEL BOARD

OTHER DIRECTORSHIPS: CEO of Kunene Brothers Holdings, Kunene Industrial Holdings, Kunene Motor Holdings, Kunene Finance Company, Non-executive director of 3C Telecommunications, Cell C, CellSAF, Grintek Ewation, OB Investments and Virgin Mobile.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Vast board and business experience having acted as president and chairman on various boards and institutions, legal, negotiation skills, strategy, business development and marketing.

Appointed to the board on 19 October 2006 and as chairman of the board on 6 July 2011.


Fikile Mhlontlo (43)

BCompt, BCompt (Hons), CTA, CA (SA) and attended various courses in leadership and management.

EXECUTIVE DIRECTOR AND GROUP CHIEF FINANCIAL OFFICER (GCFO)

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Permanent invitee of the group audit and risk, as well as the group personnel, remuneration and transformation committees, non-executive director of PMP, Denel Industrial Properties and RDM, as well as trustee of Denel Post Retirement Trust.
OTHER DIRECTORSHIPS: Former director and audit partner of one of the big four audit firms, and held various management positions. Serving as audit and risk committee member of LoveLife.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership in financial management, financial reporting and discipline, corporate governance, understanding of audit process and strategy formulation.

Appointed to the board on 1 November 2008.


Riaz Saloojee (49)

Brigadier General (Ret.), joint staff course (SANDF), senior command and staff course (SAAF), junior command and staff course (SA Army), certificate in strategic management (UP).

EXECUTIVE DIRECTOR AND GROUP CHIEF EXECUTIVE OFFICER

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Permanent invitee to the group audit and risk, the group personnel, remuneration and transformation committees, as well as business unit boards.
OTHER DIRECTORSHIPS: Former CEO of a number of defence companies such as Tau Aerospace, Metatek, Grintek Integrated Defence Systems and Saab South Africa and Saab International (Sub-Saharan Africa). Former soldier, held various positions within the Defence Force including advisor on transformation and human resources management and later leaving the force as a Brigadier General. Serving chairman of Aerospace Maritime and Defence Industries Association (AMD).
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Vast leadership experience, business development and marketing, negotiation skills, mergers and acquisitions, international defence and customer experience, significant experience working in Sub-Saharan Africa.

Appointed to the board and as group chief executive officer on 16 January 2012.


Ghandi Badela (53)

MSc (electromechanical engineering, packaging technology and engineering man.), MBA and LLB.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Group personnel and remuneration and transformation committee, chairman of DAv.
OTHER DIRECTORSHIPS: Non-executive director of City Power, Amagcisa Holdings, Badela Brothers and Kowethu Leisure, member of Advisory Council of University of Johannesburg Engineering Faculty. Former executive at Saab Grintek. Former CEO of Masana Technologies.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership, business operations management, project management, intellectual property management and commercial law.

Appointed to the board on 6 July 2011.

Dr Gert Cruywagen (56)

MSc, PMD, FIRM (SA), Risk Management Diploma, Certificate Advanced Security Management, PhD.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Group audit and risk committee member, chairman of DAe, non-executive director of Denel Dynamics.

OTHER DIRECTORSHIPS: Chairman of group governance and risk committee of City of Johannesburg, trustee of GCM Trust, trustee of Tsogo Sun Group Medical Scheme, trustee of Tsogo Sun Pension Fund, director of risk of Tsogo Sun group (Tsogo Sun Holdings), executive director of Tsogosure Insurance Company Ltd, member of the King committee on Corporate Governance, and convenor of the Risk workgroup for King II and King III.

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership in Corporate Governance, risk management, insurance, business management and strategy formulation.

Appointed to the board on 4 September 2008.

Prof Tshilidzi Marwala (40)

BSc Mech. Eng, Masters Mech. Eng, PhD Computational Intelligence Eng. Systems, Post Doc in Information Technology.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Chairman of Denel Dynamics and non-executive director of DLS.

OTHER DIRECTORSHIPS: Chairman of Committee of Deans of Engineering of South Africa, member of South Africa's Department of Higher Education and Training Research Output Committee, member of Limpopo Premier's Employment Growth and Development Strategy Advisory Council, deputy chairman of Knowledge Enabled Industry Technical Working Group, member of EOH, member of City Power Johannesburg, trustee of the Bradlow Foundation, member of South African Academy of Engineering, trustee of Carl and Emily Fuchs Foundation and has held various non-executive director roles.

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership, relevant industry skills as an engineer, business management, lecturer and researcher.

Appointed to the board on 27 August 2010.

Martie JV Rensburg (55)

BCom, BCompt (Hons) (CTA), CA (SA), Executive Leadership Programme.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Chairman group audit and risk committee, Non-executive director DAv.

OTHER DIRECTORSHIPS: Non-executive director of the Airports Company South Africa (ACSA), NMI Group, chairman of NMI (Namibia) and Headstream Holdings, past chairman of Johannesburg Water, former CEO of TCTA and has held various non-executive director roles. Non-executive member of First Rand Bank Africa Credit Committee.

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Senior leadership, financial management, project finance and project management, governance, business processes optimisation and strategy.

Appointed to the board on 27 August 2010.

Ziphozethu Mathenjwa (35)

BSc, Certificate in Financial Management and Investments, Post Grad Dipl in Management, MBA, MSc in International Business, Post Grad Dipl in Strategic management and Corporate governance.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Chairman of PMP.

OTHER DIRECTORSHIPS: Non-executive director of Mvula Trust and Umgeni Water Board, deputy chairman of audit committee of Department of Economic Development, Environment and Tourism Mpumalanga, founder and director of Gabsie Business Solutions. Former non-executive director at the Water Research Commission.

RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership, board and business experience and stakeholder engagement.

Appointed to the board on 6 July 2011.

DENEL BOARD OF DIRECTORS

Nkopane Motseki (46)

Certificate in Forensic Investigations and Crime Intelligence, various intelligence courses.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Chairman of Denel Industrial Properties and non-executive director of Mechem.

OTHER DIRECTORSHIPS: Held various executive roles in different organisations including Intelligence and Matjhabeng local municipality.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Policy development, experience in intelligence and security, strategy, media liaison and customer care.

Appointed to the board on 6 July 2011.

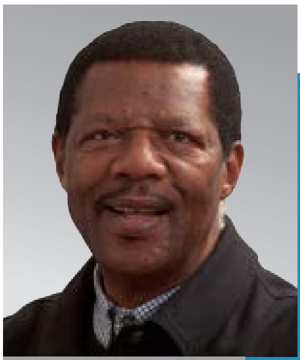
Bulelwa Paledi (41)

BA, LLB, LLM.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: The group audit and risk member, chairman of Mechem and non-executive director of DAe.
OTHER DIRECTORSHIPS: Non-executive director of ICC (DBN), executive director Ndamse Incorporated and Faku Investment Holdings (Pty) Ltd.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Leadership, legal and business management.

Appointed to the board on 27 August 2010.



Mavuso Msimang (70)

BSc, MBA.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Member of group ethics and social committee, chairman of DLS.
OTHER DIRECTORSHIPS: Former CEO of Sita and former Director General of Home Affairs. Chairman of iSimangaliso Wetland Park and Infiniturn Solutions and Gidani, non-executive director of African Parks Network, Peace Parks Foundation, Blue Print Holdings, Harmony Gold Mining, and Investment Solutions.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Senior leadership, transformation, restructuring, executive management experience, environmental management, stakeholder relations and good governance

Appointed to the board on 6 July 2011.

Bafana Ngwenya (50)

Certificate in Defence Management, Certificate in Practical Project Management, Strategic Management Certificate.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Member of the group audit and risk, non-executive director of DLS and DPS.
OTHER DIRECTORSHIPS: Hellocomms and Winter Robin Investments 9.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Business management, project management, intelligence and security as well as defence industry knowledge.

Appointed to the board on 6 July 2011.

Prof Stella Nkomo (65)

BA in Business Education, MBA, PhD.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: Chairman of the group personnel, remuneration and transformation committee as well as Denel ethics and social committee.
OTHER DIRECTORSHIPS: Professor of Human Resources Management at the University of Pretoria. International Women's Forum of SA. Previous key positions include being director of research, visiting scholar, operations director, professor of business leadership and research coordinator.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Vast experience in leadership, change management, transformation / diversity management, organisational behaviour and human resource management.

Appointed to the board on 6 July 2011.

Melissa Ntshikila (39)

BA, LLB, LLM.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: The group personnel, remuneration and transformation member, non-executive director of DPS and DTA. Senior government negotiator on labour related matters in the Department of Public Service and Administration.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Human resources, labour law expertise and labour relations, negotiations skills as well as legal.

Appointed to the board on 6 July 2011.

Matodzi Ratshimbilani (38)

B Proc, Certificate in Business Management, Mining Executive Preparatory Programme and Certificate Prospecting and Mining Law.

INDEPENDENT NON-EXECUTIVE DIRECTOR

DENEL BOARD AND BOARD COMMITTEE MEMBERSHIP: The group personnel, remuneration and transformation member, non-executive director of DISS and PMP.
OTHER DIRECTORSHIPS: Founding director at Tshisevhe Gwina Ratshimbilani Inc and non-executive director at Railway Safety Regulator.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Specialising in mergers, acquisitions and corporate governance, labour law, competition regulations and environmental management.

Appointed to the board on 6 July 2011.

Sonja Sebotsa (40)

LLB (Hons), MA SFA (UK).

INDEPENDENT NON-EXECUTIVE DIRECTOR

OTHER DIRECTORSHIPS: Founder and principal partner of Identity Partners, non-executive director of RMB Holdings, Discovery Holdings, Anglo Platinum, Mr Price Group, Dimension Data Holdings SA and Old Mutual Property Group.
RELEVANT SKILLS, EXPERTISE AND EXPERIENCE: Expertise in corporate finance, strategy, merger and acquisitions as well as international law.

Appointed to the board on 6 July 2011.

DENEL EXECUTIVES

Riaz Saloojee (49)

Executive Director and Group Chief Executive Officer
Brigadier General (Ret.), joint staff course (SANDF), senior command and staff course (SAAF), junior command and staff course (SA Army), certificate in strategic management (UP).
Denel board and board committee memberships: Permanent invitee to the group audit and risk, the group personnel, remuneration and transformation committees, as well as unit boards.
Other directorships: Former CEO of a number of defence companies such as Tau Aerospace, Metatek, Grintek Integrated Defence Systems and Saab South Africa and Saab International (Sub-Saharan Africa). Former soldier, advisor on transformation and human resources management issues, held various positions and later leaving the force as a Brigadier General. Serving chairman of Aerospace Maritime and Defence Industries Association (AMD).
Relevant skills, expertise, and experience: Vast leadership experience, business development and marketing, negotiation skills, mergers and acquisitions, international defence and customer experience, significant experience working in Sub-Saharan Africa.
Appointed as Group Chief Executive Officer on 16 January 2012.

Fikile Mhlontlo (43)

Executive Director and Group Chief Financial Officer
BCompt, BCompt (Hons), CTA, CA (SA) and attended various courses in leadership and management.
Denel board and board committee memberships: Permanent invitee to the group audit and risk, as well as the group personnel, remuneration and transformation committees, non-executive director of PMP, Denel Industrial Properties and RDM, as well as trustee of Denel Post Retirement Trust.
Other directorships: Former director and audit partner of one of the big four audit firms, and held various management positions. Serving as Audit and risk committee member of LoveLife.
Relevant skills, expertise, and experience: Leadership in financial management, financial reporting and discipline, corporate governance, understanding of audit process and strategy formulation.
Appointed to the Group Executive Committee on 6 October 2008.

John Morris (43)

Group Executive: Strategy and Commercial
BSc (Hons) (Psychology and Sociology), MSc (Agricultural Economics).
Denel board committee memberships: Non-executive director of DAe and DPS.
Other directorships: Served in various positions in the DTI, Trade and Investment South Africa and Decillion.
Relevant skills, expertise and experience: Strategy development and execution, corporate restructuring, mergers and acquisitions, economic policy and public sector knowledge.
Appointed to the Group Executive Committee on 1 November 2008.

Maj Gen (Ret) Otto Schür (62)

Group Executive: Technical
Senior certificate, various military training and executive leadership courses, post graduate qualification in aviation safety and accident investigation.
Denel board committee memberships: Non-executive director of Denel Dynamics, DAv and Denel Technical Academy (DTA).
Other directorships: 40-year career in the SAAF including advanced combat flying qualifications, squadron command tours, Defence Attaché to Switzerland, Assistant Director Fighter Programmes, Director Air Force Acquisition and Chief Director Acquisition in the Defence secretariat., non-executive director at AMD and former positions as non-executive director at DLS, OTR and TMA.
Relevant skills, expertise, and experience: 17 years of project management experience, technical and systems management, negotiation skills, problem solving, strategic planning and business development.
Appointed to the Group Executive Committee on 1 February 2008.

Mike Ngidi (54)

Group Executive: Human Resources and Transformation
BAdmin.
Denel board committee memberships: Chairman of personnel, remuneration and transformation committees of DISS, OTR and DAv. Held various positions over a 24 year period at Unilever within Human Resources.
Relevant skills, expertise, and experience: HR strategy development and deployment, industrial relations, transformation and change management.
Appointed to the Group Executive Committee on 1 April 2012.

Zwelakhe Ntshepe (54)

Group Executive: Business Development and Corporate Affairs
Post graduate Diploma in Management Studies, MBA.
Denel board committee memberships: Non-executive director of DISS, DLS, OTR and CZO. Former chief operating officer of Denel Personnel Solutions Industrial.
Other directorships: Former stockbroker in New York and has held various management roles.
Relevant skills, expertise, and experience: Business management, negotiation skills, marketing and business development.
Appointed to the Group Executive Committee on 1 September 2003.

Rentia Geldenhuys (44)

General Manager of Denel Industrial Properties
BCompt (Hons), CFS (SA).
Denel board committee memberships: Chairman of the DLS audit and risk and member of the DLS board.
Other directorships: Director of Denel Properties (Pty) Ltd and Bonaero Park (Pty) Ltd, Centurion Aerospace Village.
Relevant skills, expertise, and experience: Leadership in financial and business management, financial reporting and discipline, system implementing and process changes.
Appointed as General Manager on 1 April 2011.

Stephan Burger (54)

Chief Executive Officer of Denel Land Systems
BEng (Hons) Mechanical.
Denel board committee memberships: Non-executive director of DISS.
Relevant skills, expertise, and experience: Leadership experience in business management and engineering experience.
Appointed as Chief Executive Officer on 1 November 2004.

Ismail Dockrat (42)

Chief Executive Officer of Denel Aerostructures
NDip Electronics Engineering, Certificate in Programme Management, MBA.
Denel board committee memberships: Former positions include CEO of DAv, non-executive director of DAe, TMA and chairman of DPS.
Other directorships: Former positions include CEO of Wesgro, general manager (GM) at TISA and project manager at Armscor.
Relevant skills, expertise, and experience: Strategic leadership, business management, programme management and turnaround management.
Appointed as Chief Executive Officer on 1 March 2010.

Carel Wolhuter (61)

Chief Executive Officer of Pretoria Metal Pressings
BCom Acc, BCom Acc (Hons), CA (SA).
Relevant skills, expertise, and experience: Senior leadership, financial management, solid manufacturing and export related knowledge, including experience drawn from performing as financial director in a listed company and prior general manager positions.
Appointed as Chief Executive Officer on 1 April 1996.

DENEL EXECUTIVES

Mike Kgobe (43)

Chief Executive Officer of Denel Aviation
Masters in Aeronautical Maintenance and Production Management and Executive Leadership Programme.
Denel board committee memberships: Executive director of DPS, non-executive director of TMA and RDM.
Other directorships: Non-executive director of Commercial Aviation Association of South Africa.
Relevant skills, expertise, and experience: Business management, engineering and project management.
Appointed as Chief Executive Officer on 1 March 2010.

Jan Wessels (53)

Chief Executive Officer of Denel Dynamics
BEng (Hons) Electronics, Advanced Management Diploma.
Denel board committee memberships: Non-executive director of DISS.
Relevant skills, expertise, and experience: Systems engineer, project management expertise and business management.
Appointed as Chief Executive Officer on 1 December 2006.

Ralph Mills (47)

Chief Executive Officer of Denel Integrated Systems Solutions
BMil, MBL.
Other directorships: Non-executive director DAv.
Relevant skills, expertise, and experience: 14 years' experience as an officer in the SANDF, and 16 years' experience in the defence industry in various capacities.
Appointed as Chief Executive Officer on 1 April 2009.

Ashley Williams (55)

Chief Executive Officer of Mechem
BMil and related certificates.
Other directorships: Foundation for Military Engineering in Southern Africa and Gunners Engineers Memorial (GEM) Village (both NPOs).
Relevant skills, expertise, and experience: Business management, human resources and engineering experience.
Appointed as Chief Executive Officer on 1 June 2008.

Gawie van Zyl (46)

Acting General Manager of Denel Technical Academy
BCompt (Hons), MCom (Tax), CA (SA).
Denel board committee memberships: Audit and Risk Committee chairman of DAv and DPS and Trustee of Denel Pension Fund.
Relevant skills, expertise, and experience: Leadership in financial management and corporate governance roles. Extensive experience in strategy development, organisational restructuring and corporate finance.
Appointed as acting General Manager on 17 January 2012.

Abrie van der Walt (53)

Chief Executive Officer of Denel Overberg Test Range
MSc (Computer Science), Executive Leadership Programme.
Relevant skills, expertise, and experience: Business management and executive leadership experience.
Appointed as Chief Executive Officer on 1 December 2005.

Tsepo Monaheng (48)

Executive Manager Denel Dynamics UAVS
BSc (Physics and Maths), BSc (Electronics) Eng, MBA.
Other directorships: Non-executive board member of DAv.
Relevant skills, expertise, and experience: Engineering, business management and executive leadership experience.
Appointed as Executive Manager on 1 July 2006.

06

SUSTAINABILITY **AND** **GOVERNANCE**

SUSTAINABILITY

The Denel group strives to be a respected corporate citizen and duly recognises the impact of its business activities on the environment. Denel aims to conduct its business in a sustainable manner to preserve its future for all stakeholders by making positive contributions to its economic, social and natural environments. These principles are embedded in the group's corporate strategy and practiced in the financial and economic decisions that are made by the group, focussing on people skills, supplier development, stakeholder relationships and participation in socioeconomic development.

Denel acknowledges that sustainable business practice is a moral imperative that requires innovation, fairness and collaboration, as well as economic awareness. Denel's values and ethics policy guide business practices and behaviours in respect of sustainability objectives and performance. The group embraces the principles of the King III Report on good corporate governance, requiring an annual integrated report on the group's economic, social and environmental performance. These matters impact profitability, competitiveness and the survival of the group, and therefore are monitored and reported on.

Denel is committed to improving sustainability management and will continue to:

- Identify impacts of activities on the environment.
- Improve risk and opportunity management.
- Execute contracts profitability and diversify markets.
- Enhance brand and reputation.
- Increase customer interaction and market share.
- Increase business and operational efficiency.
- Strengthen supplier development.
- Positively strive to effect employee recruitment and retention.
- Focussing on leadership and skills development.
- Prevent regulatory noncompliance through effective oversight.

Sustainability processes are in place and these have been implemented at business unit level taking into account all aspects of sustainability, including safety, health, environment, quality and social issues. Policies and procedures account for the nature and uniqueness of each business unit. The following methodology is adopted in addressing sustainability issues:

Vision and leadership

- Understand material sustainability issues
- Appoint champions
- Identify mission, vision and operating principles
- Communicate and train staff on sustainability

Planning

- Identify key material issues
- Develop strategic plans
- Create
  - Short-term actions
  - Priorities
  - Objectives
  - Responsibilities
- Identify and engage stakeholders

Implementation

- Ensure active management and internal controls
- Include in performance management system related matters
- Extend to external parties

Monitor, review and support

- Measure progress
- Incorporate material issues in an annual report
- Incorporate feedback in communication to stakeholders
- Obtain assurance

MANAGEMENT IS AN INTEGRAL PART OF THIS PROCESS

The individual businesses are required to assess their sustainability issues, develop and implement strategies as necessary. In line with King III which requires that the disclosure of sustainability issues be reviewed, considered and evaluated. The board, through the audit and risk committee, understands the key strategies, risks and the sustainability issues pertaining to the group. The group audit and risk committee oversees the evaluation and reporting of sustainability issues. Each business unit board, through their audit and risk committee, is responsible for overseeing the implementation of sustainability strategies, practices and reporting. The overall responsibility for implementation rests with business unit executive management.

MATERIAL SUSTAINABILITY ISSUES

Identifying Denel's material issues involves engagements with both internal and external stakeholders through various initiatives, as well as considering the group's risk management processes and feedback from sustainability indices. An issue is material when it impacts the group's ability to remain commercially viable and is socially relevant to the societies in which it operates. In particular, material issues are those that have a strong bearing on Denel's stakeholders' assessments and decisions about Denel's sustainability in the long-term. As part of the group's sustainability programme, Denel developed systems, which enable the group to identify risks and opportunities.

Denel actively identifies material issues. KPIs are used throughout the group to measure and monitor performance towards achieving key goals and targets. KPIs are aligned to the key performance areas of the Shareholder's Compact, agreed on an annual basis, with additional KPIs emanating from the corporate plan across the group for implementation and regular monitoring by all levels of management. The group's performance against KPIs is provided in the *Shareholder's Compact* on page 25. The group executives are assigned responsibility to implement the KPIs and drive performance, as well as to ensure that processes for sustainable improvements are embedded within the key focus areas.

In addition to the key focus areas, sustainability practices are incorporated in Denel's conduct of business. Sustainability objectives are established and are aligned to Denel's strategic business deliverables which also assist the group in addressing its material issues. The group is proud of the positive contributions it continues to make, whilst managing its impacts on the social and natural environments in which it operates.

The group has focused on strengthening its balance sheet, addressing the continued losses posted by DAe, revenue growth and its contribution as a state-owned company (SOC) to the NGP of SA. The above mentioned challenges are the group's most significant and material issues, which are also discussed in the *directors' report* on pages 114 to 119, and throughout the *sustainability and governance section*.

However, Denel is cognisant of the fact that its long-term sustainability not only depends on successful resolution of these issues, but is also dependent on social and environmental sustainability.

Denel reviews its materiality analysis annually to ensure that the group's corporate responsibility communications remain relevant and meaningful to the group's stakeholders, reflecting the changing landscape of corporate responsibility and public awareness and concern over specific issues.

ECONOMIC IMPACT

OVERVIEW

Denel's economic footprint is broader than what is reflected in the financial statements. SA has a strong defence industry, which benefits the wider economy and is a valuable instrument in the earning of foreign currency. Denel has over the years diversified its portfolio of products and services that are based on defence-related technologies mainly to serve commercial clients in the general manufacturing and mining sectors. Denel contributes to the economy through employment, contribution to the fiscus in the form of taxes and earning foreign currency as well as development and support of the local industry.

Denel's mandate includes contributing to government priorities as articulated in policies and guideline documents such as the NGP and IPAP2. It is the policy of Denel to promote enterprise development by enabling suppliers from historically disadvantaged backgrounds and small, medium and micro enterprises (SMME's) to participate in the mainstream of the SA economy. Local suppliers are positioned to compete for business in the commercial sector as a direct result of experience and capabilities gained through involvement with Denel.

The group's economic footprint in 2011/12 is characterised by revenue of R3 568m (2010/11: R3 252m) of which R1 329m (2010/11: R1 045m) is exports. Denel contributes to the SA economy by creating and distributing wealth to the value of R1 865m (2010/11: R1 793m), refer *value added statement* on page 60. The group has a workforce of 4 716 employees (2010/11: 4 716), excluding associates.

DIRECT IMPACTS

CONTRIBUTING TO THE DEFENCE INDUSTRY

Denel is the state-owned technology partner that ensures strategic military independence for the country. Denel designs, develops, integrates, supplies and supports artillery, munitions, missiles, aircraft sub-assembly manufacturing, aircraft maintenance, UAVS and optical payloads based on high-end technology. The group's products and solutions are designed and developed to meet unique end-user requirements of the SANDF, including a full lifecycle support and ultimately reducing cost of ownership. The current programmes include the landward systems project, Hoefyster, GBADS II (design phase in the process of being contracted) and A-Darter.

Denel, together with its strategic alliances and partnerships, is contributing to creating safer environments with products that have been tailor-made for Africa, the UN, other international agencies, governments and commercial customers globally. The SANDF plays an important role in peacekeeping missions in Africa, this is very important considering that peacekeeping is the single most important precondition for economic development.

INDUSTRIAL DEVELOPMENT

Denel, through its business units and associates, plays a significant role in industrial development via its custodianship of its key conventional technologies, diverse quality products and operational capacity. This also includes R&D programmes, product development, manufacturing and maintenance activities, well-defined infrastructure and strong human capital base.

Denel delivers technologically advanced and efficient products to the global market, together with a wide range of sophisticated services and solutions to increase the value of the group's products and services to its customers. Denel is leveraging not only the enduring defence-related capabilities resulting from its 45-year heritage of supporting products and services, but also its contemporary expertise and experience, to achieve milestones.

Denel takes high-end technology and engineering capabilities in complex systems and/or products through their entire lifecycle, from conceptualisation to production and in-service support which can extend to a number of years. It provides product and logistical support, including testing and qualification, maintenance, upgrades and eventual decommissioning, as and when required. The research, design, development, integration, qualification, certification and industrialisation are undertaken primarily in-house, with selected specialised items outsourced to strategic partner companies. Significant elements of production are outsourced to the broader SA manufacturing industry and relevant businesses are also vertically integrated with production commencing with raw materials through to final products. As such, investment in R&D has a special economic significance in extending Denel's global footprint, apart from its conventional association with scientific and technological development.

By leveraging the defence technology base, innovative applications have been found to increase rail safety, crime protection, surveillance, protection of assets, mine safety management, as well as in the manufacturing of mining drill

bits, commercial brass strips, amongst others. Despite the current global economic conditions and continuous shrinking of the defence budget Denel has maintained R&D spend at R752m compared to R789m in 2010/11. R&D investment is 21% of revenue, consisting of self-funded development of 5% (2010/11: 2%) of sales and client-funded development of 16% (2010/11: 20%).

TECHNOLOGY AND INNOVATION IMPACTS ON NATIONAL DEVELOPMENT GOALS

Several policy frameworks and action plans have been launched by government in recent years to express its strategy and industrial policies to convert the SA economy from a predominantly resource and services based economy to a so-called 'knowledge-based' economy. High technology and advanced manufacturing associated with defence manufacturing are internationally regarded as one of the highest contributors to such knowledge-based economy. Denel's contribution is as follows:

- It links developed human capital to knowledge-based economic activity.
- SA's technology competitiveness is highlighted through Denel's advanced engineering and manufacturing capabilities.
- Denel's technology base includes certain products contributing to environmental management and security surveillance capabilities.
- Denel's technologies include OEM/tier 1 qualification.

EMPLOYMENT AND SKILLS DEVELOPMENT

Technology skills are a scarce resource in SA today, and the cost of developing personnel in this sector is extremely high. It is well-known that Denel provides a fertile ground for nurturing engineers, technicians and artisans, with most of these technical professions subsequently contributing to key national projects in transportation, construction and power generation, as well as wider general advanced manufacturing activities.

Indications are that for each employee of the group, there is a multiplier effect in terms of which at least four jobs that are created in the economy as a whole. This takes into account the fact that Denel subcontracts substantial work. The group's contribution to employment supports the NGP. In addition, the group makes a positive impact on a number of employees, their families, local communities and businesses. The Denel group employs 6 787 people (2010/11: 6 684), including those within associates. Comprehensive details on such initiatives are provided in the *people management section* on pages 82 and 83.

TEN-YEAR REVIEW

FOR THE YEAR ENDED 31 MARCH 2012

The following table illustrates the ten-year performance of the group. The group has experienced challenges that have impacted on its financial performance over the past few years. The performance and challenges are discussed in the *directors' report* on pages 114 to 119 of this annual report.

	2012 [1] Rm	2011 [1] Rm	2010 [1] Rm	2009 [1] Rm	2008 [1] Rm	2007 [1] Rm	2006 [1] Rm	2005 [1] Rm	2004 Rm	2003 Rm
INCOME STATEMENT										
Revenue	3 568	3 252	3 610	3 924	3 818	3 268	2 773	3 572	4 442	4 372
Profit/(loss) before net finance cost and income from associates	100	(314)	(162)	(463)	(233)	(387)	(1 076)	(1 315)	62	203
Net finance cost (before capitalised interest)	84	120	139	73	61	143	188	104	120	109
Depreciation	93	93	92	112	108	132	150	157	121	107
Profit/(loss) before taxation [3]	49	110	(236)	(508)	(312)	(494)	(1 291)	(1 409)	(350)	(45)
Profit/(loss) after taxation from continuing operations	41	111	(246)	(533)	(321)	(507)	(1 311)	(1 416)	(384)	(72)
Taxation expense [3]	(8)	(1)	(10)	(25)	(9)	(13)	(19)	(7)	19	30
Non-controlling interest in profit/(loss)	-	(47)	(65)	(91)	(13)	(1)	-	5	(7)	-
Profit/(loss) for the year	41	111	(246)	(533)	(347)	(549)	(1 363)	(1 561)	(378)	(73)
Cash outflow before financing activities	210	(23)	(416)	(1 163)	222	(946)	(1 061)	(422)	(201)	(229)
STATEMENTS OF FINANCIAL POSITION										
Non-current assets	2 131	2 110	1 677	1 623	1 476	1 348	1 601	2 173	1 350	1 415
Current assets	3 420	2 921	3 343	3 107	3 607	2 616	2 724	2 410	2 742	2 839
Assets held for sale	91	7	-	9	58	540	352	68	-	-
Total assets	5 642	5 038	5 020	4 739	5 140	4 504	4 677	4 651	4 092	4 254
Current liabilities [4]	3 659	3 704	3 671	3 446	3 081	3 000	1 938	2 888	2 347	1 960
Total equity	695	654	609	849	1 328	633	615	(16)	844	1 388
Non-controlling interest	-	-	(34)	31	102	6	7	7	9	20
Non-current interest bearing borrowings	101	101	101	53	1	2	832	848	832	841
Current interest bearing borrowings	1 865	1 845	1 943	1 074	234	833	14	520	76	9

	2012 [1] Rm	2011 [1] Rm	2010 [1] Rm	2009 [1] Rm	2008 [1] Rm	2007 [1] Rm	2006 [1] Rm	2005 [1] Rm	2004 Rm	2003 Rm
STATISTICS										
Total number of shares in issue (million)										
Class A ordinary shares	1 000	1 000	1 000	1 000	1 000	976	849	402	402	402
Class B ordinary shares	225	225	225	225	225	40	40	40	40	40
Total shares	1 225	1 225	1 225	1 225	1 225	1 016	890	442	442	442
RETURNS (%)										
Operating profit/(loss) to turnover	2.8	(9.7)	(4.5)	(11.8)	(6.1)	(11.8)	(38.8)	(36.8)	1.4	4.6
Operating profit/(loss) to average total assets	1.9	(6.2)	(3.4)	(9.9)	(4.8)	(8.4)	(23.1)	(30.1)	1.5	4.8
Operating profit/(loss) to ordinary shareholders ' interest [2]	14.4	(48.0)	(26.6)	(54.5)	(17.5)	(61.1)	(175.1)	-	7.5	14.9
RATIOS										
Debt/equity ratio [2]	2.8	3.0	3.4	1.3	0.2	1.3	1.4	-	1.1	0.6
Current asset ratio	0.9	0.7	0.8	0.9	1.2	0.9	1.4	0.8	1.2	1.4
Net finance cost cover	0.7	1.2	(1.6)	(6.9)	(5.2)	(3.5)	(6.9)	(13.5)	(3.0)	(0.4)
Revenue per employee (Rm)	0.8	0.7	0.7	0.8	0.5	0.4	0.3	0.4	0.4	0.4
Number of employees	4 716	4 716	5 090	5 067	7 276	7 634	8 850	9 942	10 925	10 878

[1] *The balances from 2005 onwards are compiled in accordance with IFRS. The financial years before 2005 are stated according to SA GAAP.*
[2] *Due to the negative equity the debt/equity ratio and loss to average ordinary shareholders interest for 2005 are undefined.*
[3] *Profit/(loss) before taxation and Taxation expense had been restated for the years 2003 to 2011 due to the change in the recognition of Share of profit in associates as disclosed on page 128.*
[4] *Current liabilities had been restated for the years 2010 and 2011 due to the change in classification of Advance payments received as disclosed on page 127.*

VALUE ADDED STATEMENT

FOR THE YEAR ENDED 31 MARCH 2012

Value added is a measure of the wealth that the group has created in its operations by adding value to the cost of materials and services purchased. The statement shows how wealth was created and how it was shared amongst employees, the providers of funds and the capital re-invested in the group for continuation and expansion of operations.

	2012		2011	
	Rm	%	*Restated* Rm	%
Revenue	3 568		3 252	
Less: Cost of materials and services purchased	(1 960)		(2 039)	
Value added	1 608		1 213	
Add:				
Finance income	61		37	
Other income	196		543	
Wealth created	1 865		1 793	
Distributed as follows:				
Employees: Salaries and relevant costs	1 563	83.8	1 467	81.8
Providers of capital	145	7.8	110	6.1
Interest on borrowings	145	7.8	157	8.7
Non-controling interests	-	-	(47)	(2.6)
Government				
Tax (refer note A)	23	1.2	12	0.7
Re-invested in the group for continuation and expansion	134	7.2	204	11.4
Depreciation (refer note 3)	93	5.0	93	5.2
Accumulated profit	41	2.2	111	6.2
Wealth distributed	1 865	100	1 793	100
Note A				
Tax				
Tax paid and provided for:	23		12	
Current tax	9		-	
Total tax	8		(1)	
Deferred tax	1		1	
Rates and taxes paid to local authorities	14		12	
Customs and excise duties included in cost of materials and services purchased				
Employer's UIF contributions	7		-	
Net skills development levy	7		-	
	37		12	
The total amount reflected above excludes the following amounts collected by the group on behalf of government:				
Net VAT	2		7	
Charged on sales	321		334	
Levied on purchases	(319)		(327)	
Employees' taxation	297		282	
Employees' UIF contributions	7		8	
	306		297	


Mk2

STAKEHOLDER ENGAGEMENT

OVERVIEW

The development and maintenance of sound relations with Denel's stakeholders remain among the key priorities of the group. Denel is aware of the importance to continuously engage with its customers, suppliers and business partners and to strengthen the group's reputation as a credible, respectable business, reliable and trustworthy partner. These engagements cover critical issues including the sustainable financial position of the group, exploration of new business opportunities, investment in new research and development, technology and manufacturing capabilities and the prospects for the development of new products and services.

Within SA, Denel strongly focuses on its relationship with its primary clients in the local defence community, most notably the DoD&MV and Armscor. Close ties are maintained with Denel's shareholder, the DPE. The Minister of Public Enterprises, the Deputy Minister, the Director General and the senior executive management of the department have demonstrated their interest in the group's business through their engagement with various Denel structures and their regular visits to units. Denel also welcomes its constructive relationships with the Parliamentary Portfolio Committees on Public Enterprises and of Defence. The group annually makes presentations to Parliament, responds to questions from committee members and host parliamentary delegations at its facilities.

With Denel's intention to grow its export business, the group is focusing on relationships with foreign stakeholders and clients as contained in the Denel strategy. In the past year the group was visited by a significant number of foreign delegations, including the President of Benin and Chairman of the African Union, Thomas Boni Yayi, and a ministerial delegation from Brazil during the IBSA Summit. Denel also places a high value on its relationship with local and international media. These engagements reflect the core values of Denel, namely professionalism, integrity, accountability and a commitment to openness and the free flow of information.

Denel organised and hosted a number of media conferences, media visits to facilities and open days, issued statements on important developments and new products launched by the company and responded in a professional manner to media queries. Amongst the highlights of the past year were the handover of three fully-certified Rooivalk combat support helicopters to the SAAF, Denel's contribution towards science, technology, engineering and mathematics education initiatives, Denel's support of peacekeeping operations and the delivery of GBADS I to the SA Army.

Some comments that appeared in the media by the group's stakeholders and Denel's response are summarised as follows:

Media report	Denel's response
Full ownership of DAe returned to the group April 2011	Denel confirmed that Swedish company, SAAB, has decided to exercise its 'put' option with regards to its equity partnership in Denel Saab Aerostructures. Denel is now a 100% shareholder in Denel SAAB Aerostructures (DSA) – subsequently renamed, Denel Aerostructures.
Denel targets the training of engineers, artisans and skilled technicians May 2011	The training of engineers, artisans and technicians is receiving priority attention in the Denel group in an effort to contribute to addressing skills shortages in SA. "There is an increasing demand for scarce skills in the fields of science and technology and we are making rapid strides to close this gap, especially in the aviation and weapon systems sectors," said Denel GCEO.
Denel products and services can help to combat scourge of piracy June 2011	Denel emphasised the contribution the group's products and services can make to combat the scourge of piracy along the African coastline. The company said in a statement it is well-positioned to support the SANDF and other regional forces and agencies that must implement the new maritime strategy.
Denel achieves level 3 B-BBEE status June 2011	Denel achieved a level-3 B-BBEE status following evaluation by Empower Logic. The results demonstrated Denel's commitment to transformation with improvement in most areas, whilst, employment equity and skills development require further improvement.
Company announces that order pipeline continues to strengthen July 2011	Denel announced that its order pipeline continues to grow significantly and prospects are being pursued. The conversion of these prospects into orders will significantly strengthen Denel's turnover and contribute to the turnaround process at the company.
PMP wins new export contract in the UK December 2011	PMP won a R93m order for ammunition components from a unit of BAE Systems in the United Kingdom. PMP began manufacturing brass cups and discs for BAE Systems in 2001, and has since supplied more than 3,4bn components in more than 350 weekly shipments. In addition to ensuring the retention of skills and jobs at PMP's brass plant, this export contract also increases PMP's foreign exchange earnings.
Denel training programmes support maths and science teaching January 2012	Specialised training in mathematics and science offered by Denel is helping a growing number of high school students to achieve outstanding results. Following the release of the 2011 matric results the group said it is contributing to an improvement in the quality of maths and science teaching through outreach programmes and additional tuition offered to learners in disadvantaged areas.

The main stakeholder interactions during the year under review were with Denel's shareholder, the DPE and NT, local client, namely the DoD&MV and Armscor, international clients, employees and members of the public.

Stakeholders	Material Issues	Outcome
Shareholders and other related government departments including: • DPE • DoD&MV • NT • DTI • DST • DIRCO • NCACC • Economic development parliamentary portfolio and select committees.	• Financial performance. • Debt and funding. • Key performance areas. • Appointment and introduction of new GCEO. • Group strategy. • DAe losses, challenges and alternatives to be explored. • Denel contribution to NGP. • Government support for export opportunities and industry participation. • Denel future state and alignment.	• Government guarantee rolled over to support loans. • Shareholder's Compact with KPI's. • Corporate plan for five years. • Cooperation between Denel and state departments. • Denel more aware and focussed on skills development. • Denel more focussed on stakeholder relations. • Organisational restructuring. • Support for DAe pursuing various scenario's. • Continue with the execution and completion of the GBADS programme. • Developed a SA focussed industrial approach to offset/industrial participation opportunities.
Clients including: • DoD&MV • Armscor • SAPS • International clients • Local commercial clients	• Custodian of core strategic and sovereign capabilities. • Value for service delivery. • Cooperation agreements. • Performance and programme delivery. • Contracting and contracting models. • DoD&MV budget constraints and requirements. • Promote product ranges and demonstrate capabilities including participating in national and international exhibitions. • Support for the release of key orders. • Approval of orders pending.	• Achieved 84% of contracted milestones for the year under review. • Agreement on conclusion of Drummer II on GBADS I programme slippages. • Secured MRO support for Rooivalk. • R752m R&D spend. • Alignment in certain strategic planning focus areas. • Integrating capabilities to improve efficiencies, i.e. C130 support at air force base. • Key milestones achieved on A-Darter, Hoefyster and Rooivalk. • Customers informed of technological developments and solutions offered by Denel.
Employees	• Sharing of general information of key business developments through internal newsletters, GCEO road shows, strategic leadership and communication forums. • Business focus and strategy updates. • Business performance updates. • Maintained the group restructuring and transformation committee. • Performance management and recognition, including transformation, health and safety, and procurement from previously disadvantaged groups.	• Informed employees. • Engagement and timeous conclusion of salary negotiations.
Defence Review Committee	• Made a presentation to the committee covering key capabilities, products, markets and industry issues.	• Draft Defence Review document was published for public comments in April 2012. • The group is currently preparing comments to present to the committee.

CORPORATE GOVERNANCE

OVERVIEW

INTRODUCTION

The company has a mature corporate governance process that meets most of the recommendations of the King III report, as well as the requirements of the new 2008 Companies Act, which became effective 1 May 2011. Statements regarding Denel's adherence to the King III report on corporate governance are set out in this report. This report details certain governance principles and the main duties of the chairman, committees and group chief executive officer. The board charter includes a schedule of matters reserved for the board and the terms of reference of various board committees.

The board is committed to sound governance and ensures that the group's business is conducted in accordance with high standards of corporate governance, using risk management and control in accordance with local and internationally accepted systems of internal controls, which have been implemented to comply with King III recommendations and the governance requirements of the 2008 Companies Act.

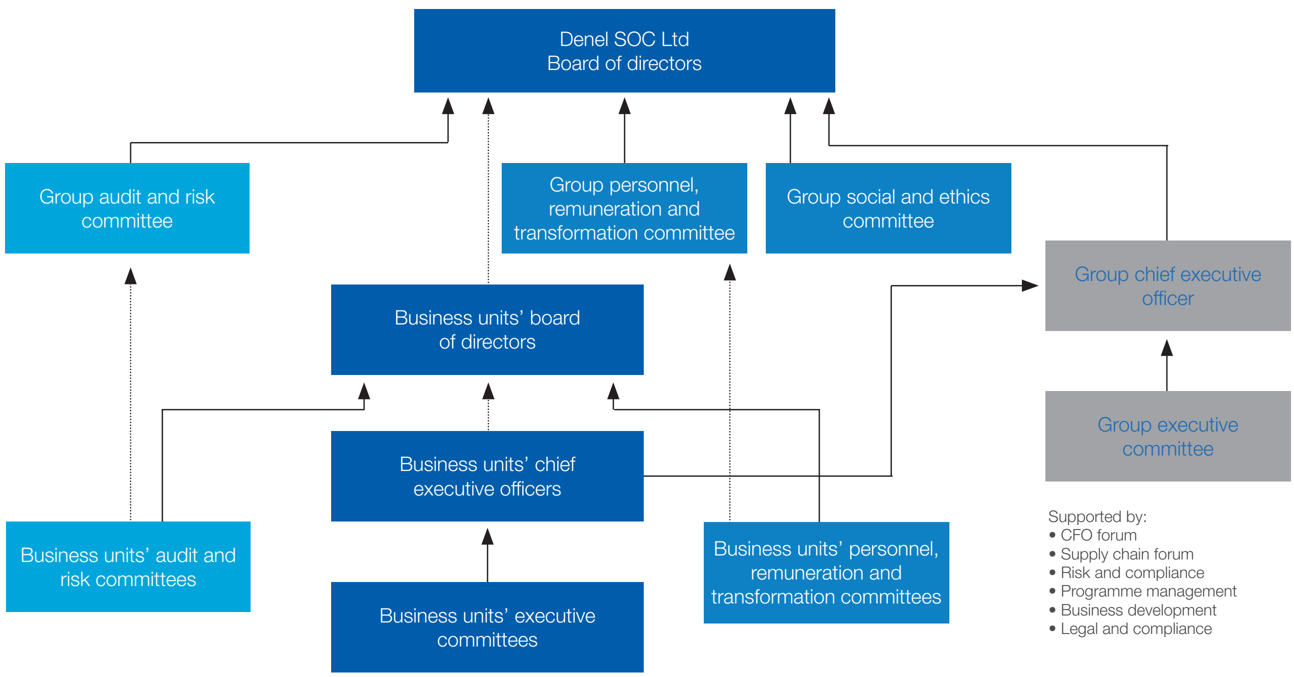
To ensure that corporate governance encompasses the concept of sound business practice within the group, it is inextricably linked to the group's management systems, structures, policies and culture of governance. This ensures that the group acts towards all stakeholders in a responsible and transparent manner from an economic, social and environmental perspective.

RESPONSIBILITY AND ACCOUNTABILITY

The board provides leadership and strategic oversight, and oversees the control environment in order to achieve and sustain value to the company's shareholder and stakeholders. The board ensures adherence to principles of good governance and accountability as espoused in King III and its board charter. 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 of character and judgement. The board ensures regular review of its performance and core governance, refer to page 67 i.t.o. the results of the 2012 board evaluation.

In executing its mandate, the board has set up a corporate governance framework that forms part of delegation of authority and is supported by the company's internal policies, internal controls and regulations, as depicted below.

THE COMPANY'S CORPORATE GOVERNANCE SYSTEMS



The day-to-day governance is the responsibility of Denel's management, who report to the board and its sub-committees. The board and the audit and risk committee chairman play an active role in driving and addressing the corporate governance issues that arise from time to time through regular interaction with executive directors, senior management and other stakeholders as and when necessary.

BOARD STRUCTURE

The group has a unitary board, comprising of two executive directors, the GCEO and the GCFO, as well as 14 non-executive directors, who all meet the board's independence criteria i.t.o. being free from any business relationship that could generally hamper their objectivity or judgement on the business and activities of the group.

APPOINTMENT AND RETIREMENT OF DIRECTORS

In terms of Denel's Memorandum of Incorporation, the shareholder appoints the chairman and directors. The executive directors are appointed by the board and their appointment approved by the shareholder.

In line with the requirements of good governance, the shareholder reviews the composition of the board on a regular basis. This ensures the rotation of directors at regular intervals, and the board remaining dynamic in its thinking and abilities. In appointing the non-executive directors, the shareholder takes cognisance of the group's needs in terms of skill, experience, diversity, size and demographics. The board comprises 88% of members from historically disadvantaged backgrounds and 38% female members, details of all board members are found on pages 44 to 47. The term of office of the non-executive directors is for a period of three years, subject to review at the annual general meeting. Re-election of non-executive directors is staggered to ensure continuity and succession planning. Retiring directors are eligible for re-appointment.

The GCEO has a three year contract, whilst the GCFO is a permanent employee, subject to Denel's conditions of service. During the year the board through its ad hoc nomination committee was tasked with the responsibilty of filling the vacancy of the GCEO following the resignation of the previous GCEO, Mr Talib Sadik. This process was finalised in October 2011, and the recommendation forwarded to the shareholder's for approval, as required by the company's Memorandum of Incorporation. In November 2011, the shareholder approved the appointment of Mr Riaz Saloojee as GCEO for a period of three years, effective 16 January 2012.

The following board changes took place during the year under review:

- Dr Sibusiso Sibisi (previous chairman), Ms Seadimo Chaba, Mr Llewellyn Jones and Mr Alan Hirsch retired from the board on 6 July 2011.
- Mr Zoli NR Kunene, a non-executive director, was appointed as chairman of the board. The following new members: Mr Ghandi Badela, Ms Ziphozethu Mathenjwa, Mr Mavuso Msimang, Mr Nkopane Motseki, Mr Bafana Ngwenya, Prof Stella Nkomo, Adv Melissa Ntshikila, Mr Matodzi Ratshimbilani and Ms Sonja Sebotsa were appointed to the board on 6 July 2011.

DIRECTORS' FORMALISED APPOINTMENT AND REMUNERATION

The executives have a contract of employment. The non-executive directors have their appointments formalised by a letter of appointment from the shareholder. This appointment letter indicates the non-executive directors' term of office, 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 annual general meeting (AGM). Although King III recommends non-executive directors to be paid an attendance fee and a base fee, Denel has elected to pay the non-executives a base fee for attendance at meetings. Details on the remuneration of executive and non-executive directors are presented on pages 72 to 73.

DIRECTORIAL INDEPENDENCE, EFFECTIVENESS AND PERFORMANCE EVALUATION

The independence of directors is guided by the King III Report, the Companies Act and best practice. The independence of individual non-executive directors is considered at every board meeting and formally evaluated every year by an independent consultant as part of the board's effectiveness review.

The independence and effectiveness review of the board is performed on a yearly basis. The evaluation report is considered at a board meeting and thereafter submitted to the shareholder representative.

Topics covered in the board's effectiveness evaluation include the following:

- Key role players
- Board meetings
- Committees of the board

- Role and responsibilities of the board
- Relationship - board and management
- Accountability of the board regarding to governance, including risk and IT
- Skills needed at the board
- Visible corporate governance

The independence and effectiveness of the board has been assessed shortly after year-end. The review was performed by an independent firm of consultants. Their report confirmed that the board was effective in performing its oversight role. There are more areas that the board is performing efficiently and scores in the top quartile in relation to other companies that have been assessed. The board has analysed the report and will implement recommendations.

BOARD INDUCTION AND SHARING OF INFORMATION

New directors undergo a detailed induction to ensure a comprehensive understanding of Denel's legislative framework, governance processes, delegation of authority and business operations. Directors are continuously briefed on relevant new legislation and regulations. The induction, along with continuous training, includes the board meetings being held at different business units, to allow the directors an opportunity to interact with business unit executives. The practice includes circulating monthly reports to the board members to keep them abreast of developments outside of the scheduled board meetings.

The Minister of the DPE also held an induction process whereby he shared his strategic intent statement with the new board and what was required from them as directors of a SOC. The board, together with the executive management, also attended a workshop to apprise them of the new Companies Act, Consumer Protection Act and Promotion of Access to Information Act (PAIA).

All non-executive directors have access to management and the records of the group as well as to external professional advisers should the need arise.

BOARD MEETINGS

The group holds four scheduled board meetings annually, as well as an AGM. All documents that are submitted to the board for discussions are meticulously prepared by the executives, taking into account matters arising from previous board meetings, ensuring completeness and other relevant matters for the board's consideration. Non-executive directors have unfettered access to the executive team and any other employees of the group to seek explanations and clarifications on any matter(s) prior to or following a board meeting. This facilitates the board's discussions and assists it in reaching speedy but informed decisions.

Members of the executive committee attend the board meetings as and when required, to report to the board on their respective operational areas.

Board members attendance for the period 1 April 2011 to 31 March 2012

	Board meetings										AGM meeting
Board members	Total	26 May 2011	Special 27 June 2011	In-Committee 20 July 2011	30 August 2011	In-Committee 6 October 2011	23 November 2011	Special 8 February 2012	13 February 2012	14 February 2012	6 July 2011
Dr SP Sibisi (chairman)*	2/2	√	√	-	-	-	-	-	-	-	√
Mr NR Kunene (chairman)+	9/9	√	√	√	√	√	√	√	√	√	√
Mr MT Sadik*	4/4	√	√	-	√	-	√	-	-	-	√
Ms SH Chaba*	2/2	√	√	-	-	-	-	-	-	-	√
Dr GC Cruywagen	9/9	√	√	√	√	C	√	√	√	√	A
Mr A Hirsch*	1/2	A	√	-	-	-	-	-	-	-	A
Ms MJ Janse van Rensburg	8/9	A	√	√	√	√	√	√	√	√	√

Board members attendance for the period 1 April 2011 to 31 March 2012 (continued)

Board members	Total	Board meetings									AGM meeting
		26 May 2011	Special 27 June 2011	In-Committee 20 July 2011	30 August 2011	In-Committee 6 October 2011	23 November 2011	Special 8 February 2012	13 February 2012	14 February 2012	6 July 2011
Mr LC Jones *	2/2	√	√	-	-	-	-	-	-	-	A
Prof T Marwala	7/9	√	√	A	√	√	√	A	√	√	A
Mr F Mhlontlo	7/7	√	√	-	√	-	√	√	√	√	√
Ms B Paledi	9/9	√	√	√	√	√	√	√	√	√	√
Mr R Saloojee ^	3/3	-	-	-	-	-	-	√	√	√	-
Mr G Badela #	7/7	-	-	√	√	√	√	√	√	√	-
Ms ZB Mathenjwa #	7/7	-	-	√	√	√	√	√	√	√	-
Mr NJ Motseki #	5/7	-	-	A	√	√	√	A	√	√	-
Mr M Msimang #	6/7	-	-	√	A	√	√	√	√	√	-
Mr BF Ngwenya #	7/7	-	-	√	√	√	√	√	√	√	-
Prof SM Nkomo #	6/7	-	-	A	√	√	√	√	√	√	-
Adv MS Ntshikila #	5/7	-	-	√	√	A	A	√	√	√	-
Mr MV Ratshimbilani #	6/7	-	-	√	√	√	√	√	A	√	-
Ms SEN Sebotsa #	3/7	-	-	A	√	√	A	A	√	A	-

A Apology
** Resigned during the year*
 # Appointed on 6 July 2011
+ Appointed as chairman on 6 July 2011
^ Appointed as GCEO on 16 January 2012
C Conference call

COMPANY SECRETARIAL

The group company secretary is responsible for developing systems and processes which enable the board to discharge specific functions efficiently and effectively. She is responsible for advising the board on corporate governance issues, setting the annual plan for the board in conjunction with the chairman and monitoring compliance with the PFMA, the Companies Act and other relevant legislation, as well as keeping the board updated on new relevant legislation. All directors have access to her services and guidance.

BOARD COMMITTEES

The board has established and delegated specific roles and responsibilities to three standing committees, namely the audit and risk committee, the personnel, remuneration and transformation committee, as well as the social and ethics committee. All standing committees are chaired by independent non-executive directors.

Each committee's role, responsibilities, and membership are in accordance with related terms of reference as approved by the board. These terms of reference are reviewed annually to ensure that they remain in line with relevant regulations, company's requirements and business climate in line with best practice in corporate governance.

Meetings of the board committees are held three times a year. Executives are regular attendees at the board and committee meetings in line with their roles and responsibilities.

In order to keep the board abreast of the activities of the committees, the minutes of the committee meetings are included in the board meeting pack for information. Significant matters discussed at these committee meetings are recommended and debated by the board prior to the board approving such matters.

AUDIT AND RISK COMMITTEE

Membership of the audit and risk committee including its chairman, comprises of independent non-executive directors, and the executive directors are standing invitees to committee meetings. All members of the committee have considerable financial and risk management experience necessary to oversee and guide the committee. These include the audit and risk functions, the governance of risk, and IT risk as recommended by King III.

Two members of the committee stepped down, and two new members were appointed, during the last AGM. These changes were attributable to the change in the board as detailed under appointments and resignations on page 66. In line with the recommendations of King III and the Companies Act, the appointment of members of the audit and risk committee was tabled at the AGM held on 6 July 2011. The relevant resolution was duly passed, with the proviso that the board appoint the chairman of the audit and risk committee. These appointments will be re-considered and voted on at every AGM.

The committee's terms of reference are reviewed and updated for relevant new legislation and best practice. The terms of reference include the 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 roles and responsibilities of the committee are detailed in the report of the audit and risk committee and include the following:

- Review of the financial statements and considering reports of the auditors on the financial statements.
- Review of risk registers, paying attention to risks, mitigation actions and overall risk management.
- Review of the effectiveness of the company's internal controls.
- Consider matters emanating from the company's ethics hotline, management planned actions and the results of enquiries.
- Agree the scope of the auditors' work and their fees.
- Monitor the performance of the internal audit function.
- Consider treasury controls and related risk management processes.

The committee chairman meets regularly with the external auditors, the group's internal auditor and the GCFO to consider the audit plans, the scope and status of the audits and progress on resolving significant issues.

The committee holds at least three meetings in any particular year. The committee has an annual work plan to ensure that all relevant matters are covered by the agendas of the meetings planned for the year as laid out in its terms of reference.

The invitees to committee meetings include the two executive directors, internal and external auditors, the group treasury manager, the group risk and compliance manager, and other executives responsible for the company's operations (when necessary). The audit and risk committee meets with the internal and external auditors without the presence of management.

At meetings of the committee, the committee fulfilled its responsibilities as set out in this report. Refer to page 110 of the *report of the group audit and risk committee*.

Attendance at the group audit and risk committee meetings

Board members	Group audit and risk committee meetings			
	Total	22 June 2011	12 October 2011	7 February 2012
Ms MJ Janse van Rensburg (chairman)	3/3	√	√	√
Dr GC Cruywagen	3/3	√	√	√
Mr BF Ngwenya +	2/2	-	√	√
Ms B Paledi +	2/2	-	√	√
Mr LC Jones *	1/1	√	-	-
Prof T Marwala †	1/1	√	-	-
Standing invitees				
Mr MT Sadik *	2/2	√	√	-
Mr R Saloojee ^	1/1	-	-	√
Mr F Mhlontlo	3/3	√	√	√

* *Resigned during the year*
^ *Appointed on 16 January 2012*
\# *Appointed on 6 July 2011*
\+ *Appointed on 20 July 2011*
† *Stepped down on 6 July 2011*

SOCIAL AND ETHICS COMMITTEE

In line with the Companies Act and accompanying regulations, the board has established a social and ethics committee and nominated non-executive directors, Prof Stella Nkomo, Dr Gert Cruywagen and Mr Mavuso Msimang as its first members. External experts, as proposed in the regulations, will be nominated and appointed by the board to this committee in the near future. Due to an overlap of certain agenda items of the audit and risk committee and the personnel, remuneration and transformation committee (PR&T) with this one, these former two committees' terms of reference had to be refined and tabled to the board for approval. The committee met for the first time on 15 June 2012 and will table a report at the AGM.

PERSONNEL, REMUNERATION AND TRANSFORMATION COMMITTEE

The norm in the industry is for the board to establish personnel and remuneration committee and a transformation committee, as two separate committees, Denel has a single committee that fulfils the roles of the two committees. During the year this committee changed its name to the PR&T in line with its updated terms of reference.

The membership of this committee comprises independent non-executive directors and is responsible for:

- Evaluating the performance of the executive directors and executive management, and setting appropriate remuneration for such officers in the group.
- Overseeing and monitoring the group's performance in respect of employment equity, transformation and staff development, taking into consideration the legal requirements.
- Skills development for retention and talent management.

Details of the company's employment equity practices and performance during the year are provided in the *transformation section* on page 84.

The performance of each executive is assessed relative to the prevailing business climate and market conditions, as well as to key predetermined targets. In accordance with principles of good governance, the executives being evaluated are recused from the meeting. Full details of the group's remuneration philosophy and payments to all executive directors and executive management are available on page 71 to 72.

Standing invitees to the committee meetings include executive directors, the group executive: HR and transformation, and other executives whose roles and responsibilities are relevant to the matters under consideration.

The committee held three scheduled meetings and one special meeting during the 2011/12 financial year, as detailed below.

Attendance at personnel remuneration and transformation committee meetings

Board members	Personnel, remuneration and transformation committee meetings					
	Total	Special 15 June 2011	25 October 2011	Special (In-Committee) 1 December 2011	Special (In-Committee) 19 January 2012	9 February 2012
Prof SM Nkomo (chairman)	4/4	-	√	√	√	√
Ms SH Chaba* (chairman)	1/1	√	-	-	-	-
Mr G Badela #	3/4	-	√	√	A	√
Adv MS Ntshikila #	4/4	-	√	√	√	√
Mr MV Ratshimbilani #	4/4	-	√	√	√	√
Mr NR Kunene +	0/1	A	-	-	-	-
Ms B Paledi **	1/1	√	-	-	-	-
Standing invitees:						
Mr MT Sadik *	3/3	√	√	-	√	-
Mr R Saloojee ^	1/1	-	-	-	-	√
Mr F Mhlontlo	3/3	√	√	-	-	√

A Apology
* *Resigned during the year*
** *Appointed to group audit and risk committee on 20 July 2011*
\# *Appointed as board member on 6 July 2011*
\+ *Appointed as chairman of the Denel board on 6 July 2011*
^ *Appointed on 16 January 2012*

REMUNERATION

The PR&T committee's mandate is to review the design and management of Denel's remuneration and reward principles, policies and implementation strategies so as to:

- Ensure that the group's executive directors and senior executives are competitively rewarded for their individual contribution to the group's overall performance.
- Demonstrate to all stakeholders that in Denel senior executives do not determine their own remuneration.
- Demonstrate to stakeholders that governance procedures are followed in the appointment of executive directors and senior executives of the group.
- Ensure that performance parameters of senior executives and executive directors are set and reviewed in accordance with the Shareholder's Compact.

In doing this, the PR&T committee ensures that there is:

- A group remuneration and reward policy governing basic pay, benefits and incentives.
- Alignment to the group's performance management system and process that outlines the process of evaluating performance.
- A formal process of appointing executive directors and senior executives.

The committee reviews, monitors and provides guidance on the group's transformation policies, plan and strategy with the broad objectives of:

- Ensuring that policies aimed at achieving the company's transformation vision, values and objectives are developed and implemented.
- Ensuring that plans and strategies aimed at compliance with legislation that impact, or have the potential to impact, on the company's rights are in place and implemented.
- Promoting an organisational culture which affords all employees the development opportunities which will enable them to achieve their optimal levels of career development in the course of their employment with the group, while recognising the diversity of the society within which the group conducts its business.

The PR&T scope of responsibilities is detailed in the terms of reference of the committee and is reviewed and approved annually by the board.

EXECUTIVE REMUNERATION REVIEWS

The PR&T committee reviews the remuneration of the GCEO, the executive committee members and the CEOs of the operating business units. In reviewing the remuneration of senior executives, the committee considers market benchmarks, internal pay parity, individual performance, as well as the guidelines on remuneration provided by the DPE for SOCs. The group works on a total cost of employment approach, where there is a guaranteed fixed pay (which includes contribution to retirement fund, medical aid, etc.) and a variable pay portion, which is at risk. Annual increases take place on 1 April of each year.

The committee also reviews and recommends to the board for approval the variable pay pay-out based on the policy. Variable pay is a portion of employees' salary package that is set aside and is at risk. Payment of variable pay is linked to the performance of the company and the individual, in that only those who meet or exceed set performance targets, qualify.

The following amounts were either paid or accrued to the executive directors and executive committee members during the year:

Executive directors and executive committee members	Fixed remuneration	Variable pay	Contributions made	2012 Total	2011 Total
	R'000	R'000	R'000	R'000	R'000
Mr R Saloojee *	706	473	104	1 283	-
Mr MT Sadik #	3 488	1 640	346	5 474	5 829
Mr F Mhlontlo	2 789	1 578	322	4 689	4 468
Mr JV Morris	1 892	980	237	3 109	2 948
Maj Gen (Ret) OA Schür	1 394	694	125	2 213	2 107
Mr ZN Ntshepe	1 395	682	154	2 249	2 038
Ms TP Mushungwa ^	1 126	-	130	1 256	2 135
Total	**12 790**	**6 047**	**1 418**	**20 255**	**19 525**

* *Appointed on 16 January 2012*
\# *Resigned on 31 January 2012*
^ *Resigned on 31 December 2011*

NON-EXECUTIVE DIRECTORS' REMUNERATION

Market benchmarks and the DPE's remuneration guidelines are used to determine and make recommendations on non-executive directors' fees and presented at the AGM for approval by the shareholder. As indicated above, for the past three financial years the shareholder has not approved any increases for the non-executive directors.

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

Non-executive directors	2012 R'000	2011 R'000
Mr NR Kunene (chairman) [2]	602	248
Dr SP Sibisi (chairman) [1]	179	715
Mr G Badela [3]	257	-
Ms S Chaba [1]	97	276
Dr GC Cruywagen	338	294
Mr LC Jones [1]	62	238
Ms MJ Janse van Rensburg	417	161
Prof T Marwala	229	123
Ms Z Mathenjwa [3]	186	-
Mr NJ Motseki [3]	187	-
Mr M Msimang [3]	236	-
Mr BF Ngwenya [3]	348	-
Prof SM Nkomo [3]	308	-
Adv Ntshikila [3]	206	-
Ms B Paledi	435	151
Mr M Ratshimbilani [3]	192	-
Ms S Sebotsa [3]	72	-
Ms CC Mulder [4]	-	86
Dr BG Halse [5]	-	54
Mr MS Phalatse [4]	-	58
Mr CML Savage [4]	-	71
Ms T Seretse [4]	-	72
Mr NR Boqo [6]	-	15
Total	**4 351**	**2 562**

[1] *Resigned on 6 July 2011*
[2] *Appointed as chairman on 6 July 2011*
[3] *Appointed on 6 July 2011*
[4] *Resigned on 27 August 2010*
[5] *Donated his director's emoluments to DTA, resigned 27 August 2010*
[6] *External independent member of the group audit and risk committee – resigned 31 January 2011*

The notable increase in the amount paid to the non-executive directors can be attributed to the following:

- The number of non-executive directors was increased from nine to fourteen.
- Two board inductions, one conducted by the company and the other by the shareholder representative.
- Numerous nomination committee meetings i.t.o. appointment of the new GCEO.
- Numerous ad-hoc committee meetings to address specific issues, e.g. Hoefyster production order, and meetings with some stakeholders, e.g. between Armscor and Denel boards.

EXECUTIVE COMMITTEE

This committee is chaired by the GCEO and comprises members of the executive team as detailed on pages 48 to 51. 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, review of the group's values, safety performance, operation and monitoring financial performance. This committee meets on a monthly basis.

The following meetings took place during the year:

	Exco meetings								Manco meeting
Exco members	Total	Special 8 April 2011	Special 3 May 2011	15 June 2011	29 August 2011	3 October 2011	Special 29 November 2011	Special 30 January 2012	19 March 2012
Mr R Saloojee ^	1/1	-	-	-	-	-	-	√	√
Mr MT Sadik ˙	6/6	√	√	√	√	√	√	-	-
Mr F Mhlontlo	6/7	√	√	√	√	√	A	√	A
Mr JV Morris	7/7	√	√	√	√	√	√	√	√
Ms TP Mushungwa +	5/6	A	√	√	√	√	√	-	-
Mr VM Ngidi ^	1/1	-	-	-	-	-	-	√	√
Mr ZN Ntshepe	5/7	√	√	√	√	A	A	√	√
Maj Gen (Ret) OA Schür	5/7	√	√	√	√	√	A	A	√

A Apology
˙ Resigned on 31 January 2012
^ Appointed on 1 April 2012
+ Resigned on 31 December 2011

RISK MANAGEMENT

The group has a sound system of internal controls, designed in terms of policies and guidelines. The board reviews and improves the risk strategy and policies formulated by the executive directors and senior management. Management is accountable to the board and has established a system of internal controls to manage the significant group risks. This system assists the board in discharging its responsibility to ensure effective management of the wide ranges of risks associated with Denel operations.

Further details on the effectiveness of risk governance can be found under the *risk governance section* of this report.

CODE OF ETHICS

Denel has a code of ethics which underpins the business practice to which all employees and suppliers are expected to adhere. The policy outlines conflicts of interest, the prevention of dissemination of company information, the acceptance of donations and gifts, and protection of the intellectual property and patent rights of the company. The policy outlines the disciplinary action (including dismissal or prosecution) that will be taken in the event of any contravention.

The group also has an independently-operated whistle-blowing mechanism. This is a fraud hotline operated by an independent organisation. Matters that have been reported through this mechanism are investigated and reported to the group audit and risk committee. Depending on the nature of allegations, some of the matters end up being reported to appropriate law enforcement agencies, e.g. the SAPS. For more detail on fraud and related issues that arose during the year under review, refer to page 78.

INTERNAL CONTROL

Responsibility for the system of internal control within Denel rests with the board. Responsibility for establishing and operating detailed control procedures lies with the CEO of each business unit. The directors review the effectiveness of the group's internal controls on a regular basis. A management representation letter is signed off by the relevant management confirming that the business unit has maintained a sound internal control environment, including operational and financial controls and risk management processes.

INTERNAL AUDIT

The function of internal audit is to appraise the adequacy and effectiveness of Denel's systems of internal control. This function has been outsourced to one of the big four audit firms. There is an internal audit charter in place that regulates the interaction between the group, management, internal auditors and the board.

The internal auditors report administratively to the GCEO and have unrestricted access to the chairman of the group audit and risk committee and to the chairman of the board of directors. Given that the internal auditors have unrestricted access to board members and regularly report to the audit and risk committee, the board is confident that the internal auditors have discharged their duties fully and independently in terms of the internal audit charter.

BUSINESS UNITS

All of Denel's subsidiaries are subject to Denel group policies, governance and financial control. They comply with the PFMA, the Companies Act and other applicable legislation, including that of foreign countries.

Each business unit is accountable to the GCEO through a performance agreement. This is further enhanced by them being included in the executive committee and various forums that are held monthly, where not only operational matters are discussed, but also topics that are relevant to executive management and the leaders of the group.

SUSTAINABILITY

The board recognises that Denel operates in the aerospace and defence industry, and plays a central role in high-end technology and globalisation. Today, this means not only addressing questions of transportation and national security, but also sustainability. From supply chain efficiency to green IT, Denel has an opportunity to increase not only the sustainability of its industry, but also the economic value that it creates. The technologies to completely eliminate emissions and wastes may not be available for some time, but Denel can and will work with its customers to take substantive actions toward sustainability and high performance today.

In recognising that sustainability efforts are no different than other business initiatives, Denel has aligned its strategy prioritising sustainability in terms of its ability to create measurable contributions to objectives, such as growth, cost reduction and the management of the business.

STAKEHOLDER ENGAGEMENT

Denel has a programme of improving relations with its main stakeholders. This includes reviewing a stakeholder engagement plan and holding meetings as part of a communication forum. The stakeholder engagements, including the achievements and challenges, are provided in the *stakeholder engagements section* of this report.

RISK GOVERNANCE

OVERVIEW

Denel is part of the global defence supply chain which must continuously respond to global developments and trends. Through the corporate planning process, both the internal and external environments are assessed for their impact on competition, regulation and trade conditions. Denel's business portfolio includes development and production of high-end technology products and services over long periods. The long-term nature of the projects and changing technologies increase project and financial risks. Denel implemented a financial and programme risk management process to respond to these risks. The group's initiatives to strengthen the balance sheet are discussed in the GCEO's and the directors' report. Denel has implemented a fraud prevention policy and has placed business ethics at the centre of corporate governance. Denel has published corporate values and policies that promote ethical business conduct. More information is provided on page 05.

RISK MANAGEMENT PROCESS

Denel has a formal risk management process that identifies, assesses and responds to risks. The board is accountable for risk management. The review of the effectiveness of the group's internal controls and risk management has been delegated to the audit and risk committee. Executive management is responsible for management of risks and reports to the audit and risk committee and ultimately to the board. Denel has integrated risk management in the corporate planning process as illustrated below.

Risk process	Actions	Output	Frequency
Risk identification is initiated during the corporate and business planning process, and continuously monitored. Sensitivity analysis and budget stress-testing, programme management reviews and monthly budget and operational effectiveness reviews are conducted.	Denel board validates business plans per product portfolio and consolidated five year corporate plan, in relation to the Shareholder's Compact	Consolidated group corporate plan	Annually
	Business units' boards approve their specific annual to five-year plan based on their business strategy to meet the corporate plan requirements	Unit business plans and budgets	Annually
	Denel executive integrates business information, assumptions, conduct sensitivity analysis and budget stress-testing analysis	Consolidated group forecast and update	Quarterly
	Corporate review of major programmes	Programme performance and risk update	Quarterly
	Business unit performance reviews	Financial and operational performance update	Monthly

In order to assist the committees and the board, independent reviews are undertaken by internal and external audit, which forms the group's process for evaluating the effectiveness of internal controls and risk management.

Key risk factors

Denel's risks arise from trends in the global, national and local arena and specifically, economic, social, political, technological and regulatory factors and internal activities. A process of risk identification, risk assessment, risk response and monitoring is followed to manage risks. Risks are reported to the board, the shareholders and stakeholders by the executive management.

The responsibility for identification, assessment, mitigation, reporting and monitoring of risk rests with management. The audit and risk committee reports the findings of its reviews to the board. The following are the most significant risks identified by the organisation.

SIGNIFICANT RISKS

	Risk	Management process and status
1	Weak solvency and liquidity position impacting sustainability.	The group is implementing funding strategies, improving cash flow management and profitability. The group is also in discussions with the shareholder regarding a suitable funding model.
2	The level of local defence spend impacting local order cover and securing of key local orders, some of which are critical for the retention and development of strategic defence capabilities within Denel.	Positioning Denel as the prime contractor for the SANDF and leveraging its technologies for diversification. The group is improving international business, thereby reducing dependence on local market.
3	Not timeously meeting employment equity targets and skills continuity in light of age profile and labour mobility.	Leadership, skills development, succession plans, mentoring programmes and diversity management are strategies used for skills transfer and development, and transformation.
4	Global events impacting the international orders, delaying orders, and increasing competition.	The balancing of local and export revenue, growing revenue by accessing new markets. Optimising cost base and building capabilities to remain competitive.
5	Programme management risks resulting from development and delivery of programmes over long periods, increase the technical and schedule risks, resulting in cost overruns.	The group implements a programme management process, which ensures quality delivery on time and within budgets. Reviews by technical, contract management and contract accounting staff are also undertaken to monitor performance.
6	Developing and agreeing contracts that adequately address key risks and ensure mutually beneficial business relationships.	Processes are implemented to standardise contract terms and ensure mitigation of contract risk exposures.
7	Organisational culture not supporting an entrepreneurial and commercial oriented strategy.	HR and transformation strategy that caters for leadership development and change management aimed at addressing organisational culture. Operational management empowered to make quick decisions and encourages innovation.
8	Aligning expectations of stakeholders and defence strategy to meet long-term business objectives.	Engagements with industry and the DoD&MV, and participation in the Defence Review process. Regular meetings with stakeholders, community outreach programmes and media relations.
9	Concentration of risk resulting from dependence on few main customers and/or markets.	At group level the business portfolio is adequately diversified. The group is leveraging technologies for new products and markets as part of diversification.

OPERATIONAL RISK CONTROL SYSTEMS

An update on occupational health and safety (OHS), environmental responsibility, anti-fraud and corruption and compliance programmes are provided in the relevant sections of this *sustainability and governance section*.

FRAUD PREVENTION AND ANTI-CORRUPTION

Denel encourages honesty and integrity among employees and implemented policies throughout the group as part of the system of internal control aimed at preventing fraud and corruption. Procurement is a significant cost driver in the organisation and a high risk area for fraud and conflicts of interest. Denel has a transparent procurement process to reduce the risk of fraud and conflicts of interest through segregation of duties, declaration of interests and delegated authority for approval of procurement transactions, among other things. The decision to embark on a closed or open tender is regulated through thresholds set by management. Committees are formed to develop specifications and tenders are evaluated and adjudicated by different committees before they are awarded. These committees comprise of employees with the relevant experience and expertise to ensure correct decision making and segregation of duties. Employees participating in the procurement process, are required to declare their interests and are prohibited from disclosing confidential information pertaining to the procurement process to prevent collusion with suppliers. The tender management process is illustrated in the table below.

PROCUREMENT GOVERNANCE PROCESS			
Steps	**Procurement stage**	**Approval criteria**	**Approval authority**
1	Requirements identification	Based on work plan and budget	Process owner/task leader
2	Requirements approval	Based on approved work plan and budget	Section/departmental manager
3	Specification development	Based on technical project requirements and procurement policy	Expert/expert team
4	Specification approval	Based on technical requirements	Section/departmental manager
5	Tender invitations	At least three quotations for transactions **below** set threshold. Advertising in three newspapers for transactions **above** set threshold	Procurement officer/manager
6	Tenders opening	Tender document	Multi-disciplinary team led by procurement officer
7	Tender evaluation	Approved specification	Multi-disciplinary team involving the procurement officer
8	Adjudication	Approved specification and procurement policy	Multi-disciplinary team
9	Award	Depending on the value of a tender	Board Executive committee Adjudication committee

FRAUD DETECTION

Denel implemented data analytics to complement fraud detection controls, which entails collating and analysing organisational data, and developing trends to identify discrepancies. Data was collated on revenue, expenditure, spend per supplier and master files, payroll, fixed assets and employee interests among other things at the units with most significant procurement volumes. This data was analysed and emerging risks relating to payment of suppliers and potential conflicts of interest were proactively mitigated.

WHISTLE-BLOWING

Denel has a confidential hotline through which fraudulent and unethical behaviour may be reported. The hotline is independently operated and all stakeholders are encouraged to make use of it. Nineteen cases of alleged unethical behaviour were recorded. The cases were assessed and it was found that the majority were not fraud-related but general complaints, which were handled through the human resources processes.

COMPLIANCE

LEGAL AND REGULATORY FRAMEWORK

Denel's compliance programme takes cognisance of the constitutional requirements of the SA and pertinent international protocols. The Companies Act and the PFMA form the foundation of Denel's corporate governance process. Other key legislation includes aviation, conventional arms control, explosives, firearms control, occupational health and safety, and environmental management legislation. Denel has developed processes and procedures to integrate legislative and regulatory requirements in the business.

The compliance system entails continuous identification and monitoring of laws and regulations impacting the business and updating policies to ensure compliance. Executive management are accountable to the board for legal and regulatory compliance.

Denel has developed customised checklists for applicable legislation and key policies for management self-assessment. Compliance has also been included in the three-year rolling internal audit plan. Internal audit reviews compliance with the Companies Act, PFMA and Income Tax Act as part of year-end process and no significant non-compliances have been reported.

Health, safety, environmental and quality management, as well as OEM accreditation systems are implemented as part of the compliance programme. For an update refer to the environmental responsibility and OHS sections on pages 85 to 86, and 99 respectively.

CONVENTIONAL ARMS CONTROL

Defence products incorporate controlled items which are regulated by various laws and as such are subject to export regulations in terms of the National Conventional Arms Control Act (NCACA) and various international protocols. Conventional arms control is at the centre of the compliance programme to ensure that development, manufacturing and servicing permits, as well as marketing, contracting, import and export permits are obtained and proper authorisation for controlled items is followed. Nothing significant has come to the attention of the board during the year under review suggesting possible non-compliance.

LEGAL AND REGULATORY AWARENESS

As part of heightening legal and regulatory compliance among employees and senior management, Denel hosted an internal legal and regulatory compliance conference addressed by various experts including leaders in the arms control environment.

PEOPLE MANAGEMENT

OVERVIEW

Denel's human resources (HR) strategies are intended to ensure that the group's business objectives and plans are achieved. Denel is implementing a skills attraction, development and retention strategy that is aimed at ensuring that the group is able to attract, develop and retain the best talent to enable the business to deliver on its mandate.

Denel is committed to creating an enabling and engaging environment for all in which employees feel they can realise their full potential. Denel recognises the critical importance of leadership in creating an effective environment to work in and as such continues to invest heavily in leadership and management development.

Priority areas for the year were:

- Improving the group's B-BBEE rating.
- Creating an enabling working environment including regularly conducting a group-wide organisation climate survey to determine progress and set new benchmarks and targets.
- To ensure a dynamic leadership by taking senior management through a leadership and management development programme.
- To ensure continuity of skills at all levels through strengthening of talent management and succession planning.

EMPLOYEE PERFORMANCE

WORKPLACE PROFILE

As at 31 March 2012, Denel had a total workforce of 4 716 (2010/11: 4 716) employed at the various business units (excluding those employed by associates) of which 3 509 (2010/11: 3 597) are employed on a permanent basis and 1 207 (2010/11: 1 119) on fixed-term contract.

The table below illustrates the employee profile per job category:

Job categories	2012 Black*	2012 White	2011 Black*	2011 White
Executive management	27	46	27	46
Management	76	236	68	255
Engineers	72	309	64	301
Scientists	3	19	3	22
Technicians	168	513	158	526
Artisans	1 154	918	1 068	965
Configuration	7	34	5	36
IT personnel	24	24	24	27
Financial	24	45	26	49
Marketing	7	10	5	11
HR	6	8	6	8
Trainers	4	26	5	21
Security	57	19	54	21
Administrative	184	290	179	293
Secretarial	28	46	22	52
Trainees	116	19	144	23
General workers	140	10	139	7
Other	40	7	43	13
Total	**2 137**	**2 579**	**2 040**	**2 676**
Total strength	**4 716**		**4 716**	

* *Black refers to African, Coloured and Indian*

The table below illustrates **appointments** by race and gender i.r.o. employees:

	2012 Number	2012 %	2011 Number	2011 %
Black* male	459	62.4	367	51.3
Black* female	88	12.0	207	29.0
White male	144	19.6	84	11.7
White female	45	6.0	57	8.0
Total	736	100	715	100

* *Black refers to African, Coloured and Indian*

The table below illustrates **terminations** by race and gender i.r.o. employees:

	2012 Number	2012 %	2011 Number	2011 %
Black* male	419	56.9	374	42.1
Black* female	87	11.8	133	15.0
White male	177	24.0	300	33.7
White female	53	7.3	82	9.2
Total	736	100	889	100

* *Black refers to African, Coloured and Indian*

REMUNERATION, REWARD AND RECOGNITION

Denel's remuneration strategy is geared towards enhancing performance and retaining best talent. Denel operates on a total cost to company principle with both a guaranteed portion and a risk portion based on achievement of company targets and individual performance.

Denel has several other mechanisms to ensure excellence and successes are recognised and celebrated. This is aimed at ensuring employees feel valued as well as encouraged to put in, extra effort. These vary from team and individual units, from month celebrations to small token payments used as immediate reinforcement of good performance.

An average payroll movement of 6.5% was approved by the Denel board and implemented with effect from 1 April 2012.

EMPLOYEE BENEFITS

- Denel Medical Benefit Trust

  The Denel medical benefit fund was established by Denel as a vehicle to ensure the company was able to meet its promise, under the old Denel pension fund scheme, of subsidising the medical aid contributions of qualifying retired employees. The employees eligible for this post-retirement medical subsidy are current and former employees who were appointed before 1 April 2000.

  Denel has offered a buy-out of the liability to qualifying beneficiaries. 80% active members and 56% of pensioners respectively have taken up the offer, with an overall acceptance of 68%.

  Denel is currently investigating the best mutually satisfactory way of finally relieving itself of this liability.

- Denel Retirement Fund

  Denel restructured its defined benefit fund during the prior year and now operates a single defined contribution fund, the Denel Retirement Fund (DenRet). DenRet is a separate unit managed by a board of trustees. The fund is in a sound financial position.

POSITIVE EMPLOYEE RELATIONS

Denel is committed to sound employee relations and engages with employees and unions at both unit and group level. Denel has formal relationships with four recognised trade unions, namely UASA, NUMSA, SAEWA and Solidarity, representing employees at various units as tabulated below.

Profile of **union representation** in Denel:

	2012		2011	
Unions	Number	%	Number	%
Solidarity	941	20.0	785	16.6
NUMSA	924	20.0	832	17.6
SAEWA	32	0.7	32	0.7
UASA	949	20.0	1 143	24.3
Total	**2 846**	**60.7**	**2 792**	**59.2**
Total strength	**4 716**		**4 716**	

EMPLOYEE WELL-BEING

Employee well-being forms an important pillar of Denel's HR strategy. The group's focus is on occupational health, physical and psychological well-being as well as HIV/Aids awareness. All units have a risk-based occupational health programme delivered through an in/out-sourced occupational health clinic. Psychological counselling is provided mostly through Independent Counselling and Advisory Services (ICAS), an outsourced provider. Some units operate an in-sourced psychological counselling service. The group provides related well-being benefits through the medical aid scheme which is a condition of employment. Denel also hosts wellness days to encourage employees to take responsibility for their health and living healthy lifestyles. Voluntary HIV counselling and testing is also encouraged during the wellness days.

SKILLS DEVELOPMENT

- Employee skills development initiatives

  Denel operates in a cutting-edge technology environment and as a result it takes long time to gain the required level of competency. Skills development is therefore critical to sustain the skills required to meet Denel's needs. Denel spent R49m (2010/11: R35m) on employee skills development and learning programmes for the current financial year.

- Schools outreach programme

  Denel skills development includes schools outreach programmes to improve Maths and Science results, as a contribution to an increased pool of engineering candidates. The programme involves conducting Saturday classes in maths and science to grade 8 to 12 pupils by a combination of professional teachers and Denel engineers.

- Artisan training

  DTA is responsible for artisan training in Denel. The academy also provides highly sought-after artisan training to local and foreign industries and enrols approximately 250 apprentices per year. Training is offered for the following:
  - Aircraft-related disciplines: Avionicians, electricians, radiotricians, instrument mechanics, structural workers and mechanics.
  - Manufacturing and engineering disciplines: Electricians, fitter and turners, machine-tool millwrights, tool and jig makers, turner, machinists and welders.

Denel has committed to the National Skills Accord to train 600 artisans by 2014. In addition, the DTA offers SACAA-certified courses and several other advanced courses.

PMP situated to the west of Pretoria provides MERSETA accredited courses for apprentices to complete artisanship within three years, as well as certain TETA, SASSETA and ABET training courses. In total 913 participants attended various training initiatives during the year.

- Bursaries

  As part of its skills attraction strategy, Denel offers bursaries to about 30 engineering students per year. The students are not only supported financially, but also with mentoring and assistance with projects. Upon completion of their studies 90% of these students are absorbed by Denel. The engineering graduates are then taken through Denel`s engineering academy of learning for further development.

- Engineering academy of learning

  The engineering academy of learning provides Denel's new engineering graduates with a twelve-month intensive training programme, which is registered with ISETT SETA, with interns registered with ECSA. Each intern is allocated a mentor.

- Collaboration with tertiary institutions

  Denel continues to strengthen relationships with universities and FETs. The group participates in various university career days and is looking at expanding this programme. Denel's engineers are involved with universities as examiners and moderators, and assist with project topics.

- Women in engineering

  Denel sponsors SAWomEng to contribute in efforts to increase the number of women taking up engineering as a career. Denel also provides opportunities for vacation work for female engineering students. This is part of the group's efforts to increase gender diversity when it comes to engineers.

- Employee study assistance

  Denel grants study loans and bursaries to employees who wish to further their studies in fields related to their careers and which complement their jobs. This ensures that employees are continually improving their skills and staying abreast with the latest technologies and developments in their fields. Various courses have been identified as part of personal development plans (PDPs) and specific job requirements are also provided.

- Leadership development

  Denel introduced a development programme to meet the group's leadership development requirements. To date all executives have gone through intensive psychometric assessments and received individual reports, which identified areas of development. The Unisa SBL-Denel leadership and management development programme was launched in June 2011 to address required competencies for all management levels in the organisation. In addition to the above, other executive programmes, including coaching and mentoring, are employed.

- Succession planning

  Denel is responding to a challenge caused by skills mobility and workforce dynamics by developing and implementing a succession planning framework that ensures the creation of a pool of candidates for leadership roles in the organisation. The framework also addresses the transformation requirements of the group.

TRANSFORMATION

OVERVIEW

Transformation is a top priority in Denel and is focussed on three pillars, namely B-BBEE, employment equity and skills development. Denel underwent an employment equity review by the Department of Labour where the employment equity plan was approved. The plan is being implemented and monitored continuously.

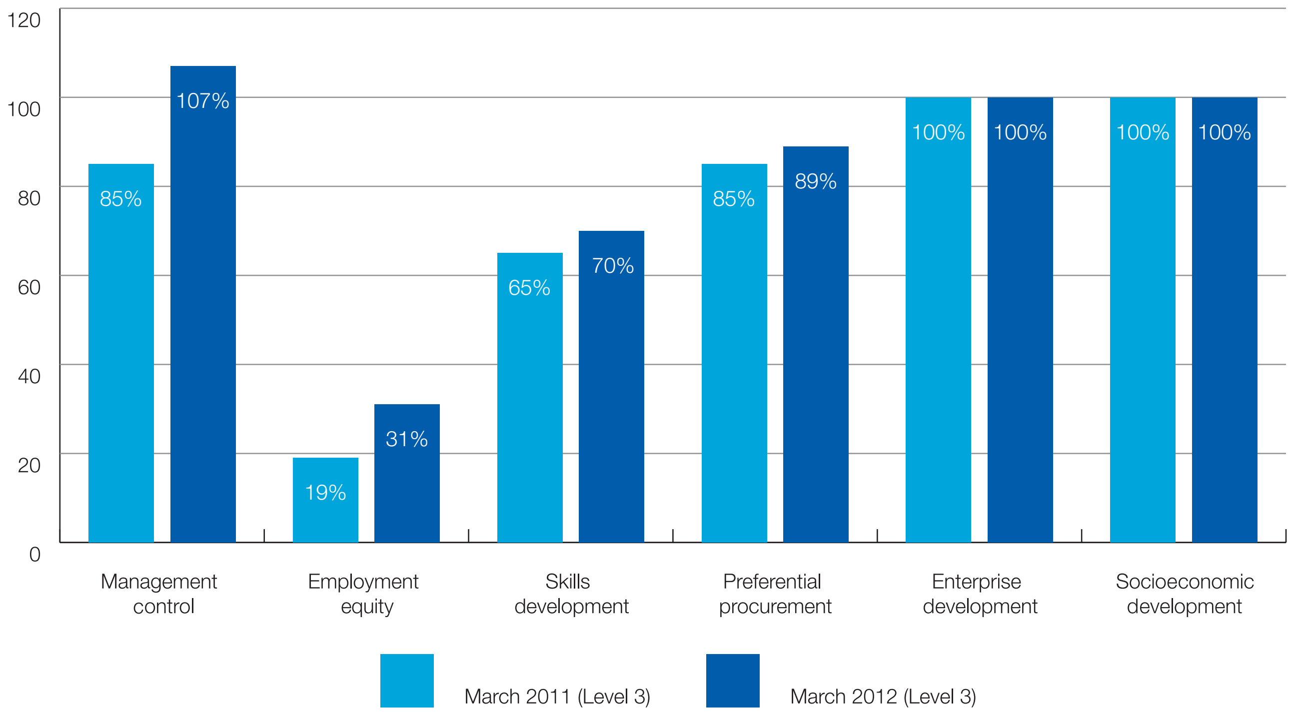
Denel conducted an organisation climate survey and action plans will be put in place for identified areas of improvement. The group has strengthened its transformation committees with unit and group executive committees being responsible for giving strategic direction and ensuring that transformation is achieved. Transformation forms part of the CEOs' performance contract.

Denel conducted training of transformation committee members to skill and update them on legislative matters to enable them to play a more effective role in the organisation.

DENEL`S PERFORMANCE ON B-BBEE

The chart below reflects Denel`s latest B-BBEE score. The group has been evaluated by EmpowerLogic verification agency, which is an accredited agency.

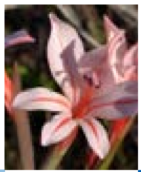
B-BBEE SCORECARD



Denel is proud to have retained a level 3 B-BBEE status for the year under review demonstrating our commitment to transformation. Although Denel maintained the level 3 status the score has improved. The graph above illustrates Denel's improved in all aspects of the scorecard with an overall score of 82% (2010/11: 76%). Our B-BBEE procurement recognition has also improved to 138% compared to 110% in the previous year. Employment equity, however, remains a challenge despite having improved significantly from the previous year. This improvement could be attributed to initiatives put in place to meet our transformation objectives. Following a review by the Department of Labour, Denel developed a five-year employment equity (EE) plan which the department has approved and is being implemented.

ENVIRONMENTAL RESPONSIBILITY





OVERVIEW

Denel aims to be a responsible manufacturer implementing business processes that ensure environmental sustainability. Denel has a sustainability policy and strategy, and procedures are in place to prevent and monitor environmental impacts. Audits are conducted to ensure compliance and corrective actions are taken. Each business unit bears the responsibility for sound environmental management by setting and achieving objectives, goals and targets. This complies with environmental legislation and protocols, to ensure that business operations meet minimum standards, and is revised on a regular basis. Employees are trained and resources made available to ensure legal and other requirements are met. Environmental committees are appointed to ensure EMS is implemented. Facilitating effective environmental management usually forms part of the function of the SHE committee.

The following key environmental objectives have been set within the group:

- Protection of species and habitats, and the conservation of biodiversity and natural resources.
- Protection of the environment against disturbance, deterioration, poisoning or destruction as a result of human activity and structures.
- Provision of a healthy working environment for its personnel.

MANAGING MATERIAL ENVIRONMENTAL IMPACTS

1. ENVIRONMENTAL POLICIES AND MANAGEMENT SYSTEMS

Denel has an environmental management policy (EMP) based on the principles of ISO 14001 that provide guidelines and outline the minimum requirements for each business unit. The policy focuses on the continual improvement of environmental management activities and operations to minimise waste, prevention of pollution and care for the environment at unit level.

Departmental managers and environmental officers ensure that monitoring and controls are in place, conduct and execute internal audits to assess compliance, identify shortcomings and implement remedial action on an on-going basis. All incidents and potential incidents of non-compliance are logged, investigated, evaluated and corrective actions taken.

Environmental groups and communities are engaged to establish relationships and promote an understanding of Denel's contribution towards sound environmental practice. These engagements also provide a platform for Denel to receive, document and respond to communications from external interested parties.

Information on environmental management systems (EMS) in place at Denel's core businesses:

Core businesses	EMS (ISO 14001 certified)	Most recent external audit conducted	Planned re-certified	Comments
PMP	ISO 14001 certified (2003)	May 2010	November 2012	No major findings
OTR	ISO 14001 certified (October 2000) EMS Legal	May 2011 surveillance system audit October 2010 legal audit	September 2012	No major findings No major findings
Denel Dynamics	ISO 14001 certified (March 2009)	November 2011	March 2012	Only minor findings were made during the audit – all were successfully closed
DAv	EMS is aligned to ISO 14001 requirements	16 January 2012	Initial certification planned for July/August 2012	ISO 14001 certification planned for 2012
DLS	ISO 14001 certified (2004) OHSAS 18001 certified (May 2010)	1st surveillance audit was successfully conducted in May 2011	May 2012 (2nd surveillance audit)	None
Mechem	ISO 14001 certified (November 2012)	1st surveillance audit DEKRA (November 2011)	2nd surveillance audit DEKRA (October 2012)	Planned IMS audit for project June 2012, conducted by DEKRA
DAe	Implementing ISO 14001	N/a	N/a	In process

2. EMPLOYEE TRAINING AND AWARENESS

Denel provides specific environmental orientation, training and environmental awareness programmes. Through these programmes employees are made aware of the importance of conformity to applicable policies and procedures, the requirements of the SHE management system, its significant environmental aspects, the related impacts associated with their work, and the roles and responsibilities each one has in respect of the environment.

Some core businesses	Training and awareness programmes
OTR	Environmental training courses, including environmental awareness for contractors, clients and OTR personnel, water sewerage works, snake handling course, fire-fighting procedures during testing activities.
PMP	Environmental training courses, including environmental awareness, training on system audits, including legal compliance and incident investigation, safety and health and environmental management awareness actions training, safe use in handling and disposal of hazardous chemical substances including lead and noise, emergency preparedness and response.
DAv	Environmental awareness training has been presented on various environmental topics including hazard awareness, spill containment, hazardous chemical substances and waste management, recycling and ISO 14001 awareness.
DLS	Health, environment and safety awareness is conducted on a monthly basis; the topics differ from alien plants and malaria to hazardous chemicals, asbestos, energy use, water use and many others.
Deniprop	SHE awareness and waste management training were presented.
Mechem	SHE awareness training was presented.
DAe	Environmental training courses, including environmental awareness, chemical/oil handling, storage and disposal were presented.

3. WASTE PRACTICES AND RECYCLING

Waste management is a key focus area for Denel. The "3 Rs" (reduce, re-use and recycle) are the pillars of waste management within the group. Denel has implemented initiatives for hazardous and general waste management that include:

- On-going monitoring of processes, including internal and external waste audits.
- All aspects of waste management are documented and encompass requirements in respect of the collection, sorting and sale, or safe disposal of waste generated on the sites. Certificates of "safe disposal" are retained on record with regards to hazardous waste disposal.
- Monitoring and analysis of effluent waste discharged into municipal sewers take place at DAe and DLS before permits are granted, authorising its release into the storm water and sewer systems.
- Deniprop has established waste management policies to educate and support contractors and suppliers on waste management. Use and safe disposal of chemical substances, domestic and hazardous waste, as well as recyclable waste are handled in a responsible manner with reputable waste removal suppliers contracted. Material safety data sheet (MSDS) are available for all chemical substances used within Deniprop.
- Approximately 50% of PMP's input materials are recycled and re-used in the production process. Catchment dams have been constructed to ensure that in the unlikely event of an effluent spillage, the waste water will not contaminate the natural water run-off. All hazardous substances are contained in environmentally-safe storage and handling facilities which are reviewed on a regular basis.
- Dynamics' recycling of e-waste continues with the replacement of old CRT monitors with energy-efficient flat- screen monitors. Recycling scrap metal and metal shavings has increased significantly during the past financial year. Recycling of all types of waste reached a record of 58.4 tons last year. Paper usage has decreased by 36% since 2009. As part of an on-going environmental awareness campaign, a project was launched inviting employees to bring recyclable waste from home. Special collection containers were placed at the two main entrances and to date, approximately 150 tons of waste has been diverted from being dumped at land fill sites.
- Mechem has implemented an environmental management safe working procedures (SWP) which enables the unit to conserve resources and reduce waste generation. Mechem employees are responsible for minimising the quantity of waste and maximising recycling of paper and all other recyclables.
- OTR has a detailed waste and pollution management plan, which also forms part of and is a requirement for the ISO 14001 EMS. Waste practices include collecting neon tubes, kitchen fat, motor coolant, magnetic data tapes, etc.
- DAe manages the effluent treatment plant for the surface treatment processes. A total of 9 046kL of industrial effluent was treated during this reporting period. DAe recycles around 80% of its water utilised from the surface treatment production process.

Details of the group's hazardous and general waste disposed and recycled are provided in the table below.

Type of waste	Weight		Disposal/recycling method and comments
	2012	2011	
Hazardous waste disposed (tons)	162	62	Disposed of at special landfills, where waste is treated in an environment friendly manner. Safe disposal certificates are received.
Hazardous waste disposed (kL)	1 722	1 450	Special landfills where the waste is treated in an environment friendly manner. Relates to soluble cutting oil and water only. Safe disposal certificates are received from waste contractors.
Hazardous waste recycled (tons)	710	308	Recycled as part of environmental management.
Hazardous waste recycled (kL)	101	75	Recycled as part of environmental management.
Non-hazardous disposed (tons) Non-hazardous disposed (kL)	2 825 2 952	448 552	Disposed of at normal landfills by waste removal companies or own transport.
Non-hazardous waste recycled (tons)	5 331	10 294	Includes paper, plastics, tins and metal shavings which are sold to recycling companies or dealers.

4. ENERGY AND WATER USE

Energy and water management plans are in place in several areas throughout the group to manage and promote the efficient use of these resources. The group has voluntarily joined the ECS Pledge, which is in collaboration with DPE. This is a drive to reduce our annual energy consumption by 10% through the implementation of a voluntary energy conservation scheme. The challenge for the group is to reduce electricity consumption, while simultaneously growing its revenue.

ENERGY

Deniprop is responsible for the implementation of energy efficiency plans for the group and creating awareness among commercial clients. Various energy initiatives are implemented throughout the group to reduce overall consumption. Specific initiatives undertaken include the following:

- Group-wide campaigns conducted to raise awareness and encourage conservation and responsible use of water and energy.
- A study conducted on all sites to investigate additional ways to save electricity. The study provided information regarding electricity savings and gave indications of how to improve current installations. The audit report further made recommendations for replacement of outdated equipment with more energy-efficient ones. Due to the financial impact of the recommendations not all actions could be implemented immediately. Denel has prioritised recommendations and developed specific plans to address the recommendations. All commercial tenants are consistently sensitised on energy efficiency and are requested to implement the energy savings as recommended in the report.

The following is a summary of further actions that have already been implemented to save energy:

- Various lighting initiatives, e.g. switching off of lights during day-time where adequate natural lighting is available and during night-time when facilities are vacated, installation of energy-efficient lamps and automation of switches to conform to energy efficiency prescripts.
- Improving air-conditioning efficiency and installing ceiling insulation in air-conditioned areas.
- Metering of energy consumption.
- Sensitising employees to get into the habit of "switching off when not in use".
- Phasing out of old CRT monitors, replaced by more energy-efficient flat-screen monitors and replacing old technology photocopiers.
- Rescheduling of peak demand operations (like brass foundry at Pretoria West and furnaces at DAe) with preferential rates negotiated due to avoidance of peak-demand periods.
- All hot water geysers have been adjusted to 60°C and fitted with geyser blankets.

WATER

- Water is a scarce resource in SA, and Denel recognises the need to use it wisely and sparingly. Fully functional water management plans are in place and are reviewed on a regular basis to ensure that these plans are still viable.
- Borehole water is used for gardens and backup fire protection systems.
- At OTR maintenance of the aged water supply system remains a major challenge. Many of the pipelines, pumps, valves and other water supply infrastructure are coming to the end of their economic life and needs to be replaced over the next five years. A capital project to sequentially replace these systems from 2013 has been identified.
- Regular operational meetings with the various users to discuss water conservation and mechanisms to save water. Leaks are repaired.
- PMP and DAe have also implemented water management systems for the water treatment plant to monitor water usage.
- PMP has water catchment dams contributing to recycling of water.

Business unit/campus	Water consumed mL		Amount spent Rm		Electricity consumed MwH		Amount spent Rm	
	2012	2011	2012	2011	2012	2011	2012	2011
Irene	41	95	1	1	16	18	8	8
Kempton Park	328	352	4	4	35	36	27	27
Lyttelton	83	75	1	1	8	9	6	5
PMP	365	365	3	3	28	28	17	17
Houwteq	23	6	1	1	1	2	1	1
Mechem	35	35	-	-	2	2	-	-
OTR	85	88	-	-	6	6	3	3
Total	**960**	**1 016**	**10**	**10**	**96**	**101**	**62**	**61**

During the year the group experienced some challenges in its efforts to reduce electricity and water consumption due to growing activities, high cost of replacing water supply infrastructure and internal effluent controls.

5. ENVIRONMENTAL IMPACTS OF PRODUCTS AND SERVICES

Environmental impact assessments are being carried out on all significant products and services with mitigation actions undertaken to limit environmental impacts. The group EMP adopts an integrated environmental management (IEM) approach, and environmental consideration is integrated into all stages of the development process. As part of operating procedures all hazardous substances are contained in environmentally-safe storage and handling facilities. Storage practices are reviewed on an on-going basis.

Examples of initiatives to mitigate environmental impacts of products and services

Details of initiatives to mitigate environmental impacts	Extent of mitigation and indicator
Operational controls implemented in areas with high significant impacts, e.g. water management plan, hazardous chemical, and storage plan and spillage procedure.	All plans are in place.
Fuel spill contamination bunkers.	Containment of spilled fuel to prevent damaging environment.
A percentage of materials used is recycled.	Different percentages of recycling are achieved, e.g. 70% of paper is recycled at Mechem.
Environmental risk assessments for testing.	Per test, total of 21 ERAs.
The emissions from the spray booth were in excess of the legal limits. This was corrected by the installation of additional filters.	During financial year 2010, emissions were 119mg/m^3 - now they are below 10mg/m^3 and within legal limits.
Testing of UAV engines.	Strict measures were introduced to reduce the noise during UAV engine testing. Testing is now limited to between 08h00 and 16h00 and full-throttle runs are restricted to two minutes maximum. This restriction is strictly adhered to and to date no complaints from our neighbours have been received. A further development is that a newer, quieter engine is being evaluated.
Bulk storage of underground fuel.	The underground fuel storage tanks are nearly 25 years old. In order to timeously detect possible leaks, daily dip-stick readings are taken. In addition, pressure tests on the integrity of the fuel tanks are conducted annually.

6. LAND STEWARDSHIP AND NATURE CONSERVATION

Denel's activities, in particular explosive and chemical-related activities, increase the risk of contamination and pollution of the environment. A decontamination policy was implemented to address these issues. Denel has sizeable tracts of land, where environmental management plans have been implemented to improve the quality of flora and fauna. The impacts of historic operations are mitigated and where applicable land is remediated for future use. Although there has been no formal environmental impact assessments (EIA) conducted by OTR, it is involved as an interested and affected party with two EIAs in its area of operation. These include whale trail, CapeNature and Struis Bay wind energy.

Independent audits and site characterisation studies were conducted to determine the contamination liabilities of each site, and to assess the adequacy of the financial provisions. The latter were raised for contamination liabilities identified and for decommissioning, taking into account the requirements for remediation of industrial facilities within the context of best practice and applicable South African environmental legislation. The costing is based on the requirements to have the properties ready and fit for anticipated future use.

The details of plans and remediation work implemented at contaminated sites are provided below:

Site/Business unit	**Actions taken to rehabilitate, including collaborations with Government and stakeholders, and expected dates of completion**
Deniprop	• Spatial development framework is used to determine levels of cleaning the contaminated areas at the Philippi site. R40m has been set aside for the remediation project in the year under review and R16m has been spent since 2008. • Environmental consultants were contracted to perform environmental audits of the remediation project. • The community consultative forum (CCF) keeps the immediate stakeholders around the Philippi site informed on environmental issues that affect the community.
DAv	• Established and implemented a spillage procedure dedicated to prevent any major spillages which may lead to land contamination. • Processes in line with requirements of ISO 14001 have been established.
Denel Dynamics	• Upgrading of fire alarm system, yearly evacuation exercises and formation of fire-fighting teams. • Fire and chemical spill management plans.
OTR	• Eradication of alien invasive plants on an area of 3 000ha is underway as part of the Department of Environmental Affairs initiative.
PMP	• Game management is done in collaboration with the Gauteng Nature Conservation Department. • Fire management and effective fire protection are done according to requirements and guidelines as set by fire brigade and disaster management plans. • Frequent action is taken to control and eradicate the growth of alien invader and other unwanted plant species. • An independent site audit and contamination assessment confirmed that there is no requirement for decontamination in the context of the Explosives Act.

Denel also plays a role in conserving and promoting the natural environment through the following nature conservation programmes:

- OTR includes various initiatives and works closely with key stakeholders viz. CapeNature, environmentalists and researchers, Overberg Air Force Base, government departments, environmental committees and private initiatives.
- Extensive game management plans are also in place at OTR and PMP which include the capture, relocation, monitoring and culling of game, with inspections of fences and watering points.
- OTR and PMP are involved in rare and endangered species monitoring, including the location, identification and mapping of rare and endangered species to preserve and conserve these from extinction. The clearing of invasive alien vegetation is a challenging and overwhelming task which is labour and capital intensive.
- OTR has a 25km coastline which is ecologically pristine. Access to the coast is restricted and controlled by OTR security, and monitoring patrols are conducted in cooperation with CapeNature which is responsible for managing the marine reserve along the coastline.
- Denel Dynamics is involved in a Luton Valley community project to develop a small environmental conservation area just east of the Irene campus. The project aims to involve and educate schoolchildren on environmental matters.

Spillage procedures and emergency response procedures are in place and are posted on notice boards. Detection systems and controls measures are installed to prevent any accidental spillage and contamination. There were no significant spillages reported during the year.

7. COMPLIANCE WITH LAWS AND LEGISLATION

Compliance with legislation is assessed on a regular basis through audits and management inspections. The intention is not to pay lip service to legislation but to implement a robust compliance management function. Denel's dedicated compliance champions ensure compliance within the units. No fines have been levied or non-monetary sanctions were imposed on Denel for non-compliance with environmental laws and regulations in the current financial year. Details of the group's compliance with legislation are provided in the *compliance section* on page 79.

8. ENVIRONMENTAL PROTECTION AND EXPENDITURES

Other expenditures for the year under review are as follows:

Business unit	Amount spend R'000		Environmental activities that funds were used for
	2012	2011	
Denel Dynamics	128	68	• ISO 14001 surveillance audits and legal compliance audits • Disposal of old, redundant chemicals and empty chemical containers. • Emission and hygiene testing (spray booth, composite facility and the transport grease trap).
OTR	488	693	• Maintaining ISO 14001 certification and all its associated costs to maintain all environmental management systems (these exclude all labour costs). • An alien vegetation management programme. • Game management programme.
PMP	1 625	1 505	• The expenditure shown in the Health and Safety report also includes expenditure associated with the environmental expenditure.
DAv	130	140	• Fuel farm contract and spill bunkers. • Hazardous waste removal.
DLS	323	449	• Hazardous waste removal. • ISO 14001 surveillance audits and legal compliance audits.
Mechem	22	266	• ISO 14001 accreditation costs.
DAe	114	57	• Hazardous waste disposal as a result of chemical surface treatment production process. Not treatable by the effluent treatment plant.

9. FUEL UTILISATION AND SIZE OF FLEET

Business unit	Actual amount of fuel utilised (kL)		Size of fleet (number of vehicles)		Environmental activities that funds were used for
	2012	2011	2012	2011	
DAv	125	102	55	55	Fleet reduced by trip optimisation.
PMP	1 873	1 409	66	102	PMP utilises an integrated approach.
DPS	8	9	9	13	Fleet reduced and maintained to get best efficiency.
DLS	26	22	16	16	Vehicles well maintained.
OTR	209	214	94	100	Assesses its vehicle fleet on an annual basis, to ascertain reduction to a limit before impacts the actual operations of the organisation. They have a daily bus service for personnel, which is more environmental friendly than having hundreds of privately owned vehicles travelling on a daily basis. Mobile electrical generators are utilised during tests.
Denel Dynamics	87	71	23	25	Infrequent transportation of products, other goods and materials does not have a significant impact on the environment. Vehicles are well maintained to ensure the impact on the environment is limited.

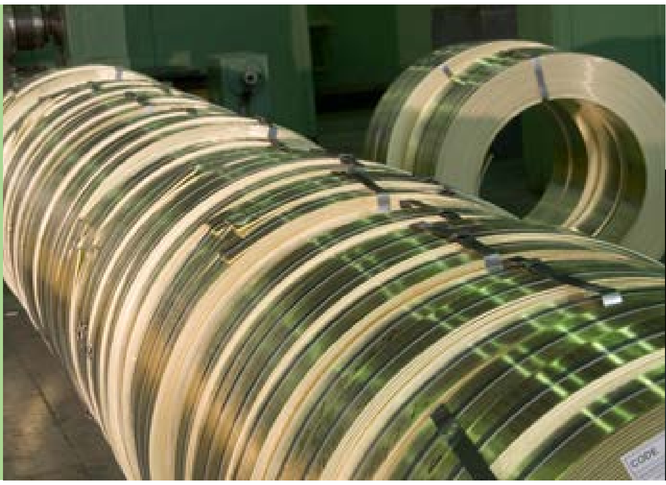
Fuel utilised includes both petrol and diesel.

10.GREENHOUSE GAS EMISSIONS, BY WEIGHT

Denel has commenced with initiatives to reduce greenhouse gas emissions, but this action is still in its infancy stage and we will report as we progress. Denel Dynamics's release of ozone-depleting fumes from the spray paint shop was reduced by 90% and it is now operating within legal limits.

Type of greenhouse gas	Weight/volume of greenhouse gas		Comments
	2012	2011	
Gas nitrogen	263 300	439 710	
Gas LPG 100%	187 376	314 047	
Emissions from the spray booth	<10mg/m^3	<10mg/m^3	Reduction in emissions is due to the installation of additional filters.

SUPPLIER MANAGEMENT



OVERVIEW

Denel has developed a reliable local and international supplier base to underpin its manufacturing capability and support obligations. Denel is committed to the development of local suppliers, with a specific focus on emerging B-BBEE and SMME companies as a direct contribution to national skills development, economic empowerment and business transformation goals set out in company policies.

This approach has guided Denel to focus on the enhancement of core competencies of design, development, qualification, strategic manufacturing and system integration, while engaging the local manufacturing sector for general manufacturing support. Significant volumes of manufacturing and development work are being sub-contracted to a growing pool of local suppliers that include an increasing number of developing SMME and BEE companies as registered and accredited suppliers to the group.

These efforts to enhance local manufacturing have not been limited to the recognised defence sector, hence the search for local manufacturing and service providers has been expanded to include the wider local manufacturing and associated services sector. Denel has impacted on a growing number of local industries as depicted below.

DENEL PROCUREMENT EXPENDITURE

B-BBEE recognised procurement spend				Total spend
Level 1 - 3	Level 4 - 5	Level 6 - 8	Level 9/unrecognised	
Rm	Rm	Rm	Rm	Rm
477	736	252	689	2 154

The targeted development of emerging suppliers remains a key focus area for Denel. This is captured in specific transformation development plans, with the outcome of these endeavours formally audited by internal and external auditors and the B-BBEE verification agency that assesses Denel annually. In line with new guidelines regarding B-BBEE codes of good practice, revised Preferential Procurement Policy Framework Act (PPPFA) imperatives and NGP goals, our focus is on identifying emerging suppliers within small, medium and micro enterprises to become sustainable service providers for a spectrum of general as well as more specific manufacturing capabilities and associated services in partnership with Denel. Further details of the transformation programme are provided on page 80.

Supply chain optimisation was identified as a strategic contributor to improved operational efficiency, as this function is recognised as a key contributor to optimised end-to-end business performance. The primary objectives of supply chain improvements are to reduce cash held in general commodities and raw materials, reduce in inventory holding that is significantly influenced by work in process (also captured under revenue recognition debtors) and the sale of obsolete inventory and general scrap. To achieve these objectives and to ensure the realisation of maximum savings in the execution of all procurement functions, internal supply chain processes and procedures have been refined and reviewed for a third year. Specific attention was given to improve strategic sourcing and shared services to maximise the benefit to be derived from volume procurement.

MANAGING SUPPLIERS

- Policies and procedures

  The Denel group is revising its current policy framework to meet the amended PPPFA, the revised B-BBEE codes of good practice and imperatives defined by the NT within the latitude granted to SOCs by the Minister of Finance. This process is reviewed by the internal and external auditors to ensure compliance, as well as ensuring optimal value is being gained from refined procurement processes.

- Management structures, roles and responsibilities

  To ensure sound governance and accountability, Denel has devolved supply chain processes, including formal delegation and review by multi-disciplinary supply chain committees. Supply chain professionals are contracted for enhanced performance and savings targets to improve operational efficiency. Supply chain managers are responsible for compliance with defence material requirements. Integrated supply chain forums coordinate and report initiatives and share best practices across the group.

- Objectives and targets

  The group has set targets to ensure improved performance as a certified B-BBEE contributor and to measure progress against its transformation programme. Denel has maintained a level 3 contributor status. Further details are provided in the *transformation section* on page 84.

  The following key high-level supply chain initiatives were pursued during the year under review:

  - Embedding an overall supply chain governance framework and associated supply chain strategy based on revised PPPFA guidelines. This was done to optimise the group's procurement costs, improve service delivery and customer satisfaction.
  - Reviewing business unit-level supply chain policies and procedures to comply with revised legislation.

SOCIOECONOMIC DEVELOPMENT

OVERVIEW

Denel acknowledges the role it has to play in contributing to the economic development of the country and as such, embraces its responsibility towards the sustainability of the economic, environmental, and social conditions. Denel's overall aim is to empower, improve and transform the lives of people, who are non-participants in the economy, to be included into the economic mainstream in a sustainable manner.

The group focuses on SED activities that are aligned with its business strategies. The group's three primary focus areas relate to:

- Supporting education programmes to create an awareness of mathematics, science and engineering amongst learners. Such investments ultimately benefit Denel and other companies in SA.
- Enterprise development through monetary and non-monetary contributions to identified exempted and qualifying small enterprise suppliers who demonstrate potential for growth and job creation, and who are aligned to Denel's required supplier base. Comprehensive details of the group's enterprise development practice, and of its performance, are provided in the *economic impact section* of the *sustainability and governance section* on pages 56 to 57.
- Socioeconomic development programmes through monetary and non-monetary contributions to:
  - Develop women, youth, people with disabilities and people living in rural areas.
  - Support community training and skills development for unemployed people, including adult basic education and training.
  - Support arts, cultural or sporting development programmes.

Denel's corporate social and economic development responsibilities extend beyond philanthropy and focus on successful community engagements, with a strong developmental theme. Denel has contributed R28m (2010/11: R20m) on education and non-educational enhancement-related projects in the year under review.

Responding to the country's socioeconomic conditions has provided Denel with opportunities to enhance its brand and promote the group as a caring and good corporate citizen. Denel is proud of the SED contributions it has made during the year under review, despite the financial constraints and challenges experienced.

EDUCATION INITIATIVE AND PROGRAMMES

The aerospace and defence industry is facing a number of challenges with regards to people sustainability:

- An ageing workforce.
- Long development cycle. It takes many years to elevate people to the required experience and skill levels.
- Increased competition for scarce skills. Denel's industry has to compete with consulting houses for the best engineers.
- Schools simply do not produce enough learners with good maths and science passes and the pool of those who pursue engineering as a career is limited.

It is against this background that Denel has adopted a holistic HR management approach to develop its people sustainability programme. The group begins at school level by providing extra maths and science Saturday classes to increase the pool of youngsters achieving good marks in these subjects. The drive is to encourage them to be able to take up engineering as a career. Bursaries are provided to those with the greatest potential by providing them with an intensive internship after successfully completing their engineering degrees. Once they come out of the internship, they are mentored by some world-class engineers within the organisation.

Denel offers apprenticeship bursaries to learners from previously disadvantaged backgrounds every year giving them an opportunity for a decent career and work opportunities. The source for most of our bursary holders is through Denel's youth foundation training programme, schools outreach programmes and shows. During the year under review, our aviation fraternity produced 90 qualified artisans with various aircraft maintenance trades. Denel also offers vacation work to university students who are studying in the engineering field.

SUPPLIER DEVELOPMENT PROGRAMMES

Denel regards small and medium SED as an important business strategy which leads to the creation of effective business partnerships and joint ventures. These enterprises also strengthen local supply chain capacity, enhance distribution networks and open up new markets.

The challenge faced by these companies is that there are limited opportunities to enter into the high technology industry. This is mainly due to lack of access to sufficient capital (core supply areas require large capital investment). There is a limited local technical base in the specific environment in which Denel operates. Low volume, high risk, high cost, challenging schedules and extreme budget constraints make this a difficult market to enter.

Denel has, despite these challenges, been able to identify a supplier falling within the small and medium category, Thuthuka Engineering, as part of its SED strategy. Thuthuka Engineering is a black-owned supplier whose capabilities are able to operate in the core areas of high technology defence-related aerospace business. The company is an electronic (harness/loom) supplier in the local industry. The project is currently being piloted at Denel Dynamics. Denel Dynamics is a highly technical business, specialising in the missiles and UAVS business.

Technical skills transfer is top priority to Denel to enable technology growth into our local industry. In turn this creates jobs - a major strategic requirement from government. With the correct technical knowledge transfer, quality control, and verification inspection skills learned, Thuthuka Engineering will be elevated to become a preferred supplier for all level 1 components under the SED programme. Currently Thuthuka is working with CZO and has shown great progress with loom manufacturing. Denel Dynamics will provide Thuthuka with technical support and skills transfer while personnel work on-site. The programme will be one of Denel's SED contributions in the next two financial years, thus ensuring sustainability towards high-end manufacturing skills transfer. Evaluation will take place ahead of each financial year-end.

BENEFITS OF SED INVESTMENT OPPORTUNITY

- Denel will inject a contribution of R700k into the project for this year.
- Support will be provided on workmanship training, because a quality assurance review is required to develop the supplier to meet Denel Dynamics' military workmanship standards.
- Business growth will be the product of Thuthuka's strengthened technical capabilities, enabling them to increase earnings by taking on more complex work.
- Thuthuka will also be able to market their services with increased stature.

BENEFITS TO DENEL

- Leads to the creation of effective strategic business partnerships and joint ventures.
- Preferential procurement targets enhanced through SED.
- Reduces costs by sourcing locally, and lowering transportation costs.
- Creates sustainability and profitability.

SOCIOECONOMIC DEVELOPMENT KEY INITIATIVES

With so many socioeconomic challenges affecting many South Africans, Denel has taken a stand to play an active role in the supporting projects and events aimed at redressing these challenges.

- **Internet facilities:** DISS established an internet facility in mid-2009 at the Air Defence Artillery School at the Kimberley army base. The internet café is utilised by Army personnel in the field of education and research on technical projects. Due to the benefits experienced with this project, DISS will continue its maintenance of the internet facility. 80% of the users of the internet café are from previously disadvantaged backgrounds.
- **Empowering women:** In celebration of Women's day, DAv, DPS and other Denel business units based on the Kempton Park campus took the opportunity to treat the women to an elegant workshop with Chata Romano themed "The Royal Makeover". The workshop focused on helping women change their lives by changing their image. The talk ranged from taking care of their hair, body and style. Chata is a well-known image consultant and has written a book called "Change your image, change your life". Each delegate at the event received a copy to keep and use on the journey to change their image.
- **Working with the less fortunate:** DPS, together with its main customer SAAF, joined forces by donating a fridge and a stove to Tshedimosetso youth network. This is a community home-based care centre, which aims at strengthening support for people affected and living with HIV/Aids. They are also working with orphans and vulnerable children's health lifestyle as well as offering counselling for treatment compliance and palliative care.
- **Nelson Mandela Day:** DISS joined Denel corporate office's initiative to celebrate Mandela's birthday by participating in the distribution of food and clothing at a school in Olievenhoutbosch. Employees have shown a keen interest to get more involved in this activity in 2012.
- **Community upliftment:** Personnel of OTR enthusiastically contributed in kind and expertise to uplift the community. Projects launched included the upgrading of the playground of the Nompumelelo Preschool in Bredasdorp, the painting of the Struisies Pre-school building in Struisbaai and urgent maintenance work needed at Ons Huis old age home in Bredasdorp. Furthermore the residents of Ons Huis were

taken on an excursion which included a bus tour, a visit to the museum and refreshments.

- **Supporting education initiatives and programmes:** OTRs primary involvement with education is by means of financial support to two local primary schools in the Overberg region, namely Waenhuiskrantz Primary and Struisbaai Primary. The financial support is a partial payment of an additional teacher's salary for each of the two schools. The result from this support is that approximately 400 primary learners at these schools gain the benefit of improving their literacy and numeracy skills.
- **Learner assistance:** In 2008 Inasham Cele won the Eskom expo for young scientists' competition that was sponsored by Denel Aviation. This gifted learner has since become an orphan and was struggling to continue with his schooling. Due to his performance at the 2008 Expo, DAv saw it fit to assist him and during the year under review the company sponsored him to complete Grade 12.
- **Chief of Air Force coffee table book:** DAv is a proud sponsor of the CAF coffee table book that showcases the aviation industry while taking an in-depth look at the role played by the SAAF. During the launch of the book some funds were raised through the auctioning of aircraft canvases and the proceeds were donated to a charity organisation. The year under review saw DAv take this initiative a step further by creating an abridged version of the book which have since been distributed to schools in previously disadvantaged communities so that they can also learn more about the industry and the career opportunities it has to offer.
- Denel Industrial Properties (Deniprop) provides **free rental** space to the DESTO for training and youth development initiatives at a cost of R84k per month. The school trained 300 ABET level 3 students during the year in various disciplines.
- **"Make 'em Fly" campaign:** DAe in partnership with Kid's Haven, a shelter for homeless children launched a campaign which involves, donations, educating their youth group and promoting maths and science, executive members acting as mentors for the children, and children being exposed to opportunities and events at DAe thus educating them on the aviation industry.
- **Saturday school programme:** DAv has adopted Reiger Park Secondary School, and its employees teach maths and science to help improve performance in these subjects. DAv also supports a similar initiative run by the East Rand community in Springs. The year under review saw DAv and DTA collaborate with the University of Pretoria who provided students to assist with the teaching of maths and science at the project's winter school camp.
- **Youth development programme (YDP):** DAv is the main sponsor of the Defence Industry YDP which has become an integral component of the Africa Aerospace and Defence (AAD) show to create awareness for career opportunities in the in the aviation and defence industry. Over the years, the youth initiative has grown into a formal programme and an asset to the AAD in terms of marketing the industry as employer of choice to the youth, educators, parents and the broader public.
- **Supporting handicapped children:** PMP provides financial support for operational costs as well as contributing to the building of a library and sports facilities to the Zodwa School for handicapped children in Atteridgeville.

LOCAL INDUSTRY 'CLUSTER DEVELOPMENT'

Less than 20% of SA's tooling demands are met locally, forcing industry to import tools from Germany and China, and leaving it vulnerable to servicing needs and breakdowns. This is according to Dirk van Dyk, CEO of the National Tooling Initiative Programme (NTIP), a public-private partnership between the Tool Making Association of SA and the DTI. SA needs an estimated 1 000 to 2 000 tool-makers a year. Denel ventured into an excellent new initiative in September 2011 with a long-term view to sustaining our workshop with future artisans while developing its SED strategy.

As a SOC, Denel is acutely aware of its responsibility as a good corporate citizen, particularly in the areas of social and economic development.

The tool, die and mould making (TDM) sector allows companies in this industry to earn BEE credits in the ED category for assisting in training artisans, as well as company improvement and development activities. Denel seized this opportunity to apply for the approval of a concession based on a skills development pilot project to assist in the rehabilitation of the TDM industry. Fifteen students will be trained by the NTIP (eight months of theory and practical modules per annum) and by Denel (four months on the job training per annum) for three years for level one to three TDM apprenticeships. The annual spend per student is R90k. The total cost for the entire duration of the programme is R4m from 2012 to 2014. Qualified artisans will then be deployed to the SMMEs associated with Denel supply cluster. These SMMEs will be repositioned through business improvement interventions by the NTIP to perform at the level required by Denel and according to world-class standards.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OCCUPATIONAL HEALTH AND SAFETY

OVERVIEW

Denel has a legal and moral obligation to ensure a healthy and safe work environment. Occupational safety is an important aspect of sustainability and contributes positively to the attainment of the UN Millennium Goals. Denel implemented systems to achieve the group's objective of a safe and healthy work environment. Risk assessments, pre-employment, exit and periodic medical examinations were conducted. Through training and communication Denel raised safety awareness among employees. In line with statutory requirements, occupational health and safety committees are in place to ensure involvement of employees and management in addressing pertinent issues. Denel has appointed responsible persons in terms of the Occupational Health and Safety Act to ensure that legal requirements are met.

Material issues relating to occupational health and safety are:

- Occupational health and safety system's performance
- Medical examinations
- Occupational health and safety training and awareness

OCCUPATIONAL HEALTH AND SAFETY SYSTEM AND PERFORMANCE

To ensure a safe working environment, safety performance is measured in terms of Lost Time Injury Frequency Rate (LTIFR) taking into account incidents, accidents and hours worked. The LTIFR target of less than 1 is set for all units to enable benchmarking of occupational health and safety performance of individual units. A comparative representation of the performance of the individual business units against this target for the last two years is summarised in the following table:

SAFETY SYSTEMS AND PERFORMANCE

		Target: LTIFR	
Business units	**Management system**	**Actual 2012**	**Actual 2011**
DAv	Aligned to OHSAS 18001 system, certification during 2011	0.78	0.88
DLS	Based on legal and regulatory requirements	0	0.92
DAe [1]	Based on legal and regulatory requirements	1.02	0.77
Denel Dynamics	Aligned to OHSAS 18001	0.14	0
Mechem	Based on legal requirements	0	0
OTR	Aligned to OHSAS 18001	0	0.7
PMP	OSHAS 18001 certified	0.27	0.48
Deniprop [1]	Based on legal requirements	1.83	0.92

[1] *DAe and Deniprop experienced lost time due to minor incidents and actions have been taken to prevent recurrence.*

MEDICAL EXAMINATIONS

Denel has established occupational health centres operated by qualified occupational health and medical practitioners to conduct pre-employment, exit and medical examinations in order to assess the health of employees, especially those involved in high-risk occupations. Procedures undertaken during the year under review are tabulated on the following page:

Procedures undertaken during the year under review are tabulated below:

	Number of employees examined							
	Mechem	DAv	DLS	PMP	OTR	Dynamics	DAe	Deniprop
Pre-employment and exit medical examinations	12	140	107	346	15	212	150	5
Periodic medical examinations	24	1 098	188	342	-	217	209	31
Biological monitoring	24	33	34	86	7	30	104	-
Audiometric (hearing) tests	-	46	290	807	-	44	95	5

OCCUPATIONAL HEALTH AND SAFETY TRAINING AND AWARENESS

Safe work practices, routine health and safety induction and specific job-related safety training are provided to all employees.

This has contributed positively to safety awareness at the various units. Details of training provided during the year are tabulated below.

	Number of employees trained per business unit							
Training type offered	Mechem	DAv	DLS	PMP	OTR	Denel Dynamics	DAe	Deniprop
Health and safety induction	49	-	-	53	14	21	130	5
Hazardous chemical substances	5	13	-	205	-	32	23	-
Material safety data sheets	10	-	-	205	-	-	-	-
Spill kit	4	-	-	-	-	-	-	-
Scaffolding	-	-	-	-	-	-	-	-
Safety representatives	3	8	-	4	-	18	7	4
Hazard identification and risk assessments	3	-	-	5	-	-	-	-
Explosives areas	-	-	-	230	-	-	-	-
Legal training for supervisors	1		-	-	-	-	7	-
First aid personnel	1	3	-	89	-	32	-	1
Fire fighters	4	20	181	129	50	12	32	41
Emergency team members	4	-	-	129	5	-	-	-
Incident investigators	4	32	-	4	-	-	-	-
Crane and forklift operators	6	7	-	73	55	49	47	14
Lead training	-	-	-	-	-	-	-	-
Noise-induced hearing loss	1	192	-	-	-	70	-	-
Vessels under pressure	-	-	-	-	-	-	-	-

GRI CONTENT INDEX

√ = fully complied with X = not complied with ◊ = partially complied with

Aspect	No.	GRI G3 indicator	2012 rating	2011 rating	2010 rating	Annual report reference
Sustainability profile						
Strategy and analysis	1.1	Statement from the GCEO and Chairman	√	√	√	Chairman's report, group chief executive officer's report
	1.2	Description of key impacts, risks and opportunities	√	√	√	Sustainability and governance section - Risk governance - Economic impact - Business unit overview
Organisational profile	2.1	Name of organisation	√	√	√	Information service - Contact information
	2.2	Primary brands, products, and/or services	√	√	√	Group overview - Nature of business Business unit overview
	2.3	Operational structure of the organisation	√	√	√	Group overview - Organisational structure
	2.4	Location of organisation's headquarters	√	√	√	Information service - Contact information
	2.5	Number of countries where the organisation operates	◊	◊	◊	Group overview - Nature of business - Economic impact - Business unit overview
	2.6	Nature of ownership and legal form	√	√	√	Group overview Cons.AFS - notes
	2.7	Markets served	◊	◊	◊	Group overview - Nature of business - Economic impact - Business unit overview
	2.8	Scale of reporting organisation	√	√	√	Group overview - Organisational structure - Business unit overview
	2.9	Significant changes during the reporting period, regarding size, structure and ownership	√	√	√	Group chief executive officer's report
	2.10	Awards received in the reporting period	√	√	◊	Sustainability and governance section Business review section - key achievements
Report profile	3.1	Reporting period for information provided	√	√	√	Business review section Business unit overview
	3.2	Date of most recent previous report (if any)	√	√	√	Business review section
	3.3	Reporting cycle	√	√	√	Business review section
	3.4	Contact point for questions regarding the report or its contents	√	√	√	Information service - Contact information

Aspect	No.	GRI G3 indicator	2012 rating	2011 rating	2010 rating	Annual report reference
Report scope and boundary	3.5	Process for defining report content	√	√	√	Sustainability and governance section - Material sustainability issues
	3.6	Boundary of the report	√	√	√	Sustainability and governance section - Sustainability
	3.7	Limitations on the scope or boundary of the report	√	√	√	Sustainability and governance section - Sustainability - Material sustainability issues
	3.8	Basis for reporting on joint ventures, subsidiaries, leased facilities, etc.	√	√	√	Sustainability and governance section - Sustainability
	3.9	Data measurement techniques and the basis of calculations	√	√	√	Sustainability and governance section - Sustainability - Material sustainability issues
	3.10	Explanation of the effect of any restatements of information provided in earlier reports	n/a	n/a	n/a	Sustainability and governance section - Sustainability
	3.11	Significant changes from previous reporting periods in the scope, boundary, or measurement methods	n/a	n/a	n/a	Sustainability and governance section - Sustainability
GRI content index	3.12	Table identifying the location of the standard disclosures in the report	√	√	√	GRI content index
Assurance	3.13	Policy and current practice with regard to seeking external assurance for the report	◊	◊	◊	Sustainability and governance section - Sustainability - Material sustainability issues

Aspect	No.	GRI G3 indicator	2012 rating	2011 rating	2010 rating	Annual report reference
Governance, commitments and engagement	4.1	Governance structure of the organisation	√	√	√	Sustainability and governance section - Corporate governance report
	4.2	Whether the chairman of the highest governance body is also an executive officer	√	√	√	Sustainability and governance section - Corporate governance report
	4.3	The number of members of the highest governance body who are independent and/or non-executive members	√	√	√	Sustainability and governance section - Corporate governance report
	4.4	Shareholder and employee recommendations or direction to the highest governance body	√	◊	◊	Sustainability and governance section - Corporate governance report - Stakeholder engagements - Risk governance
	4.5	Linkage between compensation for members of the board, senior managers, executives and the organisation's triple-bottom line performance	√	√	√	Sustainability and governance section - Corporate governance report
	4.6	Processes and highest governance body to ensure conflicts of interest are avoided	√	√	◊	Sustainability and governance section - Corporate governance report
	4.7	Process for determining the qualifications and expertise of the members of the board	√	√	√	Sustainability and governance section - Corporate governance report
	4.8	Statements of mission or values, codes of conduct and principles	√	√	√	Group overview - Strategic objectives, vision and values
	4.9	Procedures of the board for overseeing the organisation's identification and management of economic, environmental, and social performance	√	√	√	Sustainability and governance section - Corporate governance report - Sustainability
	4.10	Processes for evaluating the board's own performance	√	√	√	Sustainability and governance section - Corporate governance report
Commitments to external initiatives	4.11	Explanation of whether and how the precautionary approach or principle is addressed by the organisation	√	√	√	Sustainability and governance section
	4.12	Externally developed economic, environmental, and social charters and principles to which the organisation subscribes or endorses	√	√	√	Sustainability and governance section
	4.13	Memberships in associations and/or national/international advocacy organisations	√	√	√	Sustainability and governance section - Environmental responsibility - Risk governance - Occupational health and safety
Stakeholder engagement	4.14	Lists of stakeholder groups engaged by the organisation	√	√	√	Sustainability and governance section - Stakeholder engagement
	4.15	Basis for identification and selection of stakeholders with whom to engage	√	√	√	Sustainability and governance section - Stakeholder engagement
	4.16	Approaches to stakeholder engagement	√	√	√	Sustainability and governance section - Stakeholder engagement
	4.17	Key topics and concerns that have been raised through stakeholder engagement	√	√	√	Sustainability and governance section - Stakeholder engagement

Aspect	No.	GRI G3 indicator	2012 rating	2011 rating	2010 rating	Annual report reference
Economic indicators						
Economic performance	EC1	Direct economic value generated and distributed	√	√	√	Sustainability and governance section - Economic impact - Value added statement
	EC3	Coverage of the organisation's defined benefit plan obligations	√	√	√	Note 34 to the consolidated annual financial statements
	EC4	Significant financial assistance received from the South African Government	√	√	√	Group chief executive officer's and Chairmans report Directors' report
Market presence	EC6	Policy, practices, and proportion of spending on locally-based suppliers	√	√	◊	Sustainability and governance section - Supplier management - Transformation
	EC7	Procedures for local hiring and proportion of senior management hired from the local community at locations of significant operation	√	√	◊	Sustainability and governance section - People management
Indirect economic impact	EC8	Development and impact of infrastructure investments and services for public benefit	√	√	√	Sustainability and governance section - Socioeconomic development - Economic impact
	EC9	Significant indirect economic impacts	√	√	√	Sustainability and governance section - Economic impacts - Socioeconomic development
Social indicators						
Employment	LA1	Total workforce by employment type, employment contract, and region	◊	◊	◊	Sustainability and governance section - People management
	LA2	Total number and rate of employee turnover by age group, gender and region	◊	◊	◊	Sustainability and governance section - People management
	LA3	Benefits provided to full-time employees that are not provided to part-time or temporary employees	√	√	X	Sustainability and governance section - People management
Labour/ management relations	LA4	Percentage of employees covered by collective bargaining agreements	√	√	√	Sustainability and governance section - People management
	LA5	Minimum notice periods regarding operational changes	√	√	◊	Sustainability and governance section - People management
Occupational health and safety	LA7	Rates of injury, occupational diseases, lost days, and absenteeism, and number of work-related fatalities by region	√	√	◊	Sustainability and governance section - Occupational health and safety
	LA8	Education, training, counselling, prevention, and risk-control programmes in place to assist workforce members, their families, or community members regarding serious diseases	√	√	√	Sustainability and governance section - People management - Occupational health and safety

Aspect	No.	GRI G3 indicator	2012 rating	2011 rating	2010 rating	Annual report reference
Training and education	LA10	Total training spend by employee category	√	◊	√	Sustainability and governance section - People management
	LA11	Programmes for skills management and lifelong learning	√	◊	X	Sustainability and governance section - People management
	LA12	Percentage of employees receiving regular performance and career development reviews	√	√	X	Sustainability and governance section - People management
Diversity and opportunity	LA13	Composition of governance bodies and breakdown of employees per category according to gender, age group, minority group membership, and other indicators of diversity	◊	◊	√	Sustainability and governance section - People management
Freedom of association and collective bargaining	HR5	Operations identified in which the right to exercise freedom of association and collective bargaining may be at significant risk, and actions taken to support these rights	n/a	n/a	n/a	There are no operations within the Denel group in which the right to exercise freedom of association and collective bargaining may be at risk
Child labour	HR6	Operations identified as having significant risk for incidents of child labour	n/a	n/a	n/a	Denel does not use child labour
Forced and compulsory labour	HR7	Operations identified as having significant risk for incidents of forced or compulsory labour, and measures taken to contribute to the elimination of forced or compulsory labour	n/a	n/a	n/a	There are no incidents of forced or compulsory labour within the Denel group
Community	SO1	Nature, scope and effectiveness of any programmes and practices that assess and manage the impacts of operations on communities	√	√	√	Sustainability and governance section - Stakeholder engagements - Socioeconomic development
Corruption	SO2	Percentage and total number of business units analysed for risks related to corruption	◊	◊	◊	Sustainability and governance section - Risk governance
	SO3	Percentage of employees trained in organisation's anti-corruption policies and procedures	√	√	◊	Sustainability and governance section - Risk governance
	SO4	Actions taken in response to incidents of corruption	√	◊	◊	Sustainability and governance section - Risk governance - Stakeholder engagement
Public policy	SO5	Public policy positions and participation in public policy development and lobbying	◊	◊	◊	Sustainability and governance section - Risk governance
Anti-competitive behaviour	SO7	Total number of legal actions for anti-competitive behaviour, anti-trust or monopoly practices	n/a	X	X	Sustainability and governance section - Risk governance - Environmental responsibility
Compliance	SO8	Monetary value of significant fines and total number of nonmonetary sanctions for noncompliance with laws and regulations	√	√	X	Sustainability and governance section - Risk governance - Environmental responsibility
Customer health and safety	PR1	Life-cycle stages in which health and safety impacts of products and services are assessed for improvement	◊	◊	√	Sustainability and governance section - Supplier Management - Environmental responsibility
	PR2	Number of incidents of noncompliance with regulations	◊	◊	X	Sustainability and governance section - Supplier Management

Aspect	No.	GRI G3 indicator	2012 rating	2011 rating	2010 rating	Annual report reference
Products and services	PR3	Type of product and service information required by procedures and percentage of significant products and services subject to information requirements	◊	◊	◊	Sustainability and governance section - Supplier Management - Risk governance
	PR5	Practices related to customer satisfaction	◊	◊	◊	Sustainability and governance section - Supplier Management
Environmental indicators						
Materials	EN2	Percentage of materials used that are recycled input materials	√	◊	X	Sustainability and governance section - Environmental responsibility
Energy	EN3	Direct energy consumption	√	√	◊	Sustainability and governance section - Environmental responsibility
	EN6	Initiatives to provide energy-efficient based products and services and reductions in energy requirements	√	◊	X	Sustainability and governance section - Environmental responsibility
Water	EN8	Total water consumption	√	√	X	Sustainability and governance section - Environmental responsibility
Biodiversity	EN11	Location and size of land owned, leased, managed in, or adjacent to, protected areas and areas of high biodiversity value outside protected areas	◊	◊	◊	Sustainability and governance section - Environmental responsibility
Emissions, effluents and waste	EN12	Description of significant impacts of activities, products and services on biodiversity in protected areas	◊	◊	◊	Sustainability and governance section - Environmental responsibility
	EN22	Total weight of waste by type and disposal method	√	√	√	Sustainability and governance section - Environmental responsibility
Products and services	EN26	Initiatives to mitigate environmental impacts of products and services, and extent of impact mitigation	√	√	◊	Sustainability and governance section - Environmental responsibility
Compliance	EN28	Monetary value of significant fines and the number of non-monetary sanctions for non-compliance with environmental laws and regulations	√	√	X	Sustainability and governance section - Environmental responsibility
Overall	EN30	Total environmental protection expenditures, by type	√	√	X	Sustainability and governance section - Environmental responsibility

CONSOLIDATED **ANNUAL FINANCIAL STATEMENTS**

REPORT OF THE GROUP AUDIT AND RISK COMMITTEE

The group audit and risk committee reports that it has adopted appropriate formal terms of reference as its audit and risk committee charter and has discharged its responsibilities as contained therein.

In the conduct of its duties, the committee has, inter alia, reviewed:

- The effectiveness of internal controls.
- The risk areas of the units' operations covered in the scope of internal and external audits.
- The adequacy, reliability and accuracy of financial information provided by management.
- Accounting and audit concerns identified through internal and external audits.
- The units' compliance with legal and regulatory provisions.
- The effectiveness of the internal audit function.
- The activities of the internal audit function, including its annual audit plan, coordination with the external auditors, the reports of significant investigations and the responses of management to specific recommendations.
- The independence and objectivity of the external auditors.

The committee is of the opinion that the internal accounting controls are adequate to ensure that the 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.

Other than as reported in the directors' report, nothing significant has come to the attention of the committee indicating any material breakdown in the functioning of these controls, procedures and systems during the period under review. The committee is satisfied that the consolidated annual financial statements are based on appropriate accounting policies, supported by reasonable and prudent judgments and estimates.

The committee has evaluated the annual financial statements of the Denel group and Denel SOC Ltd for the year ended 31 March 2012 and based on the information provided to it, considers that they comply in all material respects with the requirements of the South African Companies Act, the PFMA and IFRS.

Furthermore, the group audit and risk committee concurs that the adoption of the going concern assumption in the preparation of the annual financial statements is appropriate. At its meeting on 13 June 2012, the committee recommended the adoption of the consolidated annual financial statements by the board.

Martie v Rensburg

Martie Janse van Rensburg
Chairman of the group audit and risk committee

INDEPENDENT AUDITORS' REPORT TO PARLIAMENT

INDEPENDENT AUDITORS' REPORT TO PARLIAMENT ON THE FINANCIAL STATEMENTS OF DENEL SOC LTD FOR THE YEAR ENDED 31 MARCH 2012

REPORT ON THE FINANCIAL STATEMENTS

INTRODUCTION

We have audited the consolidated and separate annual financial statements of Denel SOC Limited, which comprise the consolidated and separate statements of financial position as at 31 March 2012, and the consolidated and separate statements of comprehensive income, consolidated and separate statements of changes in equity and consolidated and separate statements of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes, and *directors' report*, as set out on pages 113 to 199.

ACCOUNTING AUTHORITY'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The company's directors which constitutes the accounting authority, is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and the requirements of the Companies Act and the Public Finance Management Act of South Africa, and for such internal control as the accounting authority determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Public Audit Act of South Africa, the General Notice issued in terms thereof and International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the unit's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the unit's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

OPINION

In our opinion, the annual financial statements present fairly, in all material respects, the consolidated and separate financial position of Denel SOC Ltd as at 31 March 2012, and its consolidated and separate financial performance and consolidated and separate cash flows for the year then ended in accordance with International Financial Reporting Standards, and the requirements of the Companies Act and Public Finance Management Act of South Africa.

EMPHASIS OF MATTER

Without qualifying our opinion, we draw attention to the fact although the group earned a total comprehensive profit of R41m (2010/11: R111m), there are conditions and other matters that are set forth in the *directors' report* on pages 113 to 120, which indicates the existence of material uncertainties, which may cause doubt about the group's ability to continue as a going concern.

OTHER REPORTS REQUIRED BY THE COMPANIES ACT

As part of our audit of the financial statements for the year ended 31 March 2012, we have read the audit committee's report and the company secretary's certificate for the purpose of identifying whether there are material inconsistencies between these reports and the audited financial statements. These reports are the responsibility of the respective preparers. Based on reading these reports we have not identified material inconsistencies between these reports and the audited financial statements. However, we have not audited these reports and accordingly do not express an opinion on these reports.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

PAA REQUIREMENTS

In accordance with the PAA and the General Notice issued in terms thereof, we report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

PREDETERMINED OBJECTIVES

We performed procedures to obtain evidence about the usefulness and reliability of the information in the *Shareholder's Compact* key performance indicators as set out on page 25 of the annual report. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury Framework for managing programme performance information.

The reliability of the information in respect of the selected objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

There were no material findings on the shareholder compact key performance indicators concerning the usefulness and reliability of the information.

COMPLIANCE WITH LAWS AND REGULATIONS

We performed procedures to obtain evidence that the unit has complied with applicable laws and regulations regarding financial matters, financial management and other related matters.

We did not identify any instances of material non-compliance with specific matters in key applicable laws and regulations as set out in the General Notice issued in terms of the PAA.

INTERNAL CONTROL

We considered internal control relevant to our audit of the financial statements, shareholder compact key performance indicators and compliance with laws and regulations. We did not identify any deficiencies in internal control that we considered sufficiently significant for inclusion in this report.

Ernst & Young Inc.

Ernst & Young Inc.
Director – Louis Pieter van Breda
Registered Auditor
Chartered Accountant (SA)
Wanderers Office Park
52 Corlett Drive
Illovo
Johannesburg
19 June 2012

DIRECTORS' REPORT

STATEMENT OF RESPONSIBILITY

The board of directors is pleased to present its report and the audited consolidated annual financial statements for the year ended 31 March 2012.

The directors are responsible for the integrity and fair presentation of the annual financial statements of Denel SOC Ltd and its subsidiaries. The *consolidated annual financial statements* presented on pages 113 to 199 have been prepared in accordance with IFRS, the South African Companies Act No. 71 of 2008 and the PFMA No. 1 of 1999. These 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 annual report and are responsible for both its accuracy and consistency.

The directors are satisfied that at the time of approving the annual financial statements it is appropriate to use the going concern basis in preparing these financial statements. In arriving at this conclusion, the directors considered the cash position at 31 March 2012, the cash requirements for at least twelve months from that date and the borrowings facilities available. The going concern is discussed in more detail on page 118 to 119 of this report.

The external auditors are responsible for independently auditing and reporting on the annual financial statements. The report of the independent auditors appears on pages 111 to 112.

During the year under review, the directors retained full and effective control over the group and monitored management in implementing the approved plans and strategies.

The directors are of the opinion that the 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 2012.

The *consolidated annual financial statements* of Denel SOC Ltd for the year ended 31 March 2012, as set out on pages 113 to 199, have been prepared under the supervision of Mr Fikile Mhlontlo CA(SA) and were approved by the board on 19 June 2012 in terms of the Companies Act and the PFMA and are signed on their behalf by:

Zoli NR Kunene
Chairman of the Board

Riaz Saloojee
Group Chief Executive Officer

CERTIFICATE BY COMPANY SECRETARY

The company secretary certifies that the company (Reg. No. 1992/001337/30) has lodged with the Companies and Intellectual Property Commission (from 1 May 2011) all such returns as are required of a public company in terms of the Companies Act, No.71 of 2008 and that all such returns are true, correct and up to date.

Elizabeth Africa
Group Company Secretary

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 associates. The nature of the group's business is described in the *nature of business* on page 04, as well as in the *business units' overview* section on pages 30 to 41 of this report.

FINANCIAL AND OPERATIONS REVIEW

The results for the financial year can be analysed as below:

	Defence, security and certification		DAe		Once-off items		Group	
	2012	2011	2012	2011	2012	2011	2012	2011
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Revenue	3 308	2 971	260	281	-	-	3 568	3 252
Cost of sales	(2 510)	(2 268)	(221)	(327)	25	(154)	(2 706)	(2 749)
Gross profit	798	703	39	(46)	25	(154)	862	503
Other income	93	43	11	37	116	463	196	543
Operating expenditure	**(834)**	**(731)**	**(124)**	**(214)**	**-**	**48**	**(958)**	**(897)**
Share in results of associates	33	81	-	-	-	-	33	81
Profit/(loss) before interest and tax (EBIT)	**90**	**96**	**(74)**	**(223)**	**141**	**357**	**133**	**230**
Net interest	(80)	(106)	(4)	(14)	-	-	(84)	(120)
Taxation expense	(8)	1	-	-	-	-	(8)	1
Net profit/(loss)	**2**	**(9)**	**(78)**	**(237)**	**141**	**357**	**41**	**111**

Denel has posted a profit of R41m (2010/11: R111m), marginal profits for two consecutive years. The decrease in profit from the prior year is mainly due to the fact that the prior year figures included an accounting gain of R463m arising from the restructuring of a pension fund. The group is still in a loss position if one considers the quality of earnings, i.e. results include certain once-off items. However, the group improved its loss before once-off items to R100m (2010/11: R246m). The financial performance for the year is mainly attributable to the following:

- Increase in revenue by R316m (10%) from the prior year, mainly as a result of more MRO services, aerostructures and landmine clearance work undertaken during the year.
- Decrease in other income by R347m as certain items accounted for in the prior results that have not recurred.
- Reduction of the share of earnings from associates by R48m to R33m due to a decrease in profits.
- Reduction in net interest costs by R36m due to lower interest rates and better working capital management.

The financial results continue to be negatively impacted by DAe losses and interest on borrowings. Progress was made during the year in restructuring DAe, resulting in reduction of financial loss from R237m to R78m. DAe will continue to post losses for the next four to five years before breakeven is achieved.

Net equity improved to R695m (2010/11: R654m), after taking into account the net profit for the year, maintaining a solvent position.

DAe

The loss in DAe is due to onerous legacy contracts and relatively low order cover. DAe's financial position places a substantial funding burden on Denel with approximately R1 391m invested (loans of R602m and investments of R789m) to date. It has an annual funding requirement of circa R200m until positive cash generation by 2017/18, liabilities will exceed assets by R487m at year-end. Consequently, Denel has subordinated loans in favour of other creditors and guaranteed support for the business until it returns to solvency. This financial position has a negative impact on the group's going concern and funding requirements, details are in the funding section of this report. Saab, a former shareholder, exercised a put option on its

20% shareholding on 31 March 2011, leaving Denel as a 100% shareholder of DAe and resulting in R66m capital contribution that had to be repaid in April 2011.

DENEL DYNAMICS MISSILES

This business historically posted financial losses due to onerous contracts, amongst others. It recorded marginal profits for the second successive year; however, order cover and the closure of key contracts remain a challenge.

INTEREST EXPENSE ON BORROWINGS

The group is funded mainly by interest-bearing borrowings, with an interest cost of circa R100m per annum, which are backed by government guarantees. Also, refer to funding section of this report.

SIGNIFICANT CONTRACTS

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

ROOIVALK

The cabinet decided, in June 2008, that the Rooivalk would need to be certified to meet a scaled-down baseline. In light of the assigned five-year life of the Rooivalk system and the reduced functional baseline, the existing contractual terms and conditions required revision. Agreement on reduced functionality for the 1F baseline and limited post-1F work to underpin operational efficiency was reached in June 2010 and, on instruction of the DoD&MV, Denel re-launched work on the programme. The SAAF issued a full Military Type Certificate for the Rooivalk Mk1. It is anticipated that Denel will complete the upgrade and delivery of the three remaining Rooivalk aircraft to the 1F baseline during the 2012/13 financial year.

In addition, the development of a small number of contracted operational enhancements will be completed and introduced to the Rooivalk fleet as in-service modifications. Most notable of these enhancements is the provision of long-range external fuel tanks to increase the self-deployment range of the aircraft. Indications are that the SAAF may extend the life of Rooivalk beyond five years, thus requiring a full revision of the current logistic support approach to ensure the retention of core deeper-level support and manufacturing capabilities. The 1F baseline is in accordance with the cabinet memo and it has been agreed to in principle and condensed into a contract proposal; however the formal contract has not been signed. In addition, the party responsible for any latent defects that may arise has not been clarified.

The remaining three helicopters will be delivered during 2012/13, allowing the upgraded aircraft to enter operational service. This makes the Rooivalk the first helicopter to be designed, built, qualified and fully-certified on the African continent. This bears testimony to the capabilities and skills residing in the country. The programme accounted for revenues of R80m during the year under review. As at 31 March 2012 the balance of the provision is R78m, and is adequate to complete the remaining aircraft and related certification work in accordance with the 1F baseline.

PROJECT HOEFYSTER

Denel is executing a contract for the development and production of the new-generation infantry combat vehicle product system programme, called Hoefyster. The 2011 Rand value of the production phase of the contract is R8,4bn. The development phase, with a value of approximately R1bn, was activated in May 2006 and the product baseline for the 'section variant' was presented to Armscor on 10 September 2010. The presentation of the section variant initiated negotiation for the placement of the production order. Despite a delay in awarding the Hoefyster production contract, Denel is looking forward to be involved in the production phase of the programme.

The programme accounted for revenues of R205m during the year covering developmental work consisting of the integration of engineering development models for evaluation, with qualification in the next year. Denel is confident that all the development phase milestones will be met and that the production order will be placed in due course. Should the second phase of this project not be secured, it will have a negative impact on Denel's ability to maintain the total system capability.

Project Hoefyster, based on the localisation of overseas designed vehicle platform, will result in a local content of at least 70% and contribute to job creation. This will create a platform for Denel to retain and train skills such as artisans, technicians and engineers to meet IPAP2 and NGP objectives. It will further strengthen Denel's position to market infantry turrets and artillery systems, which may further contribute to the industry, SMME development and B-BBEE objectives. The execution of the production phase of the contract will run over a period of 10 to 12 years and provide Denel with a stable workload, during which time new products and markets can be explored.

ARMOURED FIGHTING VEHICLE

DLS was selected during May 2011 by a prime contractor to develop, manufacture, supply, deliver and commission a turret for 8x8 armoured fighting vehicles. Denel's participation in this programme emanates from project Hoefyster which is a similar development programme. The programme is for the supply of two-man turrets, missile turrets equipped with the GI30 30mm gun and anti-tank missile system. The programme requires participation in the buying country's economic enhancement programme which entails that the production and assembly of the turrets is not taking place locally, as well as having to commit to indirect industrial participation to a collective equivalent value as the actual contract value. The contract is to be executed over a period of seven years, with a similar time period allowed to effect the required industrial participation activities. The development of the first turret is currently on schedule and will be delivered in January 2013 for trials. The programme accounted for revenues of R187m during the year under review.

A400M

DAe is contracted as a programme partner for the design, development, manufacture, supply and supporting activities of the Airbus A400M WFF and TS structural components. The WFF is an essential part of the aircraft that provides protection against lightning strikes, hail damage and bird strikes to the sensitive equipment under the centre wing portion. The WFF is made up of 86 composite panels and doors and more than 800 metallic sub-structural machined parts, and is designed for ease of systems installation and maintenance. The TS is made up of approximately 200 parts consisting of a large machined skin, engineered out of an aluminium alloy. Each aircraft is fitted with two TS, positioned in front of, and behind the wings where they are joined to the fuselage. Over 1 000 system brackets support the vital electric and electronic wiring, hot air and heat exchange piping and including the aircraft's life-rafts.

Since contract signature in early 2005, DAe has designed and manufactured seven WFFs and eight TS pre-production units inclusive of both static and fatigue models. The first production models for TS and WFF were delivered in December 2010 and November 2011 respectively. The first production aircraft MSN007 is to be delivered to the French Air Force in December 2012. The deliveries will continue until MSN198 in October 2020. DAe is now gearing up for early ramp-up which will increase production of its parts to eight in 2013, 16 in 2014 and 24 in the subsequent years.

The contract was renegotiated with Airbus resulting in price increases and reduced penalties. Included in the negotiation commitments was the reinstatement of a previously cancelled A400M work package to DAe. As a result of the price uplift, a financial breakeven position will be reached in 2016/17. Final amendments of the contracts have not yet been signed; however, the risk to conclude is considered low by the board.

AVIONICS AND NAVIGATION UPGRADE

The Drummer II programme to upgrade avionics and the navigation system of the Oryx helicopter was awarded to DAv in 2007. It is a fixed price and fixed term contract for an amount of R460m that was originally due to be completed by June 2012. During the previous financial year, it became apparent that the contract would not be completed within the planned costs, considering the engineering and flight testing effort required. The programme is expected to slip by 28 months, with the new completion date being October 2014. This includes the development, qualification and production phases for the fleet of 38 aircraft. A detailed cost to completion exercise has been performed that revealed R138m, an excess of the contract price would be paid and was provided for in the financial statements for the year ended March 2011.

Progress on the Drummer II programme during the 2012 financial year has been satisfactory. The qualification flight test phase of the programme is scheduled for completion during May 2012. The provision created last year has been increased by R7m due to higher than forecasted escalation on labour. The completion date is planned to be October 2014. This depends on the availability of aircraft from the SAAF in accordance with the schedule. Management is negotiating a contract variation order to accommodate the slip in schedule and additional cost of completing of the programme.

AIR-TO-AIR MISSILE

The development of A-Darter, a highly sophisticated missile as a collaboration programme between the governments of SA and Brazil is on track. The first series of flight clearance and integration programme for carrying and firing the A-Darter from the Gripen fighter have been successfully completed, with final missile tests, qualification and performance validation underway for the commencement of production in 2014. The success of this joint development is likely to lead to further alliances with other developing nations. There are discussions about follow-on collaborative projects and marketing strategies.

The programme accounted for revenue of R319m in the year under review and the board does not foresee material risks on this project going forward.

SURFACE-TO-AIR MISSILE

The Umkhonto block II programme was initiated by the SA Navy to equip the South African Valour-class frigates with an effective close-in air defence capability. The release to operational service led to securing a contract from a NATO country to deliver a similar missile. The programme accounted for revenues of R33m during the year under review.

In assessing the missile's performance in the client's environment, it was originally found that the configuration was inadequate and required an upgrade. The Umkhonto block II product is now mature with a number of customers and additional production orders imminent. Umkhonto is a cost-effective modern product with high technical specification, and with additional functionalities being added to enhance the product. Umkhonto is positioned to exploit opportunities where navies refurbish existing vessels or commission smaller vessels. The product is ready to be used in SA's GBADS programme, as well as other ground-based air defence programmes. The board does not foresee material risks on this project going forward.

UNMANNED AERIAL VEHICLES

Denel has over the years developed and marketed Seeker II, which has been successfully deployed by customers in SA and globally. However, the changing nature of conflicts across the globe has placed new demands on manufacturers of surveillance systems. In response to these market and operational requirements, Denel invested in Seeker 400, a new and internationally competitive system. The investment will eventually amount to approximately R114m. Seeker 400 is a surveillance and reconnaissance platform that enhances situational awareness to support homeland security needs, including border patrol, maritime patrol, peacekeeping efforts, as well as tactical and strategic surveillance.

Significant progress has been made, with the first prototype completed and the manufacturing of the second prototype underway. The system is scheduled for its maiden flight in November 2012. The programme accounted for revenue of R30m and R&D cost of R57m during the year under review. Uncertainty remains on certification requirements from the military and civil aviation authorities.

PRECISION-GUIDED MUNITION

Denel concluded an export contract during May 2011 to the value of R1,2bn for the sale of precision-guided munitions. The agreement provides for the development of seekers, and the industrialisation and production of weapons.

As a result of investment in intellectual property over the years, this contract will secure access to new intellectual property and add to a range of off-the-shelf weapons from production lines in SA, whilst Denel has access to international funded technology.

The contract requires the establishment of a joint venture company in the client country, which will lead to the waiving of all related countertrade obligations. Furthermore, the second and probably the third phase contracts of similar value (each likely to be in excess of USD100m) are committed to be placed on the joint venture company.

The ramp-up of activities under this contract is well on track and the first milestones (related to aircraft integration) have already been achieved on time and within cost. The execution of the first guided release flight tests in the SA, as well as clearance release flight tests in the client country, as expected during 2012/13.

GROUND-BASED AIR DEFENCE

DISS is responsible for the design, development, integration and qualification of Phase I of an integrated ground-based air defence capability for the SA Army as contracted under project Guardian. Although originally envisaged as a simple integration programme, it evolved into a full-blown development programme with the associated risks and delays, without a contractual provision to mitigate Denel's cost and material exposures. In August 2010 the SA Army approved a revised technical baseline that would be acceptable for system delivery due to the fact that contracted performance was not attainable within prevailing technology boundaries.

DISS was appointed as the single source supplier of GBADS to the SANDF towards the end of 2009. Challenges were experienced with the development of Phase I, leading to a delay in the awarding of Phase II of the programme. These issues have since been resolved and the system was delivered to the SA Army towards the end of March 2012. The system will now enter into the commissioning phase of the programme with the assistance of DISS. DISS is in the process of responding to a number of requests for proposal on the follow-on phases of the programme. The programme accounted for revenue of R48m in the year under review.

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 to fund this liability are housed in the Denel Medical Benefit Trust. The assets and liabilities of the trust are held and accounted for separately in the name of the trust, and are not part of the 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 that the financial risk to the group terminates, whilst the qualifying employees continue to receive the benefit. To date, 68% 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 is terminated in terms of the remaining beneficiaries.

The actuarial value of the fund and other disclosures are provided in note 34 of the consolidated annual financial statements.

IMPAIRMENT OF ASSETS

Impairment assessments were performed on business units that demonstrated possible impairment indicators. Specific considerations were made to areas where there was a marked decline in profitability and negative cash flows. In DAe detailed impairment tests were performed. A CMS router machine that was impaired in prior years had been reinstated to the value of R24m and is included in the annual financial statements.

FUNDING

Denel engages with its shareholder on an on-going basis regarding the requirement for a recapitalisation due to the group's financial position. Denel understands that due to the current pressure on the fiscus, the shareholder is supporting Denel with guarantees.

Denel has interest-bearing borrowings with a coupon value of R1,845bn, raised through a Domestic Medium Term Note (DMTN) programme. These borrowings are backed by government guarantees of R420m, R880m and R550m. The guarantees mature on 30 September 2012 and Denel will apply to have these guarantees extended for a further period. The group's borrowings are at an average interest rate of 5.82% that includes an average overnight borrowing rate of 6.70%, and an average CPP interest rate of 5.78% with a total interest cost of R114m.

Denel has maintained its FitchRatings rating during the year at AA(zaf) long-term and F1+(zaf) short-term with a negative outlook. The negative outlook is due to Denel's continued operational challenges and the rating agency is relying strongly on continued shareholder support for the group. This is based on government reaffirmation that it views Denel as a strategic state-owned company that supplies the DoD with key strategic defence equipment and services, contributing towards the building of a dynamic defence-related industrial cluster and acts as a catalyst for advanced manufacturing in the broader economy.

The cash on hand and cash forecast for the next 12 months indicate that the group will be liquid during the forthcoming year. Denel implemented a cash conservation management forum to ensure liquidity on a continuous basis with cash monitored on a daily, weekly and monthly basis.

GOING CONCERN

As detailed in previous annual reports, Denel received R3,5bn recapitalisation over a three year period to 2008 and has achieved significant successes in its restructuring process. This is evidenced in the group's improved financial performance. The group is solvent with shareholder equity of R695m at 31 March 2012, and the shareholder has indicated that Denel would further be recapitalised by R700m during 2013 which would render the company solvent for the foreseeable future. Cash and short-term deposit balances of R1bn are adequate to fund the group, especially after taking into account the additional R700m inflow expected in 2013 from the recapitalisation as announced in the 2012 budget by the Minister of Finance. Denel is a high working capital investment company due to the long-term nature of the contracts requiring on-going funding.

The balance sheet of the company, however, remains fairly weak, as such the DPE together with NT are exploring various sustainable funding mechanisms for Denel. Denel is cognisant of the fact that a complete turnaround of the group depends on funding and new revenue streams, including improvements in operational excellence, efficiency and cost structure. These issues include the improvement in contracting and risk management, as well as efficiency and cost optimisation across all business units.

The directors, in evaluating the appropriateness of the going concern assumptions used in the preparation of the annual financial statements, took the above stated risks into account, the cash requirements for 12 months from reporting date, the solvency, and cash position at year-end and available borrowing facilities. In particular, the directors considered the matters summarised below:

- The solvency and liquidity position of the group as at 31 March 2012. The shareholder provided financial support to Denel by means of a recapitalisation of R3,5bn over the past five years, announced that the company will further be recapitalised by R700m in 2013 and issued guarantees for funding of R1,85bn.
- The availability of sufficient funds to meet the group's requirements over the next 12-months, including DAe.
- The forecasted shareholder's equity for the 2013 financial year remains positive.
- 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.
- The cash flow forecast incorporating the cash on hand at year-end, the cash receivable from the R700m recapitalisation and the short-term borrowings, which are expected to enable the group to have a positive cash position at 31 March 2013.
- Government guarantees for R1,85bn to support the short-term borrowings that were extended, on 31 March 2011 to 30 September 2012, would be extended for a further period.

Based on the above factors, the directors are satisfied that Denel has adequate reserves and cash resources to continue operating as a going concern for the 12 month period to 31 March 2013. The consolidated annual financial statements were, therefore, prepared on this basis. The ability of the group to continue as a going concern in the long-term is dependent upon:

- The successful implementation of the business strategy and the recommendations of the cabinet-appointed task team, which is expected to restore the group to profitability on a sustainable basis.
- The ability of the shareholder to support the group financially.
- The receipt of the R700m recapitalisation plus rolling over and issuing of the government guarantees of R1,85bn, as may be appropriate.

Should the interventions referred to above be unable to address the profitability and liquidity issues, the group may be unable to realise its assets and discharge its liabilities in the normal course of business.

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 and monitoring the system itself to detect and address any deficiencies in order to prevent 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 ASSOCIATES

The interests in subsidiaries and associates are set out in note 12, 13 and 36 of the *consolidated annual financial statements*.

SUBORDINATION AGREEMENTS

The group has subordinated loans of R602m advanced to DAe in favour of other creditors limited to their respective equity deficit balances, until such time as assets exceed liabilities fairly valued.

CAPITAL EXPENDITURE

The board approved capital expenditure of R161m whereas R103m was utilised, mainly in upgrading the business unit 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 has been no change in the authorised share capital of the company for the financial year under review.

DIVIDENDS

No dividend was recommended for the 2012 (2011: nil) year.

COMPLIANCE WITH ACCOUNTING STANDARDS

The consolidated annual financial statements comply with International Financial Reporting Standards (IFRS).

AUDITORS

The consolidated annual financial statements are audited by Ernst & Young Inc., with SizweNtsalubaGobodo as subcontracted auditors. The statutory auditors for the forthcoming year will be confirmed at the AGM scheduled for 19 July 2012.

GROUP COMPANY SECRETARY

The group company secretary for the period under review was Ms Elizabeth Africa and her business and postal addresses during the year were as stated below, which is also the address of the registered office of the company.

Denel Building Head Office	PO Box 8322
Nellmapius Drive	Centurion
Irene	0046
Gauteng	Republic of South Africa
Republic of 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 matters arose between 31 March 2012 and 19 June 2012.


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CONSOLIDATED STATEMENTS OF FINANCIAL POSITION AS AT 31 MARCH 2012

		Group			Company		
			Restated	Restated		Restated	Restated
		2012	2011	2010	2012	2011	2010
	Notes	Rm	Rm	Rm	Rm	Rm	Rm
ASSETS							
Non-current assets		2 131	2 110	1 677	1 881	1 900	1 492
Property, plant and equipment	9	691	660	683	540	538	543
Investment properties	10	450	448	406	450	448	406
Intangible assets	11	110	57	57	110	57	57
Investments in subsidiaries	12				18	9	4
Investments in associates	13	583	566	518	477	477	477
Loans and receivables	14	286	371	5	286	371	5
Deferred tax assets	15	11	8	8	-	-	-
Current assets		3 420	2 921	3 343	3 013	2 502	2 684
Inventories	16	624	570	713	550	451	463
Trade and other receivables	17	1 450	1 157	1 332	1 203	933	1 022
Reinsurance asset	18	21	20	19	-	-	-
Loans and receivables	14	193	191	5	193	191	5
Other financial assets	19.1	38	21	77	38	21	63
Income tax receivables		-	8	4	-	7	-
Cash and short-term deposits	20.1	1 074	920	1 038	1 009	865	976
Cash held on behalf of associates	20.2	20	34	155	20	34	155
Assets classified as held for sale	5	91	7	-	90	-	-
Total assets		5 642	5 038	5 020	4 984	4 402	4 176
EQUITY AND LIABILITIES							
Equity							
Issued capital	21	1 225	1 225	1 225	1 225	1 225	1 225
Share premium	21	4 251	4 251	4 251	4 251	4 251	4 251
Other reserves		43	44	45	43	43	44
Accumulated loss		(4 824)	(4 866)	(4 878)	(5 198)	(5 202)	(5 327)
Total equity attributable to equity holders of the parent		695	654	643	321	317	193
Non-controlling interest	22	-	-	(34)			
Total equity		695	654	609	321	317	193
Non-current liabilities		1 288	680	740	1 166	543	623
Interest bearing loans and borrowings	23	101	101	101	-	-	-
Advance payments received	24	920	205	283	920	205	283
Provisions	25.1	260	369	350	246	338	340
Deferred tax liabilities	15	7	5	6	-	-	-
Current liabilities		3 659	3 704	3 671	3 497	3 542	3 360
Trade and other payables	26	826	658	633	740	602	500
Interest bearing loans and borrowings	23	1 865	1 845	1 943	1 865	1 845	1 943
Other financial liabilities	19.2	48	45	97	46	37	48
Advance payments received	24	447	655	319	412	601	278
Income tax payables		3	-	1	-	-	-
Provisions	25.2	470	501	678	434	457	591
Total liabilities		4 947	4 384	4 411	4 663	4 085	3 983
Total equity and liabilities		5 642	5 038	5 020	4 984	4 402	4 176

CONSOLIDATED INCOME STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2012

	Notes	Group 2012 Rm	Group *Restated* 2011 Rm	Company 2012 Rm	Company 2011 Rm
Continuing operations					
Revenue	2	3 568	3 252	2 823	2 632
Cost of sales	3	(2 706)	(2 749)	(2 075)	(2 121)
Gross profit		862	503	748	511
Other income	4	196	80	231	206
Other operating expenses	3	(958)	(897)	(890)	(948)
Operating profit/(loss)		100	(314)	89	(231)
Surplus allocation	33	-	463	-	463
Finance costs	7.1	(145)	(157)	(147)	(163)
Finance income	7.2	61	37	62	48
Share of profit of associates	13	33	81		
Profit before tax		49	110	4	117
Income tax expense	8	(8)	1	-	7
Profit for the year		**41**	**111**	**4**	**124**
Profit for the year is attributable to:					
Equity holders of the parent		41	158		
Non-controlling interest		-	(47)		
		41	111		

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 MARCH 2012

	Notes	Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
Profit for the year		41	111	4	124
Other comprehensive income for the year, net of tax		-	-	-	-
Total comprehensive income for the year net of tax		41	111	4	124
Attributable to:					
Equity holders of the parent		41	158		
Non-controlling interest		-	(47)		
		41	111		

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 MARCH 2012

	Notes	Attributable to equity holders of the parent			
		Issued capital Rm	Share premium Rm	Revaluation reserves [1] Rm	Contingency reserves [2] Rm
Group					
Balance at 1 April 2010		1 225	4 251	44	1
Total comprehensive income/(loss)				-	-
Profit for the year				-	-
Other comprehensive income					-
Transfer (from)/to accumulated loss				(1)	-
Acquisition of non-controlling interest	22			-	-
Balance at 31 March 2011		1 225	4 251	43	1
Total comprehensive income				-	-
Profit for the year				-	-
Other comprehensive income				-	-
Transfer (from)/to accumulated loss	9			-	(1)
Balance at 31 March 2012		1 225	4 251	43	-
Company					
Balance at 1 April 2010		1 225	4 251	44	-
Total comprehensive income				-	-
Profit for the year				-	-
Other comprehensive income				-	-
Transfer (from)/to accumulated loss				(1)	-
Balance at 31 March 2011		1 225	4 251	43	-
Total comprehensive income				-	-
Profit for the year				-	-
Other comprehensive income				-	-
Transfer (from)/to accumulated loss					
Balance at 31 March 2012		1 225	4 251	43	-

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

[2] *In terms of the Short-term Insurance Act, Densecure SOC Ltd, a subsidiary, is required to raise a contingency reserve of 10% of premiums written, less approved reinsurance (as defined in the Short-term Insurance Act, 1998). The reserve can only be utilised with prior permission of the Registrar of Insurance.*

Attributable to equity holders of the parent			
Accumulated loss Rm	Total Rm	Non-controlling interest Rm	Total equity Rm
(4 878)	643	(34)	609
158	158	(47)	111
158	158	(47)	111
-	-	-	-
1	-	-	-
(147)	(147)	81	(66)
(4 866)	654	-	654
41	41	-	41
41	41	-	41
-	-	-	-
1	-	-	-
(4 824)	695	-	695
(5 327)	193		
124	124		
124	124		
-	-		
1	-		
(5 202)	317		
4	4		
4	4		
-	-		
-	-		
(5 198)	321		

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEAR ENDED 31 MARCH 2012

	Notes	Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
OPERATING ACTIVITIES					
Net cash flows from operating activities		360	178	408	355
Receipts from customers		3 576	3 488	2 902	2 903
Payments to suppliers and employees		(3 767)	(3 625)	(3 068)	(2 940)
Cash utilised in operations	28	(191)	(137)	(166)	(37)
Increase in advance payments received	24	507	258	526	245
Interest paid		(7)	(3)	(9)	(9)
Interest received		33	32	34	43
Dividend received	4	16	33	16	113
Income tax paid		2	(5)	7	-
INVESTING ACTIVITIES					
Net cash flows used in investing activities		(150)	(201)	(208)	(371)
Purchase of property, plant and equipment	9	(103)	(88)	(73)	(75)
Proceeds from sale of property, plant and equipment		14	2	-	1
Purchase of intangible assets	11	(69)	(15)	(69)	(15)
Receipt of loans and receivables		5	5	5	5
New loans to associates		-	(105)	-	(105)
Repayments of loan advance to associates		3	-	3	-
Proceeds from reduction in share investment in subsidiary				-	27
Advances to subsidiaries				(74)	(209)
Net cash flows before financing activities		210	(23)	200	(16)
FINANCING ACTIVITIES					
Net cash flows used in financing activities		(70)	(203)	(70)	(203)
Repayments of interest bearing borrowings		(5 292)	(3 300)	(5 292)	(3 300)
Proceeds from interest bearing borrowings		5 236	3 218	5 236	3 218
Decrease in cash managed on behalf of associates		(14)	(121)	(14)	(121)
Net increase/(decrease) in cash and cash equivalents		140	(226)	130	(219)
Cash and cash equivalents:					
At the beginning of the year		954	1 180	899	1 118
At the end of the year	20	1 094	954	1 029	899

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2012

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, rounded off to the nearest million.

The consolidated annual financial statements for the year ended 31 March 2012 comprise the company, its subsidiaries and associates.

1.1 STATEMENT OF COMPLIANCE

The consolidated annual financial statements have been prepared in accordance with IFRS.

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 make judgements, 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 the 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 ongoing 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 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, except for the reclassifications as set out below:

Advance payments received

The group has changed the classification of advance payments received to make distinction between current and non-current portions. During the year the group concluded two large long-term sales contracts for which significant advance payments were received. These advance payments will be settled over a period of up to seven years. Management believe it appropriate to reclassify advance payments received by making a distinction between current and non-current liabilities. The portion of the liability that will be settled after more than one year after the end of the reporting period is classified as non-current. The non-current portion represents almost 70% of the total advance payments received in the current year.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

The additional disclosure will provide useful information to the users of the financial statements as well as fairer presentation of the advance payments received. Refer to note 24.

Share of profit of associates

Previously the group recognised its share of the profit of the associates before tax on the Income statement line *Share of profit of associates* and included its share of the taxes in the line Income tax expense. The group has now changed this treatment to show the after tax profit of the associates on the line *Share of profit of associates* on the Income statement. This treatment is in line with the *Guidance on implementing: IAS 1 Presentation of Financial Statements*.

The comparative numbers have been restated as follows:

	Restated 2011 Rm	Previously reported 2011 Rm	Restated 2010 Rm	Previously reported 2010 Rm
Group				
Non-current advance payment received	205	-	283	-
Current advance payment received	655	860	319	602
	860	860	602	602
Consolidated income statements				
Share of profit of associates	81	115		
Profit before tax	110	144		
Income tax expense	1	(33)		
Profit for the year	111	111		
Note 8				
Taxation expense				
SA Normal tax				
Current tax	7	7		
Deferred tax	(1)	(1)		
STC	(7)	(7)		
Share of associates		34		
Current tax		20		
STC		3		
Deferred tax		11		
	(1)	33		
Company				
Non-current advance payment received	205	-	283	-
Current advance payment received	601	806	278	561
	806	806	561	561

The following amended IFRS and International Financial Reporting Interpretations Committee (IFRIC) interpretations became effective during the year:

Standard/ interpretation	Previously reported title	Restated effective date	Previously reported impact and application
IFRIC 20	*Stripping Costs in the Production Phase of a Surface Mine*	1 January 2013 (early adopted)	Not relevant to the group

The adoption of these standards and interpretations did not have any effect on the financial performance or position of the group or on any additional disclosure, as no events occurred that these standards and interpretations relate to.

Basis of consolidation

The consolidated annual financial statements reflect the financial position and operating results of the company, its subsidiaries and associates. The accounting policies have been applied consistently by the group's business units.

Subsidiaries

Subsidiaries are companies in which the group has the power to govern the financial and operating policies of the unit so as to obtain benefits from its activities. Typically this will be where the company holds more than 50.0% of the voting rights, including potential voting rights that are currently exercisable or convertible, controls the composition of the board of directors, or is significantly exposed to the risks or enjoys the benefits of ownership. Subsidiaries are consolidated from the date on which effective control is transferred to the group, up until the date control ceases.

In the separate financial statements, investment in subsidiaries, jointly controlled units and associates, 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.

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

Associates

Associates are those units 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 gains and losses of associates 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 gains and losses of that associated company is adjusted to account for the difference in year-end. When the group’s share of losses exceeds its interest in an associated company, the group’s carrying amount is reduced to nil 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 an associated company.

Transactions eliminated on consolidation

All inter-company transactions, balances and unrealised gains and losses are eliminated in preparing the consolidated annual financial statements. Unrealised gains arising from transactions with associates and jointly controlled units are eliminated to the extent of the group’s interest in the unit.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

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:

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

Business units 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.
- Technical obsolescence on aircraft and missile contracts where rapidly changing technology may result in a re-engineering requirement on these systems.

Management made significant judgements on the following programmes (for more detail discussion on these programmes, refer to the *directors' report*):

Rooivalk contract

The provision for the contract loss of R78m (2010/11: R116m) at year-end has been determined based on the obligations arising from the cabinet memorandum (decision) of June 2008, representing both the customer and the shareholder. It is no longer based on the original contract. In terms of a legal opinion obtained, a cabinet memorandum is an executive decision similar in effect with law passed and is binding to all who are affected by it. Management made certain assumptions regarding the scope in determining the provision with reference to the cabinet memorandum.

Airbus A400M contract

The contract costs to completion on the A400M contract have been calculated based on management's best estimates, taking into account the technical and industrial uncertainties attached to the programme. These include quantities to be delivered on specific dates, escalations and a delay of four years.

Drummer II programme

The Drummer II programme is a fixed price fixed term amount of R460m that was originally due to be completed by June 2012. A cost overrun is expected on the programme due to the expected slippage by 28 months, with the new completion date being October 2014. This includes the development, qualification and production phases for the fleet of 38 aircraft. Assumptions have been made with regards to estimated labour hours, material costs and escalations.

Impairment of property, plant and equipment

Impairment assessments are performed on units within the group that demonstrate impairment indicators. The group's impairment tests for property, plant and equipment are based on fair value less cost to sell using the estimated fair value of the assets less the estimated costs of disposal. An amount of R24m was reversed relating to property, plant and equipment that was previously impaired as a sales agreement was concluded during the year that will lead to the use of the specific plant and equipment to manufacture the products to be supplied under the agreement.

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 nil to 10.0%, and is determined at the quotation phase and is reviewed on a regular basis.

Site restoration

Certain business units within the group carry out manufacturing and testing activities that contaminate the land on which they are situated. In accordance with the applicable legislation and the group's environmental policy in respect of decontamination, a site restoration provision has been raised.

Management performed a detailed study in consultation with external specialists in the Land Systems business segment, which was identified as the most likely area to have such contamination. Following the study, a high level review of the remaining business segments was performed, taking into consideration the results of the study and the nature of their business activities.

A conservative 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 3 and 30 years. The anticipated future cash flows determined, based on a long-term inflation rate of 6.5% (2010/11: 6.6%) have been discounted at an interest rate of 8.4% (2010/11: 8.8%), which is based on the risk-free rate of return and the expected long-term inflation rate.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

Countertrade

The group endeavours to fulfil its countertrade obligations as indicated in note 27.6 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 60.0% and 100.0% of export sales.
- 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 4.0% and 8.5%) of the obligation as mentioned above.
- 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.

1.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1.3.1 REVENUE RECOGNITION

Sale of goods and services

Revenue 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 or 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.

Long-term contracts

Contract revenue and costs relating to long-term construction contracts are recognised in profit or 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, then revenue is recognised to the extent of contract costs incurred that is probable of being recovered, while contract costs are recognised in the period in which they are incurred. Depending on the nature of the contract, the stage of completion is determined as follows:

- 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 client 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.

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

Contract revenue comprises:

a) The initial amount of revenue agreed in the contract; and
b) Variations in contract work and incentive payments:
   i) to the extent that it is probable that they will result in revenue; and
   ii) they are capable of being reliably measured.
c) 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 or loss.

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. Lease incentives granted are recognised in profit or losses an integral part of the total rental income.

Finance income and expense

Finance income comprises interest income on funds invested.

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

Finance expenses comprise interest expense on borrowings, unwinding of the discount on provisions and impairment losses recognised on financial assets. All borrowing costs are recognised in profit or loss using the effective interest rate method.

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

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

1.3.2 DISCONTINUED OPERATIONS AND NON-CURRENT ASSETS HELD FOR SALE

A discontinued operation is a component of the group’s business that has either been disposed or is classified as held for sale and that represents a separate major line of business or geographical area of operations or is a subsidiary acquired exclusively with a view to its subsequent disposal.

Assets are classified as non-current assets held for sale if the carrying amount would be recovered principally through sale and not continuing use. A business unit 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 (and all assets and liabilities in a disposal group) is done in accordance with applicable IFRSs. Then, on initial classification as held for sale, non-current assets and disposal groups are recognised at the lower of carrying amount and fair value less costs to its subsequent disposal.

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FOR THE YEAR ENDED 31 MARCH 2012

Impairment losses on initial classification as held for sale are recognised in profit or loss. Gains, limited to previously recognised impairment losses and losses on subsequent measurement, are recognised in profit or loss.

1.3.3 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 or losses finance cost as it occurs.

1.3.4 TAXES

Income tax for the year comprises of current and deferred tax. Income tax is recognised in profit or loss, except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date and any adjustments relating to prior years.

Deferred tax is provided in full using the liability method for temporary differences arising between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. 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 or loss nor taxable profit or loss. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates that are expected to apply for the year when the asset is realised or the liability is settled based on tax rates enacted or substantially enacted at the reporting date.

A deferred tax asset is only recognised to the extent that it is probable that future profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related taxation benefit will realise.

Deferred tax assets and liabilities are recognised on a net basis for each tax unit.

Secondary Tax on Companies (STC) that arises from the distribution of dividends is recognised at the same time as the liability to pay the related dividend.

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
- 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 statement of financial position.

1.3.5 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 loans receivable, trade and other receivables, cash and cash equivalents, borrowings, and trade and other payables.

Non-derivative financial instruments are recognised initially at fair value, plus, for instruments not at fair value through profit or 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 or loss, as well as loans and receivables (including insurance receivables) and cash and cash equivalents. The group currently does not hold any held-to-maturity or available-for-sale assets.

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 or 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 or 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 comprises 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.

Financial liabilities

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

Financial liabilities are initially measured at fair value less transaction costs that are directly attributable to the raising of the 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 or 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.

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FOR THE YEAR ENDED 31 MARCH 2012

Trade and other payables

Trade and other payables are stated at amortised cost. Gains and losses on the derecognition process are recognised in profit or 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. 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 or 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 client. 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 or 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 USD, GBP and 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 or loss. The embedded derivative assets or liabilities are released to sales, 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 set-off 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 offset.

Derecognition 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 them 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:
  a) has transferred substantially all the risks and rewards of the asset of ownership; or
  b) has neither transferred nor retained substantially all the risks and rewards of ownership of the asset, but has transferred control of the asset.

Where the group has transferred its contractual rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the group could be required to repay.

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 derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

1.3.6 FOREIGN CURRENCIES

Functional and presentation currency

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

Recording of foreign transactions

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

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 or loss. Nonmonetary 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. Nonmonetary 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.

1.3.7 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. 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 or 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.

The valuations are prepared by considering the aggregate of the net annual rentals receivable from the properties and where relevant, associated costs. A yield which 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 SA yields applied for each type of property is included below:

- Offices: 10.0% to 15.0%
- Manufacturing: 10.0% to 15.0%

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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 credit-worthiness, 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 reversionary increases, all notices and, where appropriate, counter notices have been served validly and within the appropriate time.

Rental income from investment properties is accounted for as described in the revenue policy for rentals. Compensation from third parties for investment property that was impaired, lost or given up is recognised in profit or 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.

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.

1.3.8 PROPERTY, PLANT AND EQUIPMENT

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.

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: 3 to 40 years
- Machinery and equipment: 3 to 60 years

- Vehicles: 5 years
- Office furniture and accessories: 3 to 20 years
- Computer equipment: 3 to 5 years

The useful lives and the residual values of items of property, plant and equipment are reassessed annually.

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 or losses an expense when incurred.

Derecognition

The carrying amount of an item of property, plant and equipment shall be derecognised at the earlier of:
a) The date of disposal; or
b) The date when no future economic benefits are expected from its use or disposal.

Gains and/or losses on derecognition of items of property, plant and equipment are recognised in profit or 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 or 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 during more than one period. 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.

1.3.9 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 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, and depreciated over the estimated useful life of the asset. The capital element of future obligations under the leases is included as a liability in the statement of financial position. Lease payments are allocated using the effective interest rate method to determine the lease finance cost, which is expensed over the lease period, and the capital repayment, which reduces the liability to the lessor.

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 or loss on a straight-line basis over the term of the lease. Lease incentives paid are recognised in profit or losses an integral part of the total lease expense.

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Combined leases with land components and building components are considered separately for classification purposes. At inception of the lease, the minimum lease payments are allocated to the components in proportion to the relative fair values of the leasehold interests in the land element and buildings element of the lease. If this cannot be measured reliably, then the lease is classified as a finance lease, unless it is clear that both elements are operating leases, in which case the entire lease is classified as an operating lease.

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

1.3.10 INTANGIBLE ASSETS

Intangible assets that are acquired separately by the group are measured on initial recognition at cost. Subsequently, intangible assets are carried at cost less accumulated amortisation and accumulated impairment losses.

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 or 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.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

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.

R&D 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. 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 economic benefit.

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 measured on initial recognition 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 units, or groups of cash-generating units, 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 units or groups of units. Each unit or group of units 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 unit (group of cash-generating units) and part of the operation within that unit 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 unit 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 or loss.

Negative goodwill arising on acquisition is recognised immediately in profit or loss.

1.3.11 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 or loss.

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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 costs to sell 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 unit to which the asset belongs.

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 unit exceeds its recoverable amount. Impairment losses are recognised in profit or loss.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units and then to reduce the carrying amount of the other assets in the unit 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 or 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 or 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.

1.3.12 INVENTORIES

Inventories are stated on the first-in-first-out (FIFO) basis at the lower of cost price and net realisable value. 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 or 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 its present location and condition.

Work-in-progress, finished products and contracts-in-progress

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.

Property development

Property development is valued at cost and includes directly attributable transaction costs, costs of purchases of property, development costs, construction costs and borrowing costs.

1.3.13 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 an expense when incurred.

1.3.14 ADVANCE PAYMENTS RECEIVED FROM SALES CONTRACTS

In the case of comprehensive and/or long-term sales contracts, advance payments are negotiated with local and foreign clients. 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 clients for advance payments received. Advance payments received are recognised as a current liability for 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.

1.3.15 EMPLOYEE BENEFITS

Pension obligations

The group operates a defined contribution plan and previously a defined benefit plan (Denel withdrew from this fund as principal employer on 1 September 2010), the assets of which are held in separate trustee administered funds. The defined pension plan was funded by payments from employees and by the relevant business units based on the recommendations of independent qualified actuaries.

The allocated surplus relating to the defined benefit pension fund apportionment scheme was recognised in profit or loss on approval of the scheme by the Financial Service Board. (FSB)

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

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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. Independent qualified actuaries carry out valuations of these obligations on an annual basis.

1.3.16 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 which requires the group to impose countertrade obligations on suppliers in favour of South Africa 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 prescribes a form of investment in the buyer's country.

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.

1.3.17 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 executive committee of Denel SOC Ltd.

1.3.18 INSURANCE CONTRACTS

An insurance contract is a contract that transfers significant insurance risk from policyholder to insurer. An assessment of whether recognised insurance liabilities are adequate is performed at each reporting date, using current estimates of future cash flows under insurance contracts. If the assessment shows that the carrying amount of insurance liabilities (less related deferred acquisition costs and related intangible assets) is inadequate in light of the estimated future cash flows, the entire deficiency is recognised in profit or loss.

Reinsurance contracts held

Contracts entered into by the company with reinsurers under which the group is compensated for losses on one or more insurance contracts issued by the group and that meet the classification requirements for insurance contracts are classified as reinsurance contracts held. Contracts that do not meet these classification requirements are classified as financial assets. The benefits to which the group is entitled under its reinsurance contracts held are recognised as reinsurance assets, which are dependent on the expected reinsurance claims and benefits arising under the related reinsured insurance contracts. These assets consist of short-term receivables due from reinsurers. The amounts recoverable from or due to reinsurers are measured in terms of each reinsurance contract.

Reinsurance assets are assessed for impairment at each reporting date. A reinsurance asset is deemed impaired if there is objective evidence, as a result of an event that occurred after its initial recognition, that the group may not recover all amounts due, and that event has a reliably measurable impact on the amounts that the group will receive from the reinsurer. Impairment losses on reinsurance assets are recognised in profit or loss for the period.

Receivables and payables related to insurance contracts

Insurance receivables and payables are recognised when due. These include amounts due to and from agents, brokers and insurance contract holders.

1.3.19 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 asset or liability or an unrecognised firm commitment
- Cash flow hedges when hedging exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction
- 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 or loss.

If a cash flow hedge meets the conditions for hedge accounting the portion of the gain or loss on the hedge instrument that is determined to be an effective hedge is recognised in other comprehensive income and the ineffective portion is recognised in profit or loss.

If an effective hedge of a forecast transaction subsequently results in the recognition of a financial asset or financial liability, the associated gains or losses recognised in equity are recognised in profit or loss in the same period in which the asset or liability affects profit or loss.

If a hedge of a forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, the associated gains or losses recognised in equity are included in the initial measurement of the acquisition cost or other carrying amount of the asset or liability.

If a hedge of a net investment in a foreign unit 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 other comprehensive income and the ineffective portion is recognised in profit or loss. On disposal of a foreign unit, the gain or loss recognised in equity is transferred to profit or 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, for cash flow hedges, the forecast transaction is no longer expected to occur or when the hedge designation is revoked.

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FOR THE YEAR ENDED 31 MARCH 2012

1.4 STANDARDS, INTERPRETATIONS AND AMENDMENTS ISSUED THAT ARE NOT YET EFFECTIVE

At the date of authorisation of the consolidated annual financial statements for the year ended 31 March 2012, the following standards and interpretations were in issue but not yet effective:

Standard or Interpretation	Title	Issue date	Effective date
IFRS 9	*Financial Instruments*	November 2009	1 January 2015
IFRS 10	*Consolidated Financial Statements*	May 2011	1 January 2013
IFRS 11	*Joint Arrangements*	May 2011	1 January 2013
IFRS 12	*Disclosure of Interests in Other Units*	May 2011	1 January 2013
IFRS 13	*Fair Value Measurement*	May 2011	1 January 2013
IFRS 7	*Financial Instruments: Disclosures* — *Amendments enhancing disclosures about offsetting of financial assets and financial liabilities* *Financial Instruments: Disclosures* — *Amendments requiring disclosures about the initial application of IFRS 9*	December 2011 December 2011	1 January 2013 1 January 2015 (or otherwise when IFRS 9 is first applied)
IAS 1	*Presentation of Financial Statements* — *Amendments to revise the way other comprehensive income is presented*	June 2011	1 July 2012
IAS 19	*Employee Benefits (Amendment)*	June 2011	1 January 2013
IAS 27	*Consolidated and Separate Financial Statements* — *Reissued as IAS 27 Separate Financial Statements (as amended in 2011)*	May 2011	1 January 2013
IAS 28	*Investments in Associates* — *Reissued as IAS 28 Investments in Associates and Joint Ventures (as amended in 2011)*	May 2011	1 January 2013
IAS 32	*Financial Instruments: Presentation* — *Amendments to application guidance on the offsetting of financial assets and financial liabilities*	December 2011	1 January 2014
	Annual Improvements	May 2012	1 January 2013
IFRS 1	*First-time Adoption of International Financial Reporting Standards* — *Repeated application of IFRS 1* — *Borrowing costs*		
IAS 1	*Presentation of Financial Statements* — *Clarification of the requirements for comparative information*		
IAS 16	*Property, Plant and Equipment* — *Classification of servicing equipment*		
IAS 32	*Financial Instruments: Presentation* — *Tax effect of distribution to holders of equity instruments*		
IAS 34	*Interim Financial Reporting* — *interim financial reporting and segment information for total assets and liabilities*		

IFRS 9 Financial Instruments

The new standard introduces new requirements for classifying and measuring financial assets. The new standard forms part of a three-part project to replace IAS 39 Financial Instruments: Recognition and Measurement. The group plans to adopt the standard only once the other parts of the project are available to enable the group to adopt them simultaneously. The group is in the process of evaluating the impact on the financial statements. The following are the main features of the standard:

- At initial recognition, all financial assets (including hybrid contracts with a financial asset host) are measured at fair value.

Debt instruments

For subsequent measurement, financial assets that are debt instruments are classified at amortised cost or fair value on the basis of both:

- The unit's business model for managing the financial assets; and
- The contractual cash flow characteristics of the financial asset.

Debt instruments may be subsequently measured at amortised cost if:

- The asset is held within a business model whose objective is to hold the assets to collect the contractual cash flows; and
- The contractual terms of the financial asset give rise, on specified dates, to cash flows that are solely payments of a principal and interest on the principal outstanding.

All other debt instruments are subsequently measured at fair value.

Equity investments

All financial assets that are equity investments are measured at fair value either through Other Comprehensive Income (OCI) or profit or loss. This is an irrevocable choice the unit makes by instrument unless the equity investments are held for trading, in which case they must be measured at fair value through profit or loss.

IFRS 10 Consolidated Financial Statements

IFRS 10 Consolidated Financial Statements establishes principles for the presentation and preparation of consolidated financial statements when an unit controls one or more other units.

IFRS 10 replaces the consolidation requirements in *SIC-12 Consolidation—Special Purpose Units and IAS 27 Consolidated and Separate Financial Statements.*

IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an unit should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess.

The group is in the process of evaluating the impact on the financial statements.

IFRS 11 Joint Arrangements

IFRS 11 Joint Arrangements provides for a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The standard addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled units.

IFRS 11 removes the option to account for jointly controlled units (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method.

The group is in the process of evaluating the impact on the financial statements.

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FOR THE YEAR ENDED 31 MARCH 2012

IFRS 12 Disclosure of Interests in Other Units

IFRS 12 Disclosure of Interests in Other Units is a new and comprehensive standard on disclosure requirements for all forms of interests in other units, including subsidiaries, joint arrangements, associates and unconsolidated structured units.

The group is in the process of evaluating the impact on the financial statements.

IFRS 13 Fair Value Measurement

IFRS 13 Fair Value Measurement establishes a single source of guidance under IFRS for all fair value measurement that will improve consistency and reduce complexity by providing, for the first time, a precise definition of fair value and disclosure requirements for use across IFRSs. IFRS 13 does not change when an unit is required to use fair value, but rather, provides guidance on how to measure fair value under IFRS when fair value is required or permitted by IFRS.

The group is in the process of evaluating the impact on the financial statements.

IAS 1 Financial Statement Presentation – Presentation of Items of Other Comprehensive Income

The amendments to IAS 1 changes the grouping of items presented in *Other Comprehensive Income*. Items that could be reclassified (or 'recycled') to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. The amendment affects presentation only and has there no impact on the group's financial position or performance.

IAS 19 Employee Benefits (Amendment)

The IASB has issued numerous amendments to IAS 19. These range from fundamental changes such as removing the corridor mechanism and the concept of expected returns on plan assets to simple clarifications and re-wording. The group is currently assessing the full impact of the amendments.

IFRS 7 Financial Instruments: Disclosures

The amendment amended the required disclosures to include information that will enable users of an unit's financial statements to evaluate the effect or potential effect of netting arrangements, including rights of set-off associated with the unit's recognised financial assets and recognised financial liabilities, on the unit's financial position.

Further amendments to IFRS 7 relate to additional disclosures requirement on the transition from IAS 39 to IFRS 9.

IAS 27 Separate Financial Statements (as revised in 2011)

As a consequence of the new IFRS 10 and IFRS 12, what remains of IAS 27 is limited to accounting for subsidiaries, jointly controlled units, and associates in separate financial statements. The group will adopt the changes in of IAS 27 simultaneously with IFRS 10, IFRS 11, IFRS 12 and IAS 28.

IAS 28 Investments in Associates and Joint Ventures (as revised in 2011)

As a consequence of the new IFRS 11 and IFRS 12, IAS 28 has been renamed *IAS 28 Investments in Associates and Joint Ventures,* and describes the application of the equity method to investments in joint ventures in addition to associates. The group will adopt the changes in of IAS 27 simultaneously with IFRS 10, IFRS 11, IFRS 12 and IAS 28.

IAS 32 Financial Instruments: Presentation

The amendment clarifies the meaning of "currently has a legally enforceable right to set off the recognised amounts (IAS 32.42(a)). This means that the right of set-off:

- must not be contingent on a future event; and
- must be legally enforceable in all of the following circumstances:
  - the normal course of business;
  - the event of default; and
  - the event of insolvency or bankruptcy of the unit and all of the counter parties.

Annual improvements (May 2012)

IFRS 1 – First-time Adoption of International Financial Reporting Standards. In this amendment, it is stated that an unit can be a first-time adopter more than once. An unit that has in the previous reporting period prepared its financial statements in terms of IFRSs, but whose most recent financial statements did not contain an explicit and unreserved statement of compliance is permitted to either apply IFRS 1 when it re-adopts IFRSs or IA*S 8 – Accounting Policies, Changes in Accounting Estimates and Errors*. A first-time adopter is permitted to apply *IAS 23 – Borrowing Costs*, either from the date of transition or an earlier date.

IAS 1 – Presentation of Financial Statements. In this amendment, the IASB clarifies the requirements for providing comparative information for the opening statement of financial position when an unit changes its accounting policies, or makes retrospective restatements or reclassifications, in accordance with IAS 8 and the requirements for providing comparative information when an unit provides financial statements beyond the minimum comparative information requirements.

IAS 16 – Property, Plant and Equipment. This amendment states that major spare parts and stand-by equipment may be recognised as property, plant and equipment provided that the definition of property, plant and equipment is met.

IAS 32 – Financial Instruments: Presentation. This amendment clarifies that income taxes on distributions to equity holders and transaction costs should be accounted for in terms of *IAS 12 – Income Taxes*.

IAS 34 – Interim Reporting. The amendment provides that the total assets and liabilities for a particular reportable segment are required to be disclosed if, and only if: a measure of total assets or of total liabilities (or both) is regularly provided to the chief operating decision maker; and there has been a material change from those measures disclosed in the last annual financial statements for that reportable segment.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
2	**Revenue**				
	Sale of goods and services	3 498	3 183	2 739	2 548
	Rental income	70	69	84	84
		3 568	3 252	2 823	2 632
3	**Cost of sales and other operating expenses**				
	Cost of sales and other operating expenses are arrived at after taking the following items into account:				
	Amortisation of intangible assets (refer note 11)	16	15	16	15
	Software	16	15	16	15
	Impairment (reversed)/raised	(31)	15	109	286
	Property, plant and equipment (refer note 9)	(24)	2	-	(2)
	Investments in subsidiaries (refer note 12)	-	-	65	243
	Inventories (refer note 16)	(5)	11	46	43
	Trade and other receivables	(2)	2	(2)	2
	Auditors' remuneration	18	17	14	13
	Current year	15	14	14	12
	Previous year's under accrual	-	1	-	-
	Other	3	2	-	1
	Depreciation (refer note 9)	93	93	71	73
	Buildings	11	10	10	10
	Plant and machinery	55	56	40	41
	Vehicles and office furniture	11	10	5	5
	Computer equipment	16	17	16	17
	Operating expenses for investment properties	120	90	120	90
	Operating lease payments	82	79	80	76
	Buildings	71	68	71	68
	Plant and machinery	1	4	-	3
	Vehicles and office furniture	2	2	2	2
	Computer equipment	8	5	7	3
	Directors' remuneration [2]	15	12	15	12
	Executive directors	11	10	11	10
	Non-executive directors	4	2	4	2
	Costs of inventories recognised as an expense	1 031	1 315	692	1 097
	Loss on disposal of assets	-	8	-	8
	Property, plant and equipment	-	8	-	8
	Net loss on financial instruments (refer note 6)	-	10	-	52
	Research and development costs [1]	635	706	585	684
	Staff costs	1 563	1 467	1 178	1 062
	Services costs	1 347	1 308	976	928
	Staff and related provisions	40	(34)	50	(17)
	Medical fund contributions	81	82	67	59
	Termination benefits paid	1	15	1	15
	Pension costs: Defined contribution plan	90	91	81	72
	Other long-term benefit contributions	4	5	3	5

[1] *The research and development costs are mainly client-funded, excluding an amount of R59m (2011: R74m) charged against provisions and R58m (2011: R9m) that has been capitalised.*

[2] *Detailed remuneration is fully disclosed in the directors' report. Executive directors' remuneration included is from date of appointment as director.*

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
4	**Other operating income**				
	Administration and management fees	-	2	9	11
	Royalties income [1]	3	8	3	8
	Fair value adjustment on investment properties (refer note 10)	92	42	92	42
	Net gains on financial instruments (refer note 6)	76	-	80	-
	Profit on disposal of property, plant and equipment	5	1	-	-
	Dividend received	-	-	16	113
	Other [2]	20	27	31	32
		196	80	231	206

1 *Royalties income as a result of the use of intellectual property developed by the group.*

2 *Other is mainly made up of scrap sales, insurance claims, low claim bonuses and discount received.*

		Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
5	**Non-current assets held for sale**				
	Property, plant and equipment (refer note 9)	1	7	-	-
	Investment properties (refer note 10)	90	-	90	-
		91	7	90	-

The property, plant and equipment relates to a specific unutilised machine for which an offer was received and negotiations for the disposal are in progress.

Investment properties relates to the Phillippi facility that was recently vacated by RDM. The negotiations relating to the selling of the property are in an advance stage and the selling price has already been determined.

		Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
6	**Net gains/(losses) on financial instruments**				
6.1	**Net foreign exchange differences**	73	(10)	77	(52)
	Losses on settled transactions	(56)	(15)	(39)	-
	Gains on settled transactions	128	81	116	45
	Losses on fair value adjustments	(41)	(121)	(38)	(101)
	Gains on fair value adjustments	7	57	3	16
	Losses on firm commitment remeasurement	(16)	(13)	(16)	(13)
	Gains on firm commitment remeasurement	51	1	51	1
6.2	**Net differences on commodity derivatives**	3	-	3	-
	Losses on fair value adjustments	-	-	-	-
	Gains on fair value adjustments	3	-	3	-
		76	(10)	80	(52)

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
7	**Net finance cost**				
	The amounts below relate to financial instruments measured at amortised cost (financial liabilities, loans and receivables):				
	7.1 Finance costs				
	Current interest bearing borrowings	114	118	114	118
	Inter-group finance costs			2	6
	Finance costs on financial liabilities	114	118	116	124
	Unwinding of discount on provisions	31	39	31	39
	Total finance costs	145	157	147	163
	7.2 Finance income				
	Gross interest received	61	37	57	33
	Inter-group finance income			5	15
	Total finance income	61	37	62	48
	Net finance costs	84	120	85	115
8	**Taxation expense**				
	SA Normal tax				
	Current tax	9	7	-	-
	Deferred tax (refer note 15)	(1)	(1)	-	-
	STC	-	(7)	-	(7)
		8	(1)	-	(7)
	No provision for SA Normal tax has been made for all companies within the group that are in a calculated tax loss position.				
		%	%	%	%
	Reconciliation of tax rate				
	Effective tax rate	16.3	(0.9)	-	(6.0)
	Adjustment in tax rate due to:	11.7	28.9	28.0	34.0
	Exempt income	16.0	10.6	289.6	37.0
	Secondary tax on companies	-	6.0	-	5.7
	Deferred tax asset not recognised	36.3	(113.6)	883.9	(52.9)
	Impairment of investments	-	-	(437.8)	(58.1)
	Taxable at capital gains tax rate	17.8	-	205.5	-
	Share of associates	18.9	20.6	-	-
	Other	(77.3)	105.3	(913.2)	102.3
	SA Normal tax rate	28.0	28.0	28.0	28.0

	Group 2012 Calculated tax losses Rm	Group 2011 Calculated tax losses Rm	Company 2012 Calculated tax losses Rm	Company 2011 Calculated tax losses Rm
8 Taxation expense (continued)				
The calculated tax losses available for offset against future taxable income are as follows:				
Calculated tax losses	6 074	5 883	4 810	4 699
Capital gains tax losses	175	175	175	175
Net available calculated tax losses	6 249	6 058	4 985	4 874

	Land and buildings Rm	Plant and machinery Rm	Vehicle and office furniture Rm	Computer equipment Rm	Total Rm
9 Property, plant and equipment					
Group					
2012					
Carrying value at 1 April	240	350	37	33	660
Additions	11	58	20	14	103
Disposals	-	(2)	-	-	(2)
Transfer to assets held for sale (refer note 5)	-	(1)	-	-	(1)
Impairment reversal for the year (refer note 3)	-	24	-	-	24
Depreciation for the year (refer note 3)	(11)	(55)	(11)	(16)	(93)
Carrying value at 31 March	240	374	46	31	691
Cost	384	1 357	118	160	2 019
Accumulated depreciation and impairment	(144)	(983)	(72)	(129)	(1 328)
Carrying value at 31 March	240	374	46	31	691
2011					
Carrying value at 1 April	248	359	34	42	683
Additions	2	64	12	10	88
Disposals	-	(9)	-	-	(9)
Reclassification	-	1	1	(2)	-
Transfer to assets held for sale (refer note 5)	-	(7)	-	-	(7)
Impairment for the year (refer note 3)	-	(2)	-	-	(2)
Depreciation for the year (refer note 3)	(10)	(56)	(10)	(17)	(93)
Carrying value at 31 March	240	350	37	33	660
Cost	373	1 317	99	149	1 938
Accumulated depreciation and impairment	(133)	(967)	(62)	(116)	(1 278)
Carrying value at 31 March	240	350	37	33	660

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

	Land and buildings Rm	Plant and machinery Rm	Vehicle and office furniture Rm	Computer equipment Rm	Total Rm
9 Property, plant and equipment (continued)					
Company					
2012					
Carrying value at 1 April	239	249	18	32	538
Additions	10	45	4	14	73
Depreciation for the year (refer note 3)	(10)	(40)	(5)	(16)	(71)
Carrying value at 31 March	239	254	17	30	540
Cost	382	1 048	57	150	1 637
Accumulated depreciation and impairment	(143)	(794)	(40)	(120)	(1 097)
Carrying value at 31 March	239	254	17	30	540
2011					
Carrying value at 1 April	248	236	18	41	543
Additions	1	60	4	10	75
Disposals	-	(9)	-	-	(9)
Reclassification	-	1	1	(2)	-
Impairment for the year (refer note 3)	-	2	-	-	2
Depreciation for the year (refer note 3)	(10)	(41)	(5)	(17)	(73)
Carrying value at 31 March	239	249	18	32	538
Cost	372	1 029	54	139	1 594
Accumulated depreciation and impairment	(133)	(780)	(36)	(107)	(1 056)
Carrying value at 31 March	239	249	18	32	538

Registers of property, plant and equipment are open for inspection at the business units of the group.

Owing to the operating losses at certain of the business units within the group, the property, plant and equipment have been assessed for impairment. *IAS 36 Impairment of assets* provides that the recoverable amount of an asset is the higher of its fair value less cost to sell and its value in use. The impairment was based on the fair value less cost to sell for all property, plant and equipment items. Certain property, plant and equipment were impaired in the recent past due to a lack of orders, whilst no new impairment raised this year.

An amount of R24m for assets previously impaired has been written back as a new contract was concluded that will lead to a certain group of assets being utilised.

Plant and machinery includes assets under construction of R18m (2010/11: R24m) for the group and R11m (2010/11: R17m) for the company.

		Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
10	**Investment properties**				
	Fair value at 1 April	448	406	448	406
	Fair value adjustment	92	42	92	42
	Transfer to assets held for sale (refer note 5)	(90)	-	(90)	-
	Fair value at 31 March	450	448	450	448

Valuations of investment properties were carried out at the 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. Fair values were determined having regard to recent market transactions for similar properties in the same location as the group's investment properties.

The property division of Denel has over the past five years not been actively marketing the Houwteq property located in the Western Cape. However, the business unit continues to be in discussion with the Department of Science and Technology (DST) regarding the disposal of the said property. There are significant uncertainties that the property will be disposed of, therefore, the directors consider that the assets do not meet the requirements for disclosure as assets held for sale at this stage.

		Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
11	**Intangible assets**				
	Development costs	67	9	67	9
	At cost	155	97	155	97
	Accumulated amortisation and impairment	(88)	(88)	(88)	(88)
	Software	43	48	43	48
	At cost	103	92	103	92
	Accumulated amortisation and impairment	(60)	(44)	(60)	(44)
	Total carrying value at 31 March	110	57	110	57
	Reconciliation				
	Development costs				
	Carrying value at 1 April	9	-	9	-
	Capitalised during the year	58	9	58	9
	Carrying value at 31 March	67	9	67	9
	Software				
	Carrying value at 1 April	48	57	48	57
	Additions	11	6	11	6
	Amortisation for the year (refer note 3)	(16)	(15)	(16)	(15)
	Carrying value at 31 March	43	48	43	48
	Total carrying value at 31 March	110	57	110	57

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
12	**Investments in subsidiaries**				
	Unlisted shares			860	860
	Net loans			548	559
	Amounts due by subsidiaries			606	621
	Amounts due to subsidiaries			(58)	(62)
	Gross investments			1 408	1 419
	Accumulated impairment			(1 390)	(1 410)
	Carrying value at 31 March			18	9
	Loans to subsidiaries of R601m (2010/11: R621m) have been subordinated in favour of other creditors of the subsidiaries. The subordination agreements will remain effective until such time that the subsidiaries involved return to solvency. In addition, the company has undertaken to provide financial support to DAe.				
	The offer received from a local company within the industry to buy significant assets within DAe in the prior year did not materialise.				
	A detailed breakdown of the investments in subsidiaries is contained in note 36.				
	Reconciliation of carrying value of investments in subsidiaries				
	Gross investment			1 408	1 419
	Accumulated impairment			(1 390)	(1 410)
	Carrying value at 31 March			18	9
	The accumulated impairment loss on investments in subsidiaries is as follows:				
	Unlisted shares			789	789
	Balance at 1 April			789	723
	Impairment for the year			-	139
	Amounts written-off due to subsidiaries wind-up			-	(73)
	Loans			601	621
	Balance at 1 April			621	619
	Impairment for the year			65	104
	Amounts written-off due to subsidiaries wind-up			(85)	(102)
				1 390	1 410

Included in the impairment for the prior year of unlisted shares is an amount of R73m that relates to a dividend received from pre-acquisition reserves.

		Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
13	**Investment in associates**				
	The group holds a 49% interest in Turbomeca Africa (Pty) Ltd. The year-end of Turbomeca Africa (Pty) Ltd is 31 December.				
	The group holds a 30% interest in Carl Zeiss Optronics (Pty) Ltd. The year-end of Carl Zeiss Optronics (Pty) Ltd is 30 September.				
	The group holds a 49% interest in Rheinmetall Denel Munition (Pty) Ltd. The year-end of Rheinmetall Denel Munition (Pty) Ltd is 31 December.				
	Cost of investments in associates:				
	Unlisted shares	476	476	477	477
	Net share of results in associates	107	90		
	Share of current year profit before tax	42	115		
	Share of current year tax	(9)	(34)		
	Share of current year profit after tax	33	81		
	Dividend paid by associates	(16)	(33)		
	Accumulated profit/(loss) at 1 April	90	42		
	Total net investments in associates	583	566	477	477
	The following represents the summarised financial information of the associates:				
	Total assets	2 366	2 052		
	Non-current assets	574	449		
	Current assets	1 792	1 603		
	Total liabilities	(1 372)	(1 102)		
	Non-current liabilities	(77)	(244)		
	Current liabilities	(1 295)	(858)		
	Net assets	994	950		
	Group share of associates' net assets	440	422		
	Revenue	1 739	1 820		
	Group share of revenue	770	817		
	Group share of profit before tax	42	115		
	A detailed breakdown of the investments in the associates is contained in note 36.				

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

	Group		Company	
	2012 Rm	2011 Rm	2012 Rm	2011 Rm
14 Loans and receivables				
Non-current loans and receivables	286	371	286	371
Current loans and receivables	193	191	193	191
	479	562	479	562
14.1 Loans receivable				
Loans at amortised cost	102	110	102	110
Secured loan	-	5	-	5
Loans to an associate	102	105	102	105
Less: Current portion of loans receivable	(85)	(93)	(85)	(93)
Secured loan	-	(5)	-	(5)
Loans to an associate	(85)	(88)	(85)	(88)
Non-current loans receivable	17	17	17	17

The loan to SITA has a balance of R0m (2010/11: R5m) and earns interest at a rate equal to the prime lending rate plus 1.5% per annum. The loan was repayable in fixed monthly instalments with the last instalment paid on 31 March 2012. The loan was secured by a mortgage bond over certain land and buildings owned by SITA.

The loans to an associate (RDM) comprises two separate loans. The non-current loan of R17m (2010/11: R17m), repayable not before January 2014, earns interest at a rate based on the three month JIBAR plus 1.4% per annum. The loan granted is in the same proportion to the shareholding. The current loan is a revolving credit facility granted to the associate to meet its short-term bridging finance, is repayable on 31 August 2012 and earns interest at a rate based on the three month JIBAR plus 1.4% per annum (2010/11: the prime lending rate minus 2.0% per annum). The parent company of the associate guarantees 51% of the outstanding balance of the loan.

	Group		Company	
	2012 Rm	2011 Rm	2012 Rm	2011 Rm
14.2 Pension asset				
Gross amount receivable	377	452	377	452
Less: Current portion of pension holiday receivable	(108)	(98)	(108)	(98)
Non-current portion	269	354	269	354

The pension asset relates to the unutilised balance of the pension surplus. DenPen, a defined benefit plan, became a pensioners' alone fund on 1 September 2010 following a decision by the trustees and members, and as a result Denel withdrew as a principal employer. The actuarial surplus in the fund mostly arising before the said restructuring was shared on a 50/50 basis between Denel and the members of the fund. The active members were transferred to DenRet. The assets underlining the actuarial surplus allocated to Denel were transferred to DenRet and are accessed by Denel through a contribution holiday over the next four years.

These assets are mainly invested in the money market.

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
15	**Deferred tax**				
	Deferred tax assets	11	8	-	-
	Deferred tax liabilities	(7)	(5)	-	-
		4	3	-	-
	Movement of deferred tax assets and liabilities:				
	Balance at 1 April	3	2	-	-
	Per income statement	1	1	-	-
		4	3	-	-
	Net deferred tax asset comprises:				
	Provisions	248	282	229	261
	Property, plant and equipment allowance	22	37	3	3
	Prepayments received	383	241	373	225
	Amounts due to customers for work invoiced, not yet performed	7	6	7	6
	Embedded derivative liabilities	4	10	4	8
	Other tax deductible differences	160	221	110	183
	Limit deferred tax asset to liability	(532)	(536)	(476)	(470)
	Assessed loss	1	3	-	-
		293	264	250	216
	Net deferred tax liability comprises:				
	Capital allowances	(110)	(108)	(111)	(108)
	Doubtful debt allowance	(5)	(5)	(5)	(5)
	Prepayments made	(4)	(3)	(4)	(3)
	Amount due from customers for contract work	(163)	(132)	(129)	(99)
	Reinsurance asset	(6)	(6)	-	-
	Other taxable differences	(1)	(1)	(1)	(1)
		(289)	(255)	(250)	(216)

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 709m (2010/11: R1 696m) for the group and R1 396m (2010/11: R1 365m) for the company.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Group		Company	
		2012 Rm	*Restated* 2011 Rm	2012 Rm	2011 Rm
16	**Inventories**				
	Inventories are valued at the lower of cost and net realisable value and are categorised as follows:				
	Raw materials and bought-out components	123	118	94	78
	Work in progress	287	232	253	180
	Contracts in progress	2	2	-	-
	Finished products	160	128	153	125
	Consumable inventory	52	90	50	68
		624	570	550	451
	Accumulated impairment	258	307	200	198
	Net amount of write-down/(write back) of inventories recognised as an expense	(5)	11	46	43
17	**Trade and other receivables**				
	Financial assets	643	573	521	479
	Trade receivables	614	539	483	450
	Trade receivables: Inter-group			11	7
	Interest accrued	2	2	2	2
	Other receivables	27	32	25	20
	Non-financial assets	807	584	682	454
	Amount due from customers for contract work	580	473	460	355
	Prepayments and advances made	220	105	215	94
	Other receivables	7	6	7	5
		1 450	1 157	1 203	933

Trade receivables are non-interest bearing and are generally on 30 to 90 day terms. Specific impairments are made for identified doubtful debts.

	2012			2011		
	Trade receivables Rm	Other receivables Rm	Total Rm	Trade receivables Rm	Other receivables Rm	Total Rm
17 Trade and other receivables (continued)						
Impairment account reconciliation						
Individually impaired						
Group						
Balance at 1 April	72	-	72	92	-	92
Impairment losses recognised	13	-	13	7	-	7
Written off as uncollectible	(2)	-	(2)	(21)	-	(21)
Recovered during the year	(1)	-	(1)	(4)	-	(4)
Impairment losses reversed	(14)	-	(14)	(2)	-	(2)
	68	-	68	72	-	72
Company						
Balance at 1 April	71	-	71	90	-	90
Impairment losses recognised	13	-	13	7	-	7
Written off as uncollectible	(1)	-	(1)	(20)	-	(20)
Recovered during the year	(1)	-	(1)	(4)	-	(4)
Impairment losses reversed	(14)	-	(14)	(2)	-	(2)
	68	-	68	71	-	71

	Group		Company	
	2012 Rm	2011 Rm	2012 Rm	2011 Rm
18 Reinsurance asset				
Balance at 1 April	20	19		
Reinsurance income	1	1		
	21	20		

Densecure SOC Ltd, a subsidiary of the group, has a reinsurance asset with Santam Risk Finance Ltd, under which a performance bonus is payable to Densecure SOC Ltd when the annual premium paid exceeds the amount deductible in terms of costs and claims during the year.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

	Group		Company	
	2012 Rm	2011 Rm	2012 Rm	2011 Rm
19 Other financial assets and liabilities				
19.1 Other financial assets				
Derivatives	9	21	9	21
Foreign exchange contracts	-	16	-	16
Foreign exchange options	9	5	9	5
Firm commitments	29	-	29	-
Foreign exchange contracts designate as fair value hedges	12	-	12	-
Foreign exchange options designate as fair value hedges	17	-	17	-
	38	21	38	21
19.2 Other financial liabilities				
Derivatives	26	3	25	3
Foreign exchange contracts	9	3	8	3
Foreign exchange options	17	-	17	-
Embedded derivatives				
Foreign exchange embedded derivatives	15	36	14	28
Firm commitments	7	6	7	6
Foreign exchange contracts designate as fair value hedges	7	3	7	3
Foreign exchange options designate as fair value hedges	-	3	-	3
	48	45	46	37
20 Cash and cash equivalents				
Cash and short-term deposits (refer note 20.1)	1 074	920	1 009	865
Cash held on behalf of associates (refer note 20.2)	20	34	20	34
	1 094	954	1 029	899
20.1 Cash and short-term deposits				
Deposits				
Local call deposits	594	762	541	709
Cash in bank	500	192	488	190
Local banks	93	90	83	88
Foreign banks	407	102	405	102
	1 094	954	1 029	899
Less: Amount managed on behalf of associates (refer note 20.2)	(20)	(34)	(20)	(34)
	1 074	920	1 009	865

		Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
20.1	**Cash and short-term deposits (continued)**				
	Cash and cash equivalents are as per the cash flow statement. The weighted average effective interest rate on call deposits is 5.4% (2010/11: 6.1%). Interest on cash in bank is earned at market rates. The funds included in cash and short-term deposits are available on demand.				
	Included within cash and cash equivalents is R402m (2010/11 R0m) which is not immediately available for use in the business. This amount is held by a local bank in a foreign currency account as collateral for advance payment guarantees issued to a foreign customer. This is due to the withdrawal of a foreign bank from South Africa that reduced Denel's total banking facilities. Denel is in the process of negotiating new facilities to replace these facilities after which the amount should become available for use in the business.				
	(refer to note 27.1)				
20.2	**Cash held on behalf of associates**				
	Amount managed on behalf of associates (refer note 20.1)	20	34	20	34
	The amount disclosed as cash held on behalf of associates, is cash managed on behalf of the associates under service level agreements. Currently, the cash is held in the group's name until bank facilities are secured for these associates and the cash, guarantees and derivative financial instruments can be transferred to their own bank facilities (refer to note 23 and 27.1).				
21	**Issued capital**				
	Authorised				
	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
	Issued				
	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
	Share premium	4 251	4 251	4 251	4 251

At year-end, the number of issued Class A ordinary shares were 1 000 000 000 and the number of issued Class B ordinary shares were 225 049 663. The unissued shares are under the control of the 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.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
22	**Non-controlling interests**				
	Balance at 1 April	-	(34)		
	Share of net loss of subsidiaries	-	(47)		
	Acquisition of additional ownership interest in subsidiary	-	81		
		-	-		
	During the previous year, a holder of the non-controlling interest (Saab AB) in a subsidiary (DAe) exercised its share put option. Denel had to buy back 20% shareholding of the issued shares of DAe. Original capital contribution and a nominal value of shares totalling R66m was repaid on 1 April 2011. Denel now holds 100% of the issued shares of DAe.				
23	**Interest bearing loans and borrowings**				
	Unsecured loan				
	Unsecured loan from Saab AB	101	101	-	-
	The unsecured loan represents borrowings of DAe from its former non-controlling interest shareholder and bears no interest since 1 April 2010 (previously prime lending rate minus 2.0%). Originally the loan was repayable in February 2014, but due to the financial difficulty of the subsidiary, the amount will be repaid when the business is in a position to do so. The former non-controlling interest shareholder did subordinate the loan in favour of other debt.				
	Non-current portion of interest bearing loans and borrowings	101	101	-	-
	Current portion of interest bearing loans and borrowings	1 865	1 845	1 865	1 845
	Commercial paper	1 845	1 811	1 845	1 811
	Cash managed on behalf of associates	20	34	20	34
	Total interest bearing loans and borrowings	1 966	1 946	1 865	1 845

The borrowings have been raised through a commercial paper programme and have a coupon value of R1,85bn and are due for rollover at various stages during the next financial year. These borrowings are backed by government guarantees. The interest rate is linked to JIBAR.

The commercial paper programme is a short-term debt instrument issued as part of the Domestic Medium-Term Note (DMTN) programme and is secured by a government guarantee. Denel registered a R2,2bn DMTN programme with the JSE. Under the programme Denel could raise senior and/or subordinated notes up to the facility limit of R2,2bn with no limitation on the maturity date. The programme contains cross-default (indebtedness of outstanding amount equals or exceeds 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 guarantees, guarantee 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. These guarantees are due for rollover on 30 September 2012.

The undrawn borrowing facilities available for future operating activities amount to R390m (2010/11: R190m).
Refer to note 32.4 for fair value.

		Group		Company	
		2012	2011	2012	2011
23	**Interest bearing loans and borrowings (continued)**				
	Weighted average effective interest rates	%	%	%	%
	Local unsecured loans (fixed rate)	6.7	6.6	6.7	6.6
	Unsecured loan of former non-controlling interest shareholders	0.0	0.0	0.0	0.0
	Short-term bank borrowings (floating rate)	5.8	7.6	5.8	7.6
		Rm	Rm	Rm	Rm
	Summary of maturity of borrowings				
	Maturing within 12 months	1 865	1 845	1 865	1 845
	Maturing within 12 to 60 months	101	101	-	-
		1 966	1 946	1 865	1 845
24	**Advance payments received**				
	Non-current	920	205	920	205
	Current	447	655	412	601
		1 367	860	1 332	806
	The carrying amount of the advance payment is expected to be settled as follows:				
	Less than one year	447	655	412	601
	Between one and two years	206	54	206	54
	Between two and five years	637	150	637	150
	More than five years	77	1	77	1
		1 367	860	1 332	806

During the year the group entered into two large long-term contracts on which advance payments were received. These advance payments will be settled over a period of up to seven 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	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
25	**Provisions**				
25.1	**Non-current provisions**	260	369	246	338
	Contract risks and onerous contracts	36	123	22	92
	Product warranty and recall	28	54	28	54
	Site restoration	196	192	196	192
25.2	**Current provisions**	470	501	434	457
	Contract risks and onerous contracts	124	179	124	179
	Performance guarantees	41	36	41	36
	Product warranty and recall	63	64	60	64
	Site restoration	41	45	41	45
	Insurance	5	11	-	-
	Other	196	166	168	133
		730	870	680	795

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

	Contract risks and onerous contracts Rm	Performance guarantees Rm	Product warranty and recall Rm	Site restoration Rm	Insurance provision Rm	Other Rm	Total Rm
25 Provisions (continued)							
Reconciliation							
Group							
2012							
Balance at 1 April	302	36	118	237	11	166	870
Realised	(146)	-	(23)	(26)	(6)	(132)	(333)
Unused amounts reversed	(26)	-	(20)	-	-	(3)	(49)
Unwinding of discount on provisions	11	-	1	19	-	-	31
Charged to the income statement	19	5	15	7	-	165	211
	160	41	91	237	5	196	730
2011							
Balance at 1 April	313	65	119	265	6	260	1,028
Realised	(239)	-	(24)	(2)	-	(179)	(444)
Unused amounts reversed	(10)	(29)	(5)	(48)	-	(77)	(169)
Unwinding of discount on provisions	16	-	1	22	-	-	39
Charged to the income statement	222	-	27	-	5	162	416
	302	36	118	237	11	166	870
Company							
2012							
Balance at 1 April	271	36	118	237	-	133	795
Realised	(126)	-	(23)	(26)	-	(99)	(274)
Unused amounts reversed	(19)	-	(20)	-	-	(3)	(42)
Unwinding of discount on provisions	11	-	1	19	-	-	31
Charged to the income statement	9	5	12	7	-	137	170
	146	41	88	237	-	168	680
2011							
Balance at 1 April	268	65	118	265	-	215	931
Realised	(225)	-	(23)	(2)	-	(124)	(374)
Unused amounts reversed	(3)	(29)	(5)	(48)	-	(64)	(149)
Unwinding of discount on provisions	16	-	1	22	-	-	39
Charged to the income statement	215	-	27	-	-	106	348
	271	36	118	237	-	133	795

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.

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 within the group, 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 effected persons, as well as specific terms negotiated with individuals or their labour representatives. The carrying amount included in other provisions is R0m (2010/11: R3m) for the group and R0m (2010/11: R0m) for the 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 R150m (2010/11: R121m) for the group and R122m (2010/11: R90m) 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 units 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 R13m (2010/11: R16m) for the group and the company.

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. The carrying amount included in other provisions is R33m (2010/11: R27m) for the group and company.

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		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
26	**Trade and other payables**				
	Financial liabilities	801	636	715	580
	Trade payables	490	403	447	379
	Trade payables: Inter-group			5	3
	Interest accrued	17	-	17	-
	Other accruals	294	233	246	198
	Non-financial liabilities	25	22	25	22
	Amounts due to customers for work invoiced, not yet performed	25	21	25	21
	Other non-financial liabilities	-	1	-	1
		826	658	740	602

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 (refer note 23).

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
27	**Contingent liabilities**				
27.1	**Guarantees**				
	The following guarantees were issued by the group:				
	Advance payments guarantees *	1 318	1 009	1 318	1 009
	Performance guarantees	622	473	622	473
	Participating guarantees	11	-	11	-
	Guarantees to local authorities	7	7	7	7
	Guarantees to banks for credit facilities	545	90	545	90
	Other guarantees	111	45	111	45
	Total of guarantees issued	2 614	1 624	2 614	1 624
	Guarantees issued on behalf of associates	(181)	(218)	(181)	(218)
	Advance payments guarantees	(53)	(91)	(53)	(91)
	Performance guarantees	(59)	(63)	(59)	(63)
	Guarantees to banks for credit facilities	(55)	(55)	(55)	(55)
	Guarantees to local authorities	(1)	(2)	(1)	(2)
	Sundry guarantees	(13)	(7)	(13)	(7)
		2 433	1 406	2 433	1 406
	Recognised in the annual financial statements	(1 408)	(896)	(1 373)	(842)
	Advance payments received	(1 367)	(860)	(1 332)	(806)
	Provision for performance guarantees	(41)	(36)	(41)	(36)
		1 025	510	1 060	564

* *A local bank held R402m (2010/11: R0m) cash and cash equivalent as collateral for advance payment guarantees issued by the bank (refer note 20.1)*

27.2 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 R20m (2010/11: R16m). 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:

27.2.1 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. The customer has notified the Government of its intention to proceed with the matter. It is expected that the matter may involve legal proceedings in a South African court. It is not possible at this stage to estimate the potential damages and legal costs involved as the group has not been formally notified of the proceedings. The company has agreed to cooperate with this customer, which is likely to lead to a settlement of the matter.

27.2.2 The group was involved in a system development, this contract was cancelled by the customer on allegation of non-performance . At this stage, it is not possible to estimate the potential damages and other related costs as these have not yet been communicated to the group. It is envisaged that a legal process will ensue if the issue is not resolved.

27.3 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 R1,5bn and an estimated contract loss of approximately R1,4bn. This loss has not been raised as a provision following a written commitment 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.

27.4 Performance guarantee on behalf of a subsidiary

The company has provided a guarantee for the contract referred to in note 27.3 to the prime contractor, a European-based company. The company guaranteed that the subsidiary will discharge, in full, its contractual obligations and liabilities, including without limitation, counter claims or setoff. Negotiations are underway to revise certain key contract terms and conditions. As part these negotiations, an in principle agreement has been reached to cap any potential claim for liquidated damages to EUR2m.

27.5 Site restoration

Provision for site restoration has been calculated and raised, based on certain key assumptions, refer to note 1. A contingency of 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 ordnance 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 R35m (2010/11: R36m) for the group and company.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

27 Contingent liabilities (continued)

27.6 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 buyer's country
- participation in a business venture in the buyer's country
- exchange of countertrade obligations with companies from buyers' countries that have countertrade obligations in SA

The group is constantly in negotiations to conclude any outstanding portion of the countertrade obligation. The group issued guarantees to the value of R33m (2010/11: R32m) for 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 set off. 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.

The table below summarises the group's countertrade position:

	2012			2011		
	Export contracts Rm	Local defence contracts Rm	Total Rm	Export contracts Rm	Local defence contracts Rm	Total Rm
Countertrade obligation						
Total countertrade obligation	474	605	1,079	399	547	946
Obligation discharged	(14)	(556)	(570)	(12)	(485)	(497)
Outstanding obligation	460	49	509	387	62	449
To be settled by third party	-	(47)	(47)	-	(60)	(60)
Net obligation of the group	460	2	462	387	2	389
Penalties						
Maximum penalty for noncompliance	39	2	41	33	3	36
Third party obligation	-	(2)	(2)	-	(3)	(3)
Net group exposure	39	-	39	33	-	33
Guarantees issued						
Group issued	34	-	34	32	-	32
Third party guarantees	-	3	3	-	3	3
	34	3	37	32	3	35
Provision to settle obligation (refer note 25)	33	-	33	27	-	27

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
28	**Notes to the cash flow statement**				
	Reconciliation of profit with cash retained from operations				
	Net profit/(loss) before tax	58	144	4	117
	Adjusted for:	(52)	(559)	78	(293)
	(Profit)/loss on disposal of property, plant and equipment [1]	(5)	7	-	8
	Depreciation [1]	93	93	71	73
	Amortisation of intangible assets [1]	16	15	16	15
	Remeasurement of derivatives	35	53	34	39
	Remeasurement of embedded derivatives	(21)	(55)	(14)	(14)
	Remeasurement of firm commitments	(28)	6	(28)	6
	Interest paid (refer note 7)	145	157	147	163
	Interest received (refer note 7)	(61)	(37)	(62)	(48)
	Dividend received	-	-	(16)	(113)
	Decrease in provisions	(171)	(196)	(146)	(174)
	Impairment raised on property, plant and equipment [1]	(24)	2	-	(2)
	Impairment in subsidiaries [1]	-	-	65	243
	Share of profit of associates (refer note 13)	(42)	(115)	-	-
	Fair value adjustment of investment properties (refer note 4)	(92)	(42)	(92)	(42)
	Pension fund surplus apportionment	-	(463)	-	(463)
	Pension holiday	103	16	103	16
	Operating loss before changes in net current assets	6	(415)	82	(176)
	Changes in net current assets:	(197)	278	(248)	139
	(Increase)/decrease in inventories	(54)	143	(99)	12
	(Increase)/decrease in receivables	(293)	175	(270)	89
	Increase in reinsurance asset	(1)	(1)	-	-
	Increase/(decrease) in trade and other payables	151	(39)	121	38
	Cash utilised in operations	(191)	(137)	(166)	(37)

[1] *Refer note 3*

		Group 2012 Rm	Group 2011 Rm	Company 2012 Rm	Company 2011 Rm
29	**Capital commitments**				
	Approved and contracted for	57	30	37	23
	Land and buildings	14	-	14	-
	Plant and machinery	41	24	21	17
	Vehicles and office furniture	1	-	1	-
	Computer equipment	1	6	1	6
	Approved but not contracted for	13	7	13	7
	Land and buildings	12	-	12	-
	Plant and machinery	1	7	1	7
		70	37	50	30

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.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

	Buildings Rm	Plant and machinery Rm	Vehicles and office furniture Rm	Computer equipment Rm	Total Rm
30 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:					
Group					
2012					
Less than one year	58	1	2	3	64
Between one and five years	187	5	6	9	207
More than five years	236	4	-	-	240
	481	10	8	12	511
2011					
Less than one year	63	1	1	3	68
Between one and five years	31	1	4	2	38
More than five years	-	10	-	-	10
	94	12	5	5	116
Company					
2012					
Less than one year	58	-	2	2	62
Between one and five years	187	-	6	3	196
More than five years	236	-	-	-	236
	481	-	8	5	494
2011					
Less than one year	63	1	1	3	68
Between one and five years	31	-	4	-	35
	94	1	5	3	103

31 **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 R1m have not been included in the table below.

National Government and state controlled-units

Denel SOC Ltd is fully controlled by its sole shareholder, the government represented by the DPE.

The group operates in an economic environment currently dominated by business units directly or indirectly owned by the Government. As a result of the constitutional independence of all three spheres of Government, 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 government was provided by the NT.

Post-employment benefit plans

Other related parties also consist of post-retirement benefit plans (refer note 34).

Key Management Personnel

Key management is defined as individuals with the authority and responsibility for planning, directing and controlling the activities of the business unit. All individuals who are members of the Denel executive committee and the board of directors, as well as the business unit CEOs 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 unit. There were no material transactions other than the directors' emoluments as detailed on pages 72 to 73.

Business units within the group

Denel SOC Ltd is the ultimate parent company of the group. The company advanced loans to these units 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.

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.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

	National government Rm	Major national public units Rm	Between the company and its subsidiaries Rm	Associates Rm	Other related parties Rm
31 Related parties (continued)					
The following transactions were carried out with related parties:					
Group					
2012					
Purchases of goods	40	17	-	91	-
Sales of goods	1 114	1	-	18	-
Services rendered	610	2	-	14	-
Services received	8	15	-	175	-
Lease payments	-	63	-	-	-
Lease received	8	-	-	33	-
Guarantees issued to related parties	215	-	-	-	-
Guarantees issued to third parties on behalf of related parties	-	-	-	181	-
Guarantees issued to third parties by related parties	1 850	-	-	-	-
Interest received	-	-	-	7	-
Dividend received	-	-	-	16	-
Outstanding balances payable	121	7	-	114	-
Outstanding balances receivable	169	-	-	106	-
Advance payments received	360	-	-	-	-
Advance payments made	-	-	-	9	-
2011					
Purchases of goods	5	-	-	180	-
Sales of goods	1 231	23	-	65	-
Services rendered	606	3	-	15	-
Services received	4	22	-	45	21
Lease payments	-	63	-	-	-
Lease received	2	-	-	32	-
Guarantees issued to related parties	135	-	-	-	-
Guarantees issued to third parties on behalf of related parties	-	-	-	218	-
Guarantees issued to third parties by related parties	1 850	-	-	-	-
Interest received	-	1	-	3	-
Interest paid	-	-	-	1	-
Dividend received	-	-	-	33	-
Outstanding balances payable	4	1	-	80	-
Outstanding balances receivable	342	5	-	111	-
Advance payments received	468	-	-	-	-
Advance payments made	-	-	-	20	-

	National government Rm	Major national public units Rm	Between the company and its subsidiaries Rm	Associates Rm	Other related parties Rm
31 Related parties (continued)					
Company					
2012					
Purchases of goods	40	17	13	91	-
Sales of goods	996	1	1	14	-
Services rendered	372	-	59	14	-
Services received	6	15	14	176	-
Lease payments	-	63	-	-	-
Lease received	8	-	14	33	-
Guarantees issued to related parties	215	-	-	-	-
Guarantees issued to third parties on behalf of related parties	-	-	-	181	-
Guarantees issued to third parties by related parties	1 850	-	-	-	-
Interest received	-	-	5	7	-
Interest paid	-	-	2	-	-
Dividend received	-	-	-	16	-
Outstanding balances payable	3	4	5	114	-
Outstanding balances receivable	148	-	11	106	-
Advance payments received	360	-	-	-	-
Advance payments made	-	1	-	9	-
2011					
Purchases of goods	4	-	14	180	-
Sales of goods	1 115	23	3	53	-
Services rendered	364	1	47	15	-
Services received	4	22	15	45	-
Lease payments	-	63	-	-	-
Lease received	2	-	15	32	-
Guarantees issued to related parties	62	73	-	-	-
Guarantees issued to third parties on behalf of related parties	-	-	-	218	-
Guarantees issued to third parties by related parties	1 850	-	-	-	-
Interest received	-	1	14	3	-
Interest paid	-	-	5	1	-
Dividend received	-	-	80	33	-
Outstanding balances payable	4	-	3	80	-
Outstanding balances receivable	226	5	7	110	-
Advance payments received	445	-	-	-	-
Advance payments made	-	-	-	20	-

Post-employment benefit plans (refer note 34)

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
31	**Related parties (continued)**				
	Compensation paid to key management personnel (including information in the *directors' report)*				
	Short-term employee benefits	37	33	30	29
	Post-employee benefits	2	1	2	1
		39	34	32	30

32 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 group audit and risk 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 group audit and risk 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 group audit and risk 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 group audit and risk committee.

32.1 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 group audit and risk 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. Divisions and subsidiaries 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 business units within the group (includes but is not limited to payment history);
- The most recent credit rating of the country that the potential customer operates in, from the group's treasury department. 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 group audit and risk 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. Counter parties are assessed based on their official FitchRatings rating. Counter parties are approved by the group audit and risk committee and any rating agency publications and financial news regarding counter parties are regularly monitored by the treasury department. The group limits its exposure by spreading investments over the approved counter parties, as well as by investing with counter parties, 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 GCEO.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		2012			2011		
		Domestic Rm	Foreign Rm	Total Rm	Domestic Rm	Foreign Rm	Total Rm
32	**Financial risk management (continued)**						
	Credit exposure and concentration of credit risk (continued)						
	The carrying amount of financial assets represents the maximum credit exposure at the reporting date. The following table represents the group's concentration of risk for all non-derivative financial assets:						
	Group						
	Trade receivables	240	374	614	314	225	539
	Government and related entitles	171	90	261	256	137	393
	Non-government units	69	284	353	58	88	146
	Sundry receivables	27	-	27	24	8	32
	Government and related entitles	12	-	12	9	-	9
	Non-government units	15	-	15	15	8	23
	Interest receivable (non-government)	2	-	2	2	-	2
	Loans and receivables	479	-	479	562	-	562
	Government and related entitles	-	-	-	5	-	5
	Non-government units	479	-	479	557	-	557
		748	374	1 122	902	233	1 135
	Company						
	Trade receivables	214	269	483	287	163	450
	Government and related entitles	149	60	209	232	124	356
	Non-government units	65	209	274	55	39	94
	Sundry receivables	25	-	25	20	-	20
	Government and related entitles	10	-	10	6	-	6
	Non-government units	15	-	15	14	-	14
	Interest receivable (non-government)	2	-	2	2	-	2
	Loans and receivables	479	-	479	562	-	562
	Government and related entitles	-	-	-	5	-	5
	Non-government units	479	-	479	557	-	557
		720	269	989	871	163	1 034

	Receivables not impaired Rm	Receivables impaired Rm	Impairment amount Rm	Carrying value Rm
32 Financial risk management (continued)				
Credit exposure and concentrations of credit risk (continued)				
Ageing				
The ageing of financial assets at the reporting date is included below. The ageing categories include:				
Group				
2012				
Trade receivables	614	68	(68)	614
Not past due	480			480
Not past due, but impaired		7	(7)	-
Past due				
Less than 30 days	46	-	-	46
30 to 60 days	26	-	-	26
61 to 90 days	17	4	(4)	17
More than 90 days	45	57	(57)	45
Other receivables	27	-	-	27
Not past due, not impaired				
Interest accrued	2	-	-	2
Not past due, not impaired				
Loans and other receivables	479	-	-	479
Not past due, not impaired				
Current portion	193	-	-	193
Non-current portion	286	-	-	286
	1 122	68	(68)	1 122
2011				
Trade receivables	539	72	(72)	539
Not past due	405			405
Past due				
Less than 30 days	79	58	(58)	79
30 to 60 days	36	-	-	36
61 to 90 days	8	-	-	8
More than 90 days	11	14	(14)	11
Other receivables	32	-	-	32
Not past due, not impaired	24			24
Past due				
Less than 30 days	5	-	-	5
61 to 90 days	1	-	-	1
More than 90 days	2	-	-	2
Interest accrued	2	-	-	2
Not past due, not impaired				
Loans and other receivables	562	-	-	562
Not past due, not impaired				
Current portion	191	-	-	191
Non-current portion	371	-	-	371
	1 135	72	(72)	1 135

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Receivables not impaired Rm	Receivables impaired Rm	Impairment amount Rm	Carrying value Rm
32	**Financial risk management (continued)**				
	Credit exposure and concentrations of credit risk (continued)				
	Ageing				
	The ageing of financial assets at the reporting date is included below. The ageing categories include:				
	Company				
	2012				
	Trade receivables	483	68	(68)	483
	Not past due	381			381
	Not past due, but impaired		7	(7)	-
	Past due				
	Less than 30 days	35	-	-	35
	30 to 60 days	18	-	-	18
	61 to 90 days	17	4	(4)	17
	More than 90 days	32	57	(57)	32
	Other receivables	25	-	-	25
	Not past due, not impaired				
	Interest accrued	2	-	-	2
	Not past due, not impaired				
	Loans receivable	479	-	-	479
	Not past due, not impaired				
	Current portion	193	-	-	193
	Non-current portion	286	-	-	286
		989	68	(68)	989
	2011				
	Trade receivables	450	71	(71)	450
	Not past due	333			333
	Not past due, but impaired		-	-	-
	Past due				
	Less than 30 days	69	58	(58)	69
	30 to 60 days	30	-	-	30
	61 to 90 days	8	-	-	8
	More than 90 days	10	13	(13)	10
	Other receivables	20	-	-	20
	Not past due, not impaired	15			15
	Past due				
	Less than 30 days	4	-	-	4
	More than 90 days	1	-	-	1
	Interest accrued	2	-	-	2
	Not past due, not impaired				
	Loans receivable	562	-	-	562
	Not past due, not impaired				
	Current portion	191	-	-	191
	Non-current portion	371	-	-	371
		1 034	71	(71)	1 034

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
32	**Financial risk management (continued)**				
	Credit exposure and concentrations of credit risk (continued)				
	Ageing				
	The ageing of financial assets at the reporting date is included below. The ageing categories include:				
	Security held over non-derivative financial assets				
	Irrevocable confirmed Letters of Credit				
	• Confirmed by local banks	-	13	-	13
	• Confirmed by foreign banks	238	26	238	26
	Unconfirmed Letters of Credit	64	4	64	4
		302	43	302	43

32.2 Liquidity risk

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. Updated cash flow information and projections of future cash flows are received from divisions and subsidiaries 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. The group received government guarantees of R1,85bn to raise borrowings. These guarantees expire on 30 September 2012.

Surplus funds are deposited in liquid assets (i.e. negotiable certificates of deposits and call deposits) (refer note 20).

	Group		Company	
	2012 Rm	2011 Rm	2012 Rm	2011 Rm
Undrawn credit facilities	390	190	390	190

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.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Contractual undiscounted cash flows				
		Carrying amount Rm	Total cash flows Rm	Less than 3 months Rm	Between 3 and 12 months Rm	Between 1 and 5 years Rm
32	**Financial risk management (continued)**					
32.2	**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:					
	Group					
	2012					
	Interest bearing borrowings	1 845	1 872	712	1 160	-
	Non-interest bearing borrowings	101	101	-	-	101
	Loans from associates	20	20	20	-	-
	Trade and other payables	801	801	691	110	-
	Derivative financial liabilities	26	26	2	10	14
		2 793	2 820	1 425	1 280	115
	2011					
	Interest bearing borrowings	1 811	1 849	25	1 824	-
	Non-interest bearing borrowings	101	101	-	-	101
	Loans from associates	34	34	34	-	-
	Trade and other payables	636	636	536	100	-
	Derivative financial liabilities	3	3	1	2	-
		2 585	2 623	596	1 926	101
	Company					
	2012					
	Interest bearing borrowings	1 845	1 872	712	1 160	-
	Loans from associates	20	20	20	-	-
	Trade and other payables	715	715	629	86	-
	Derivative financial liabilities	25	26	2	10	14
		2 605	2 633	1 363	1 256	14
	2011					
	Interest bearing borrowings	1 811	1 849	25	1 824	-
	Loans from associates	34	34	34	-	-
	Trade and other payables	580	580	505	75	-
	Derivative financial liabilities	3	3	1	2	-
		2 428	2 466	565	1 901	-

32.3 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.

Divisions and Subsidiaries

The divisions and subsidiaries are responsible for the preparation and presentation of market risk information as it affects the relevant business unit. Information will be submitted to treasury where it is monitored and further analysed to be used in the decision-making process. In certain instances a business unit will prepare and use market risk information for its own purposes.

Treasury

Treasury is responsible for reporting to the group audit and risk 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 borrowings. There is no other exposure to fair value interest rate risk as all fixed rate financial instruments are measured at amortised cost.

The group audit and risk committee determines the interest rate risk strategy based on economic expectations and reports received from treasury. Treasury 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.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Group		Company	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
32	**Financial risk management (continued)**				
32.3	**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				
	Commercial paper	1 845	1 811	1 845	1 811
	Loans and other receivables	-	5	-	5
	Variable rate instruments				
	Cash and short-term deposits	1 074	920	1 009	865
	Cash held on behalf of associates	20	34	20	34
	Loans and other receivables	479	557	479	557
	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 or loss.				
	Cash flow sensitivity analysis for variable rate instruments				
	A change of 50 basis points in interest rates at the reporting date would have increased/decreased profit or 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 or loss.				
	Cash and cash equivalents	8	8	8	7

Net effect on profit or loss is equal but opposite for a 50 basis points increase on the financial instruments listed above.

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 divisions/ subsidiaries. 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 executive committee 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.

		2012			2011		
		US Dollar (USD) Millions	Euro (EUR) Millions	Sterling (GBP) Millions	US Dollar (USD) Millions	Euro (EUR) Millions	Sterling (GBP) Millions
32	**Financial risk management (continued)**						
32.3	**Market risk (continued)**						
	The group's exposure to currency risk was as follows based on the notional amounts:						
	Group						
	Assets	95	57	-	60	6	-
	Trade receivables	21	18	-	16	5	-
	Controlled Foreign Currency accounts (CFC)	-	39	-	15	-	-
	Embedded derivatives (export sales)	8	-	-	16	-	-
	Firm commitment (export sales)	66	-	-	13	1	-
	Liabilities	(1)	-	-	(1)	(4)	-
	Trade payables	(1)	-	-	-	(2)	-
	Firm commitment (import)	-	-	-	(1)	(2)	-
	Gross balance sheet exposure	94	57	-	59	2	-
	Forecast transactions: sales	19	17	-	2	1	-
	Forecast transactions: purchases	(1)	(6)	-	(2)	-	-
	Gross exposure	112	68	-	59	3	-
	Forward Exchange Contracts						
	Export sales	(24)	(17)	-	(20)	(11)	(1)
	Import	1	6	-	3	4	-
	Foreign Currency Options (Zero Cost Collars)						
	Export sales	(49)	(1)	-	(11)	-	-
	Net exposure	40	56	-	31	(4)	(1)

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FOR THE YEAR ENDED 31 MARCH 2012

		2012			2011		
		US Dollar (USD) Millions	Euro (EUR) Millions	Sterling (GBP) Millions	US Dollar (USD) Millions	Euro (EUR) Millions	Sterling (GBP) Millions
32	**Financial risk management (continued)**						
32.3	**Market risk (continued)**						
	Company						
	Assets	82	57	-	48	5	-
	Trade receivables	11	18	-	10	5	-
	Controlled Foreign Currency accounts (CFC)	-	39	-	14	-	-
	Embedded derivatives (export sales)	5	-	-	11	-	-
	Firm commitment (export sales)	66	-	-	13	-	-
	Liabilities	(1)	-	-	(1)	(4)	-
	Trade payables	(1)	-	-	-	(2)	-
	Firm commitment (import)	-	-	-	(1)	(2)	-
	Balance sheet exposure	81	57	-	47	1	-
	Forecast transactions: sales	19	17	-	2	1	-
	Forecast transactions: purchases	(1)	(6)	-	(2)	-	-
	Gross exposure	99	68	-	47	2	-
	Forward Exchange Contracts						
	Export sales	(23)	(17)	-	(20)	(11)	(1)
	Import	1	6	-	3	4	-
	Foreign Currency Options (Zero Cost Collars)						
	Export sales	(49)	(1)	-	(11)	-	-
	Net exposure	28	56	-	19	(5)	(1)
	A 5% strengthening of the Rand against the following currencies at 31 March would have increased/(decreased) profit or loss by the following amounts:						
	Group	16	29	-	6	2	-
	Company	11	29	-	6	1	-

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 or loss.

	2012			2011		
	Foreign currency notional amount Rm	Local currency amount Rm	Fair value Rm	Foreign currency notional amount Rm	Local currency amount Rm	Fair value Rm
32 Financial risk management (continued)						
32.3 Market risk (continued)						
Foreign currency derivatives						
The fair value of foreign currency derivatives are disclosed in note 19.1.						
The following foreign exchange contracts existed at 31 March:						
Purchase contracts						
US Dollar (USD)	1	9	9	3	24	24
Euro (EUR)	6	63	63	4	37	35
Sterling (GBP)	-	-	-	-	3	3
Swedish Krona (SEK)	2	2	2	-	-	-
Swiss Franc (CHF)	1	13	13	-	-	-
Other		1	1		-	-
		88	88		64	62
Sales contracts						
US Dollar (USD)	24	184	185	20	139	128
Euro (EUR)	17	185	186	11	105	102
Sterling (GBP)	-	-	-	1	9	9
Singapore Dollar (SGD)	-	-	-	-	2	2
Swiss Franc (CHF)	-	-	-	1	8	8
		369	371		263	249
The following foreign exchange options existed at 31 March:						
Sales contracts						
US Dollar (USD)	49	378	361	11	75	80
Euro (EUR)	1	6	6	-	-	-
		384	367		75	80

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

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		2012 Foreign currency notional amount				2011 Foreign currency notional amount			
		Million 1 Year	Million 2 Years	Million 3-5 Years	Million Total	Million 1 Year	Million 2 Years	Million 3-5 Years	Million Total
32	**Financial risk management (continued)**								
32.3	**Market risk (continued)**								
	Maturity table								
	Foreign exchange contracts								
	Purchase contracts								
	US Dollar (USD)	1	-	-	1	3	-	-	3
	Euro (EUR)	6	-	-	6	4	-	-	4
	Swedish Krona (SEK)	2	-	-	2	-	-	-	-
	Swiss Franc (CHF)	1	-	-	1	-	-	-	-
	Sales contracts								
	US Dollar (USD)	24	-	-	24	14	6	-	20
	Euro (EUR)	-	17	-	17	10	-	-	10
	Sterling (GBP)	-	-	-	-	1	-	-	1
	Swiss Franc (CHF)	-	-	-	-	1	-	-	
	Foreign exchange options								
	Sales contracts								
	US Dollar (USD)	15	26	8	49	8	3	-	11
	Euro (EUR)	1	-	-	1	-	-	-	-

Foreign exchange embedded derivatives and firm commitment

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, contain a foreign exchange embedded derivative (to sell or buy the equivalent amount of foreign currency), are separated and accounted for at fair value even though the contract is not recognised.

Denel views the USD, GBP and EUR as common currencies. The embedded derivatives recognised relate to balances of existing contracts at the date of the change of accounting policy. The changed accounting policy is applied prospectively from the said date in line with the transition requirements of IFRIC 9 and IAS 8.

		2012			2011		
		Foreign currency notional amount Million	Local currency amount Rm	Fair value Rm	Foreign currency notional amount Million	Local currency amount Rm	Fair value Rm
32	**Financial risk management (continued)**						
32.3	**Market risk (continued)**						
	Foreign currencies						
	Export transactions						
	Embedded derivatives						
	US Dollar (USD)	8	64	49	16	140	119
	Firm commitment relating to foreign exchange contracts						
	US Dollar (USD)	17	136	134	8	59	56
	Euro (EUR)	-	-	-	1	9	9
	Sterling (GBP)	-	-	-	-	6	6
	Swiss Franc (CHF)	-	-	-	1	9	9
			136	134		83	80
	Firm commitment relating to foreign exchange options						
	US Dollar (USD)	49	378	361	5	30	33
	Euro (EUR)	-	2	2	-	-	-
			380	363		30	33
	Import transactions						
	Firm commitment relating to foreign exchange contracts						
	US Dollar (USD)	-	-	-	-	1	1
	Euro (EUR)	-	1	1	2	11	11
			1	1		12	12

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

	2012 Foreign currency notional amount				2011 Foreign currency notional amount			
	Million 1 Year	Million 2 Years	Million 3-5 Years	Million Total	Million 1 Year	Million 2 Years	Million 3-5 Years	Million Total
32 Financial risk management (continued)								
32.3 Market risk (continued)								
Maturity table								
Export transactions								
Embedded derivatives								
US Dollar (USD)	5	3	-	8	10	4	2	16
Firm commitment relating to foreign exchange contracts								
US Dollar (USD)	17	-	-	17	8	-	-	8
Euro (EUR)	-	-	-	-	1	-	-	1
Sterling (GBP)	-	-	-	-	1	-	-	1
Swiss Franc (CHF)	-	-	-	-	1	-	-	1
Firm commitment relating to foreign exchange options								
US Dollar (USD)	15	26	8	49	5	-	-	5
Euro (EUR)	1	-	-	1	-	-	-	-

Import transactions

Firm commitment relating to foreign exchange contracts

The maturity of all import transaction firm commitments is within one year.

Commodity risk

Commodity risk arises from the movement in commodity prices. The group purchases mainly two commodities as raw material (i.e. copper and zinc). The risk is managed by hedging the purchase price using commodity swap contracts. No transactions of a speculative nature are entered into.

Commodity swap derivatives

The fair value of the commodity swap derivatives are disclosed in note 19.2.

	2012			2011		
	Units in tons	Local currency amount Rm	Fair value Rm	Units in tons	Local currency amount Rm	Fair value Rm
The following commodity swap contracts existed at 31 March:						
Copper swaps	24	2	2	254	17	17
Zinc swaps	148	2	2	65	1	1
		4	4		18	18

	2012 Units in tons				2011 Units in tons			
	1 Year	2 Years	3-5 Years	Total	1 Year	2 Years	3-5 Years	Total
32 Financial risk management (continued)								
32.3 Market risk (continued)								
Maturity table								
Copper swaps	24	-	-	24	230	24	-	254
Zinc swaps	148	-	-	148	57	8	-	65

	Notes	Loans and receivables Rm	Liabilities at amortised cost Rm	Held for trading Rm	Total carrying value Rm	Fair value Rm
32.4 Fair value of financial assets and liabilities						
The categorisation of each class of financial asset and liability, including their fair values, are included below:						
Group						
2012						
Financial assets						
Loans and receivables	14	377			377	377
Associates: Loans receivable	14	102			102	102
Trade and other receivables	17	643			643	643
Derivative financial assets	19.1			38	38	38
Cash and cash equivalents	20.1	1 074			1 074	1 074
Cash held on behalf of associates	20.2	20			20	20
Financial liabilities						
Interest bearing borrowings	23		(1 845)		(1 845)	(1 860)
Non interest bearing borrowings	23		(101)		(101)	(101)
Associates: Borrowings	23		(20)		(20)	(20)
Trade and other payables	26		(801)		(801)	(801)
Derivative financial liabilities	19.2			(48)	(48)	(48)
		2 216	(2 767)	(10)	(561)	(576)
2011						
Financial assets						
Loans and receivables	14	457			457	457
Associates: Loans receivable	14	105			105	105
Trade and other receivables	17	573			573	573
Derivative financial assets	19.1			21	21	21
Cash and cash equivalents	20.1	920			920	920
Cash held on behalf of associates	20.2	34			34	34
Financial liabilities						
Interest bearing borrowings	23		(1 811)		(1 811)	(1 813)
Non interest bearing borrowings	23		(101)		(101)	(101)
Associates: Borrowings	23		(34)		(34)	(34)
Trade and other payables	26		(636)		(636)	(636)
Derivative financial liabilities	19.2			(45)	(45)	(45)
		2 089	(2 582)	(24)	(517)	(519)

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Notes	Loans and receivables Rm	Liabilities at amortised cost Rm	Held for trading Rm	Total carrying value Rm	Fair value Rm
32	**Financial risk management (continued)**						
32.4	**Fair value of financial assets and liabilities (continued)**						
	Company						
	2012						
	Financial assets						
	Loans and receivables	14	377			377	377
	Associates: Loans receivable	14	102			102	102
	Trade and other receivables	17	521			521	521
	Derivative financial assets	19.1			38	38	38
	Cash and cash equivalents	20.1	1 009			1 009	1 009
	Cash held on behalf of associates	20.2	20			20	20
	Financial liabilities						
	Interest bearing borrowings	23		(1 845)		(1 845)	(1 860)
	Associates: Borrowings	23		(20)		(20)	(20)
	Trade and other payables	26		(715)		(715)	(715)
	Subsidiaries: Borrowings			(58)		(58)	(58)
	Derivative financial liabilities	19.2			(46)	(46)	(46)
			2 029	(2 638)	(8)	(617)	(632)
	2011						
	Financial assets						
	Loans receivable	14	457			457	457
	Associates: Loans receivable	14	105			105	105
	Trade and other receivables	17	479			479	479
	Derivative financial assets	19.1			21	21	21
	Cash and cash equivalents	20.1	865			865	865
	Cash held on behalf of associates	20.2	34			34	34
	Financial liabilities						
	Interest bearing borrowings	23		(1 811)		(1 811)	(1 813)
	Associates: Borrowings	23		(34)		(34)	(34)
	Trade and other payables	26		(580)		(580)	(580)
	Subsidiaries: Borrowings			(62)		(62)	(62)
	Derivative financial liabilities	19.2			(37)	(37)	(37)
			1 940	(2 487)	(16)	(563)	(565)

Determination of fair values

Non-derivative financial instruments

Quoted market prices at reporting date have been used to determine the fair value of loan and receivables and interest bearing borrowings. Where there is no quoted market price a valuation technique, most commonly discounted cash flows, was used. For trade receivables and payables the fair value was determined using discounted cash flow method at market related interest rate. All other financial assets and liabilities carrying amount approximates fair value.

Derivative financial instruments

The fair value of derivative financial instruments is determined using accepted valuation techniques and incorporating market quoted prices.

Fair value hierarchy

The group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

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 19 and falling within level 2 of the hierarchy. During the year there were no transfers between any of the levels of fair value measurements.

33 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 to the directors' report 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 R3,5bn with an additional R700m to be injected into the company during the 2012/13 financial year. The shareholder has in the interim provided government guarantees 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 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. The company maintained a solvency margin higher than the statutory requirement of 25%.

34 Pension and other post-retirement obligations

The group offers pension and post-retirement benefits through one defined contribution plan and two defined benefit plans.

34.1 Denel Pension Fund

The Denel Pension Fund (DenPen), a defined benefit plan, became a pensioners alone fund on 1 September 2010 as Denel withdraw as principal employer from the fund.

The group will make no further contributions to this defined benefit pension plan.

34.2 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.

The fund is valued annually by independent actuaries using the projected unit credit method. The result of the valuation carried out at 31 March 2012 indicated a surplus of R302m (2010/11: R477m).

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.

Due to the current surplus of this fund, the group only contributes to the fund when a qualifying member goes on early retirement and it is, therefore, unable to determine the contribution for 2013.

During the year a further 245 members accepted the second phase buy-out offer and were settled on 1 April 2012. The group is exploring further options for the remaining members to limit the financial risk to the group. Refer to the directors' report for details.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Denel Pension Fund		Denel Medical Benefit Trust	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
34	**Pension and other post-retirement obligations (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	n/a	4 129	674	681
	Service cost benefits earned during the year	n/a	1	8	12
	Interest cost on projected benefit obligation	n/a	186	61	62
	Actuarial (gain)/ losses	n/a	(651)	113	(52)
	Benefits paid	n/a	(120)	(30)	(39)
	Settlement cost	n/a	(3 545)		
	Liability buy-out			(71)	10
	Present value of funded obligations at 31 March	n/a	-	755	674
	Change in plan assets				
	Fair value of plan assets at 1 April	n/a	5 129	1 151	1 248
	Expected return on plan assets	n/a	245	103	126
	Actuarial gains	n/a	(277)	(54)	(197)
	Employer and member contributions	n/a	-	1	3
	Benefits paid	n/a	(120)	(30)	(39)
	Settlement cost	n/a	(4 514)		
	Surplus apportionment to the company	n/a	(463)		
	Liability buy-out			(114)	10
	Fair value of plan assets at 31 March	n/a	-	1 057	1 151
	Fund excess	n/a	-	302	477
	Excess not recognised	n/a	-	302	477
	Unrecognised actuarial gains	n/a	-	-	-
	Net benefit expenses				
	Service cost	n/a	1	8	12
	Interest cost	n/a	186	61	62
	Expected return on plan assets	n/a	(245)	(103)	(126)
	Net actuarial loss recognised during the year	n/a	-	113	(52)
	Income	n/a	(58)	79	(104)
	The principal actuarial assumptions used for accounting purposes were:	%	%	%	%
	Expected return on plan assets	n/a	8.50	9.90	8.97
	Future salary increase	n/a	6.25		
	Future pension increase	n/a	6.30		
	Discount rate	n/a	8.25		
	Inflation rate	n/a	5.25		
	Expected medical inflation			7.90	6.97

The Medical Benefit Trust'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% per annum.

		Denel Pension Fund		Denel Medical Benefit Trust	
		2012 Rm	2011 Rm	2012 Rm	2011 Rm
34	**Pension and other post-retirement obligations (continued)**				
	The beneficiary members from the funds are as follows:				
	Active members	n/a	-	374	719
	Retired members	n/a	-	1 720	1 669
	The beneficiary members who accepted the buy-out offer are as follows:				
	Active members			245	-
	Retired members			-	-

	2012 Rm	2011 Rm	2010 Rm	2009 Rm	2008 Rm
Amounts for the current and previous four periods are as follows:					
Denel Pension Fund					
Defined benefit obligation	n/a	-	(4 129)	(3 278)	(3 248)
Plan assets	n/a	-	5 129	4 493	4 889
Surplus	n/a	-	1 000	1 215	1 641
Experience adjustments on plan liabilities	n/a	810	971	110	278
Experience adjustments on plan assets	n/a	(277)	(496)	(572)	(324)
Denel Medical Benefit Trust					
Defined benefit obligation	(755)	(674)	(681)	(1 323)	(1 076)
Plan assets	1 057	1 151	1 248	1 768	1 894
Surplus	302	477	567	445	818
Experience adjustments on plan liabilities	(25)	(4)	(33)	10	(10)

	2012		2011	
	Increase Rm	Decrease Rm	Increase Rm	Decrease Rm
A 2% change in assumed healthcare cost trend rates would have the following effects:				
Effect on defined benefit obligation	(197)	166	(204)	166

34.3 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 of 1956 (Act No. 24 of 1956). The contributions are charged to the income statement as incurred.

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

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35 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, OTR and Denel Integrated System Solutions

Aviation: Denel Aviation, Rooivalk and Denel Personnel Solutions SOC Ltd

Land systems: Denel Land Systems and Mechem SOC Ltd

Munitions: PMP

Non-core: Property divisions and property subsidiaries

Corporate services: Corporate activities mainly consist of corporate office and treasury functions, 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 and DTA.

The results of business units with revenue less than 10% of the group revenue are aggregate within an operating segment which products and services closes relates to that of the specific business unit.

More detail on the business units is stated in the *business unit overview* on pages 30 to 41.

	Aero-structures Rm	Aero-space systems Rm	Aviation Rm	Land Systems Rm	Munitions Rm	Non-core and Corporate services Rm	Con-solidation entries Rm	Total Rm
35 Segment reporting (continued)								
2012								
Segment revenue	260	894	1 047	847	499	319	(298)	3 568
Sales to external customers	247	846	1 018	847	474	136		3 568
Inter-group sales	13	48	29	-	25	183	(298)	-
Segment result	(74)	45	60	44	8	30	(13)	100
Pension fund surplus apportionment								-
Finance charges								(84)
Share of results of associates								42
Taxation								(17)
Loss for the year								41
Segment assets	333	1 362	514	1 231	602	5 503	(3 914)	5 631
Deferred tax assets								11
Total assets								5 642
Segment liabilities	820	1 187	493	1 077	92	3 827	(2 556)	4 940
Deferred tax liabilities								7
Total liabilities								4 947
Cash flows from:								
Operating activities	(66)	417	(121)	90	(9)	151	(102)	360
Investing activities	1	(103)	(4)	(20)	(15)	(240)	231	(150)
Financing activities	65	10	63	227	-	525	(960)	(70)
Capital expenditure	12	38	4	20	14	15	-	103
Impairment losses	-	-	40	2	29	243	(233)	81
Impairment losses reversed	(75)	(9)	-	(2)	(22)	(171)	167	(112)
Depreciation/ amortisation in respect of segment assets	15	37	9	13	16	19	-	109
Revenue from major customers								
SA National Government	119	446	773	227	152	15	-	1 732
Significant non-cash items:								
Fair value adjustment	-	-	-	-	-	92	-	92
(Profit)/loss on disposal of property, plant and equipment	(5)	-	-	-	-	-	-	(5)

NOTES TO THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 MARCH 2012

		Aero-structures Rm	Aero-space systems Rm	Aviation Rm	Land Systems Rm	Munitions Rm	Non-core and Corporate Services Rm	Con-solidation entries Rm	TOTAL Rm
35	**Segment reporting (continued)**								
	2011								
	Segment revenue	281	1 002	736	705	501	321	(294)	3 252
	Sales to external customers	267	960	676	704	494	151		3 252
	Inter-group sales	14	42	60	1	7	170	(294)	-
	Segment result	(223)	(48)	(155)	26	14	(57)	129	(314)
	Pension fund surplus apportionment								463
	Finance charges								(120)
	Share of results of associates								115
	Taxation								(33)
	Profit for the year								111
	Segment assets	351	991	544	577	573	4 982	(2 988)	5 030
	Deferred tax assets								8
	Total assets								5 038
	Segment liabilities	760	874	634	453	74	3 274	(1 690)	4 379
	Deferred tax liabilities								5
	Total liabilities								4 384
	Cash flows from:								
	Operating activities	(99)	121	103	(24)	26	10	41	178
	Investing activities	(5)	(62)	(3)	(11)	(13)	(181)	74	(201)
	Financing activities	75	29	19	-	-	(171)	(155)	(203)
	Capital expenditure	6	53	3	11	13	2	-	88
	Impairment losses	35	1	43	3	21	248	(219)	132
	Impairment losses reversed	(65)	(4)	(12)	(8)	(18)	(10)	-	(117)
	Depreciation/ amortisation in respect of segment assets	15	37	11	13	15	17	-	108
	Revenue from major customers								
	SA National Government	116	501	619	474	120	9	-	1 839
	Significant non-cash items:								
	Fair value adjustment	-	-	-	-	-	42	-	42
	(Profit)/loss on disposal of property, plant and equipment	(1)	8	-	-	-	-	-	7

		2012				2011			
		Share capital issued [2]	Share investment by Denel SOC Ltd [2]	Amounts owing to/(by) Denel SOC Ltd [2]	Effective shareholding	Share capital issued [2]	Share investment by Denel SOC Ltd [2]	Amounts owing to/(by) Denel SOC Ltd [2]	Effective shareholding
		Rm	Rm	Rm	%	Rm	Rm	Rm	%
36	**Subsidiaries and associates**								
	The following unlisted companies are subsidiaries or associates of Denel SOC Ltd								
	Subsidiaries								
	Bonaero Park (Pty) Ltd	-	-	-	-	-	-	-	100
	Denel International Ltèe (incorporated in Mauritius)	-	-	-	-	-	-	-	100
	Denel Personnel Solutions SOC Ltd	-	-	(57)	100	-	-	(44)	100
	Denel Properties (Pty) Ltd	-	-	-	-	-	-	-	100
	Denel Aerostructures SOC Ltd	789	789	601	100	789	789	536	100
	Densecure SOC Ltd	8	8	-	100	8	8	-	100
	La Forge Manufacturing (Pty) Ltd	-	-	-	-	-	-	85	100
	Mechem SOC Ltd	63	63	4	100	63	63	(18)	100
	Denel Do Brasil Tecnologia Aplicada E Participacoes Limitada (incorporated in Brazil)	-	-	-	[1]	-	-	-	[1]
	Total investment		860	548			860	559	
	Less: Accumulated impairment of investment		(789)	(601)			(789)	(621)	
	Net investment of Denel SOC Ltd		71	(53)			71	(62)	
	Associates								
	Turbomeca Africa (Pty) Ltd		49	-	49		49	-	49
	Carl Zeiss Optronics (Pty) Ltd		57	-	30		57	-	30
	Rheinmetall Denel Munition (Pty) Ltd		371	102	49		371	105	49
	Net investment of Denel SOC Ltd		477	102			477	105	

	2012 Rm	2011 Rm
Aggregated loss of subsidiaries	(47)	(148)

[1] *Shares are not held by the group but effective management control is exercised in these units*
[2] *Amounts smaller than R1m due to rounding are not reflected against the units but in aggregate on this page*

INFORMATION **SERVICE**

GLOSSARY

Acronym	Full description
AAD	Africa Aerospace and Defence
ABET	Adult Basic Education and Training
Adv	Advocate
AGM	Annual General Meeting
AMD	South African Aerospace, Maritime and Defence Industries Association
AUD	Australian Dollar
BAC	Battle area clearance
B-BBEE	Broad-based black economic empowerment
BEE	Black economic empowerment
bn	Billion
Board	Board of directors
BRICS	Brazil, Russia, India, China and South Africa
CAF	Chief of Air Force (South Africa)
CCF	Community consultative forum
CEO	Chief executive officer
CFC	Controlled foreign currency
CFO	Chief financial officer
CHF	Swiss Franc (currency unit)
CNES	National Centre for Space Studies
Companies Act	South African Companies Act, No.71 of 2008
CPP	Commercial Paper Programme
CRM	Customer relationship management
CRT	Cathode ray tube
CSANDF	Chief of South African National Defence Force
CSDP	Competitive supplier development policy
CSIR	Council for Scientific and Industrial Research
CVO	Contract variation order
CZO	Carl Zeiss Optronics (Pty) Ltd
DAe	Denel Aerostructures SOC Ltd
DAS	Denel Aerospace Systems
DEKRA	Deutscher Kraftfahrzeug-Überwachungsverein e.V.
Deniprop	Denel Industrial Properties
DenPen	Denel Pension Fund
DenRet	Denel Retirement Fund

Acronym	Full description
DESTO	Desto (Pty) Ltd
DIRCO	Department of International Relations and Cooperation
DISS	Denel Integrated Systems Solutions
DLS	Denel Land Systems
DMTN	Domestic Medium Term Note
DoD	Department of Defence
DPE	Department of Public Enterprises
DPS	Denel Personnel Solutions SOC Ltd
DRC	Democratic Republic of the Congo
DSA	Denel Saab Aerostructures (Pty) Ltd
DST	Department of Science and Technology
DTI	Department of Trade and Industry
Dynamics	Denel Dynamics
DAv	Denel Aviation
DTA	Denel Technical Academy
DoD&MV	Department of Defence and Military Veterans
EBIT	Earnings before interest and taxation
ECSA	Engineering Council of South Africa
ECS	Energy Conservation
EMP	Environmental management policy
EMS	Environmental management system
EOD	Explosive ordnance disposal
ERW	Explosive remnants of war
EUR	Euro (currency unit)
ERAs	Environmental risk assessments
EIA	Environmental impact assessment
EXCO	Executive committee
FIFO	First-in-first-out
FSB	Financial Services Board
GBADS	Ground-based aerial defence system
GBP	British sterling pound (currency unit)
GCEO	Group chief executive officer
GCFO	Group Chief Financial Officer
GDP	Gross domestic product
Government	South African National Government

Acronym	Full description
GRI	Global Reporting Initiative
HR	Human resources
IAS	International accounting standards
IASB	The International Accounting Standards Board
IBSA	India-Brazil-South Africa Dialogue Forum
ICAS	Independent Counselling and Advisory Services
ICV	Infantry combat vehicle
IEM	Integrated environmental management
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standards
IMS	Integrated management system
Inc.	Incorporated
IPAP2	Industrial Policy Action Plan
ISETT	Information Systems, Electronics and Telecommunications Technologies
ISO	International Standards Organization
IT	Information technology
JCEs	Jointly controlled units
JIBAR	Johannesburg Interbank Agreed Rate
kL	Kilolitre
KPI	Key performance indicator
LTIFR	Lost time injury frequency rate
LIW	Lyttelton Ingenieurswerke
LMT	LMT Holdings (Pty) Ltd
LPG	Liquate Petroleum Gas
Ltd	Limited
m	Million
MANCO	Management committee
mm	Millimetre
mL	Megalitre
MERSETA	Manufacturing, Engineering and Related Services
MwH	Mega watt hour
NATO	North Atlantic Treaty Organisation
NTIP	National Tooling Initiative Programme
MRO	Maintenance, repair and overhaul

Acronym	Full description
MSDS	Material safety data sheet
NATO	North Atlantic Treaty Organization
NCACA	National Conventional Arms Control Act
NCACC	National Conventional Arms Control Committee
NT	National Treasury
NUMSA	National Union of Metal Workers of South Africa
NGP	New Growth Path
OCI	Other Comprehensive Income
OEM	Original equipment manufacturer
OHS	Occupational health and safety
OHSAS	Occupational Health Safety Assessment Series
OTB	Overberg Toetsbaan
OTR	Overberg Test Range
PAW	Personal Area Weapon
PDPs	Personal Development Plans
PFMA	Public Finance Management Act, No. 1 of 1999
PMP	Pretoria Metal Pressings
(Pty) Ltd	(Proprietary) Limited
PR&T	Personnel, remuneration and transformation committee
PPPFA	Preferential Procurement Policy Framework Act
PAIA	Promotion of Access to Information Act
R&D	Research and Development
Rand	South African Rand
Rm	Rand million
RDM	Rheinmetall Denel Munition (Pty) Ltd
RWM	Rheinmetall Waffe Munition GmbH
SA	South Africa
SAAF	South African Air Force
SACAA	South African Civil Aviation Authority
SAD	Safe and arming devices
SAEWA	South African Equity Workers Association
SASSETA	Safety and Security SETA
SANDF	South African National Defence Force
SAPS	South African Police Service
SAWomEng	South Africa Women in Engineering
SBL	School of Business Leadership

Acronym	Full description
Scheme	EE Employment equity
SDP	Sector development plan
SED	Socioeconomic development
SEK	Swedish Krona
SETA	Sector Education and Training Authority
SET	Science, engineering and technology
SFAS	Statement of Financial Accounting Standards
SGD	Singapore Dollar
Shareholder	South African National Government as shareholder of Denel SOC Ltd
SHE	Safety, health and environment
SITA	State Information Technology Agency
SMME	Small, medium and micro enterprises
SOC	State-owned company
SOE	State-owned enterprise
STC	Secondary tax on companies
SWP	Safe working procedures
TDM	Tool, die and mould making
TETA	Transport Education Training Authority

Acronym	Full description
TISA	Trade and Investment SA
TS	Top shells
TMA	Turbomeca Africa (Pty) Ltd
UAE	United Arab Emirates
UAS	Unmanned aerial systems
UASA	United Association of South Africa
UAVS	Unmanned aerial vehicles systems
UK	United Kingdom
Unisa	University of South Africa
UN	United Nations
UP	University of Pretoria
US	United States
USA	United States of America
USD	United States Dollar (currency unit)
VAT	Value added tax
WFF	Wing-to-fuselage-fairing
YDP	Youth development programme

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Registration number 1992/001337/30

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