

Chemring Group PLC
Annual Report and Accounts 2011

Identifying growth in new markets

A world-leading defence company

Chemring is a global group that specialises in the manufacture of energetic material products and countermeasures. We provide solutions for highly demanding customer requirements in defence, security and safety markets. We are a world-leading defence company involved in advanced development programmes in the UK, USA, Europe and Australia.

With strong growth in threat detection systems, electronics now represents 40% of our revenues. Our long-term strategy is to maintain a balance between high technology electronics and energetic products.

Highlights



Continued growth at NIITEK

NIITEK increased revenue by 24% to £126.9 million, driven by high level of demand for spares and support for the 200+ HMDS systems in service with the US and Canadian Armies. In addition, 77 HMDS systems were delivered to the US Army.

For more information see page 6



Growth in non-NATO countries

Sales to non-NATO countries grew by 81% in 2011 and now represent 29% of the Group revenues. We believe that our non-NATO business will grow to 40% of Group revenues, driven by economic growth and modernisation programmes in the Middle East, Far East and South America.

For more information see page 6

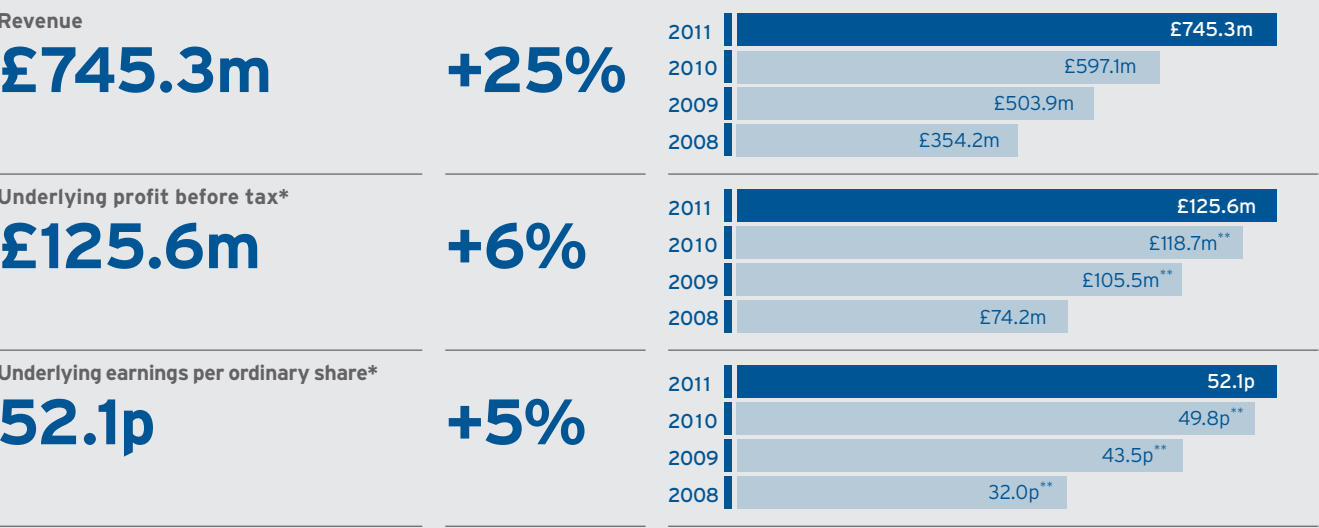


Acquisition of Chemring Detection Systems

In July 2011, the Group completed the acquisition of the Detection Systems operations of General Dynamics Armament and Technical Products. This acquisition brings a leading US capability in chemical and biological threat detection systems.

For more information see page 8

2011 Financial highlights



* Before acquisition related costs, restructuring and incident costs, provision release, intangible amortisation arising from business combinations and gain/(loss) on fair value movements on derivatives totalling £34.8 million (2010: £29.6 million)

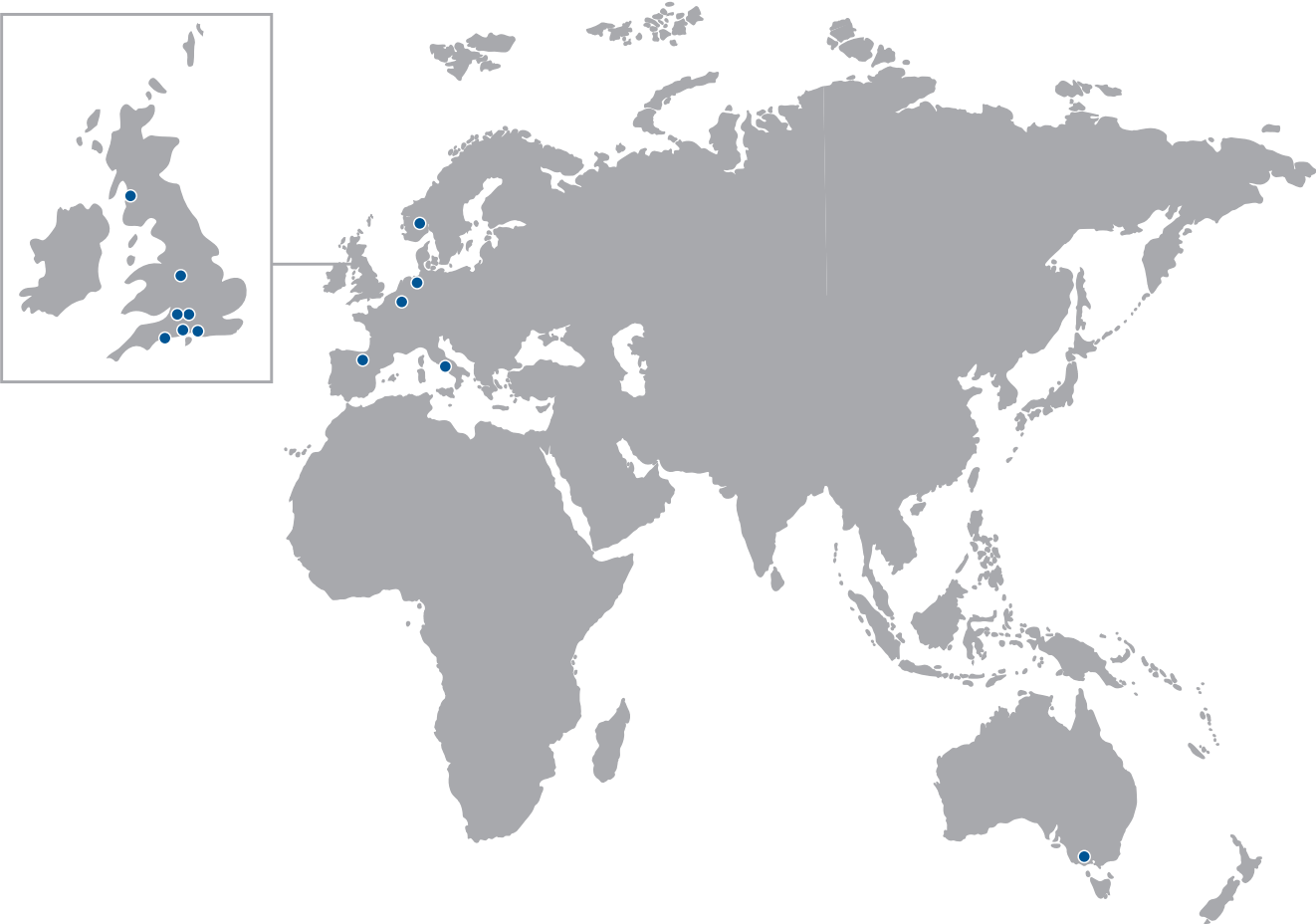
** Restated figures for prior years to reflect the subdivision of shares (see Note 13) as well as the reclassification of certain items from underlying costs to non-underlying costs (see Note 6)

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Chemring at a glance

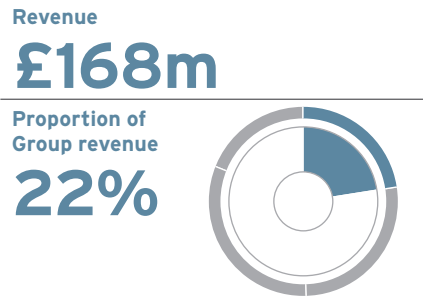
Chemring operates in four market sectors: Counter-IED, Countermeasures, Pyrotechnics and Munitions. All our products are technically demanding, requiring high reliability and integrity, and the highest level of safety in manufacture and use.



Counter-IED

Chemring is the leading supplier of vehicle-mounted ground penetrating radar (GPR) detection systems, chemical and biological detection systems, and counter-IED electronic countermeasures. We manufacture portable minefield breaching systems and a range of detonators, initiators and disruptors for demolition and explosive ordnance disposal.

- Leader in vehicle-mounted IED detection
- Leader in vehicle-mounted chemical and biological detection systems
- Supplier of disruptors, demolition stores and mine-field breaching systems to US and European forces

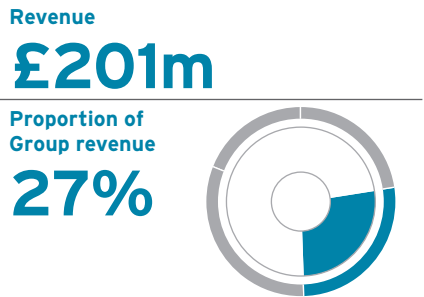


For more information see page 14

Countermeasures

Chemring is the world leader in the design, development and manufacture of advanced expendable countermeasures for protecting air, sea and land platforms. We are also a leading developer of man-portable electronic warfare equipment.

- 50% share of expendable decoy market
- Largest supplier of airborne decoy countermeasures to the US Department of Defense and the UK Ministry of Defence
- Technology leader in spectral, special material and thrusted flares for fixed-wing and rotary aircraft
- Supplier of RESOLVE man-portable electronic warfare equipment to UK and other military customers

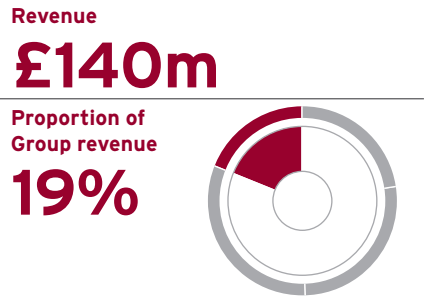


For more information see page 16

Pyrotechnics

Chemring is a leading developer and manufacturer of pyrotechnics for space, safety systems, military training, screening, signalling and illumination applications.

- Leading supplier of low shock satellite separation products and NASA standard initiators
- Largest supplier of pyromechanisms for aircraft egress systems
- Significant supplier of training products to the US Army and other NATO forces
- Growing demand for advanced pyrotechnic rounds and payloads

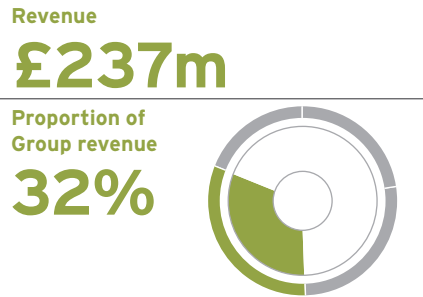


For more information see page 18

Munitions

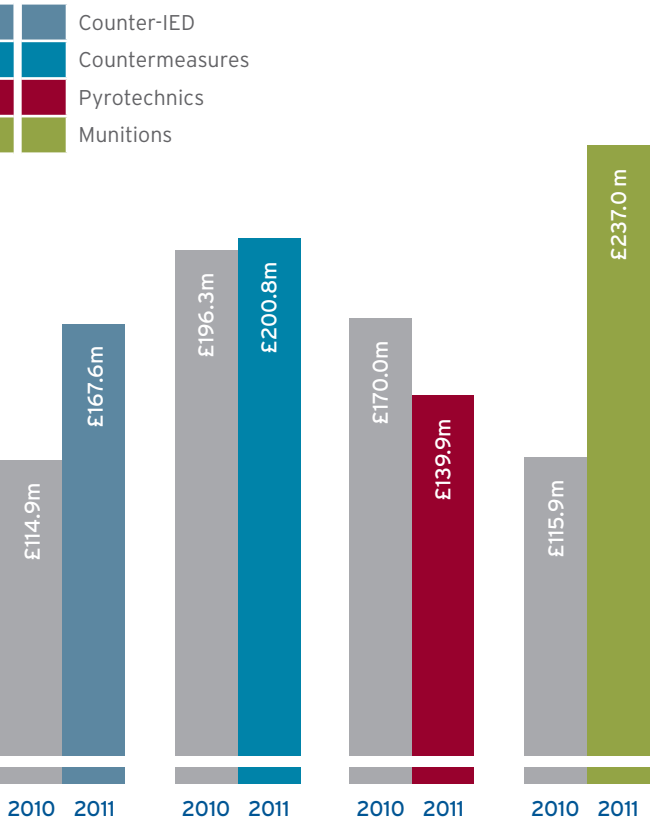
Chemring operates as a prime contractor in certain market niches and, as a component supplier, offers a unique capability in supplying energetic materials, components and subsystems.

- Market leader in naval ammunition
- Market leader in 90mm ammunition for light armoured vehicles
- Manufacturer of critical components for PAC-3 anti-ballistic missile system
- Leader in materials development for insensitive munitions



For more information see page 20

Group revenue by sector



Statement by the Chairman

The Group has pursued a strategy of combining significant organic growth from its existing businesses with a successful programme of acquisitions which have contributed further to the Group’s growth.

- Highlights
- Revenue up 25% to £745.3 million
 - Underlying operating profit* up 3% to £141.8 million
 - Underlying profit before tax* up 6% to £125.6 million
 - Underlying earnings per share* up 5% at 52.1p
 - Profit before tax £90.8 million
 - Basic earnings per share 39.8p
 - Total dividend per share for the year up 25% at 14.8p

Key information

Underlying profit before tax*

£125.6m

+6%

Underlying earnings per share*

52.1p

+5%

Dividend per ordinary share

14.8p

+25%

* Before non-underlying items (see Note 6)

Chemring produced another year of growth in profits and earnings, although both were affected in the last month by a slippage of deliveries into the current financial year. Revenue was £745.3 million, an increase of 25%, and this generated an underlying operating profit* of £141.8 million, up 3%. Underlying profit before tax* increased by 6% to £125.6 million, producing underlying earnings per share* of 52.1p, 5% above last year. The Board is recommending a final dividend of 10.8p per share which will provide a full year dividend of 14.8p, an increase of 25% over last year.

The order intake for the Group was £819.1 million, which was slightly lower than last year. We saw strong order book growth in our Counter-IED and Munitions businesses, which was offset by a downturn in orders received in the Countermeasures and Pyrotechnics divisions. These two divisions suffered from reduced customer demand, which was driven, in the main, by government fiscal and budgetary controls. The closing order book reached £878.3 million, which was 9% above last year.

In July the Group acquired the Detection Systems business of General Dynamics Armament and Technical Products for a total cash consideration of £56.1 million. The business, which is now operating as Chemring Detection Systems, Inc., is a US leader in chemical and biological threat detection and has an advanced capability in stand-off detection of improvised explosive devices. The acquisition greatly enhances the capabilities of our Counter-IED division, and has already made a good contribution to the Group’s earnings.

Balance sheet, cash flow and debt

The Group generated an underlying operating cash flow* of £124.6 million, which was 88% of underlying operating profit*. At the end of the year, net debt was £262.7 million compared with £307.5 million last year.

In April 2011, approximately £112 million of new equity was raised in order to fund

two potential acquisitions. We went ahead with the purchase of Chemring Detection Systems but did not, in the end, proceed with the other potential opportunity, as further investigation indicated that it would not generate sufficient value. In the light of this, the Board has reviewed the balance sheet to determine the appropriate levels of debt and gearing for the Group in the future. We have taken a cautious view in the light of the world’s economic and financial uncertainties and will continue reducing debt levels when appropriate. However, we have also concluded that we should consider returning surplus capital to shareholders whilst maintaining the strength of the balance sheet. Accordingly, we will seek approval at the forthcoming Annual General Meeting to renew our authority to buy back shares, when it is considered appropriate, over the course of the next year. We would only expect to exercise this authority for a buyback of up to £50 million of shares.

The Board also considered its long term dividend policy as part of this balance sheet review. For many years, the Group has adopted a policy of maintaining dividend cover at around four times. With our strong annual cash generation, we believe it would be appropriate to reduce the cover to three times over the next year. As part of this move, the proposed total dividend for 2011 will be covered 3.5 times by underlying after tax earnings*, compared with 4.2 times last year.

Group strategy

Over a number of years, the Group has pursued a strategy of combining significant organic growth from its existing businesses with a successful programme of acquisitions which have contributed further to the Group’s growth. This has enabled us to develop new products and technologies, and utilise our market positions to exploit opportunities. The acquisitions have usually been relatively modest in size, but have demonstrated a strong potential for expansion. Whilst there are none

planned at the current time, we operate in markets where consolidation may become attractive, and we will therefore continue to consider opportunities when they arise and pursue them only if there is a clear opportunity to enhance shareholder value. We see long term growth coming from our existing businesses but there will be times when acquisitions may be appropriate to supplement and enhance our portfolio.

Board of directors

During the year, there have been some changes in the composition of the Board. Two new directors were appointed during 2011. Sarah Ellard, who has been head of the Group’s legal affairs for fourteen years, joined the Board in October as Legal Director. On 1 November 2011, Vanda Murray, who has a number of non-executive appointments, was appointed to the Board as a non-executive director. I welcome them both to the Board.

David Evans, who has been a director since 1988, first as Chief Executive and for the last seven years as a non-executive director, has indicated his intention to retire from the Board at the Annual General Meeting in March. During his time with the Group, David has made a major contribution to its development, and I would like to take the opportunity to thank him on behalf of the Board and wish him well in the future.

Dividends

In line with the revised long term dividend policy outlined above, the Board is recommending a final dividend for the year of 10.8p (2010: 8.4p). With the interim dividend paid of 4p (2010: 3.4p), this gives a total dividend for 2011 of 14.8p (2010: 11.8p), an increase of 25%. The dividend is covered 3.5 times by underlying after tax earnings*, and with a solid balance sheet and cash flow, the Group remains well positioned to increase its return to shareholders.

Prospects

During the last year, many governments have struggled with increasing deficits and lower economic growth. This has affected defence procurement, leading to volume reductions and delays. The continuing problems of the Eurozone and the impact of possible sequestration in the US indicate that our traditional markets will not be any easier this year. We continue to pursue our policy of reducing our dependence on these markets, and will actively seek more business from elsewhere. It is encouraging to note that 44% of today’s order book emanates from these non-NATO markets, compared with 33% at the same time last year. We see further good growth prospects in these markets and will pursue the opportunities they offer. I am confident that we have the products, the management and technological skills to achieve our objectives and provide the foundation for steady growth.


P C F Hickson
Chairman
24 January 2012



Review by the Chief Executive

The Group delivered another year of good growth. Revenue from continuing operations grew by 25% to a record £745.3 million.

Operational highlights

- Excellent performance from NIITEK, which grew by 24% and delivered a further 77 ground penetrating radars for the Husky Mounted Detection Systems (HMDS) to the US Army
- Our Munitions business had a tremendous year, with revenue up 104% to a new record of £237.0 million and growing demand for our products from a variety of Middle East customers
- Acquisition of Chemring Detection Systems adds the US leader in chemical and biological threat detection and brings advanced capability in the stand-off detection of improvised explosive devices
- Our total expenditure on research and development grew by 74% to £59.6 million, which represents 8% of the total Group revenue

Key information

Year end order book

£878.3m
+9%

Revenue

£745.3m
+25%

Number of employees

4,679
+9%

* Before non-underlying items (see Note 6)
Organic growth at constant US dollar excludes growth from contracts and customers acquired with Roke, Mecar and Chemring Detection Systems

Group results

The Group delivered another year of good growth. This was achieved despite the disruption within the US defence market caused by the extended Continuing Resolution position that delayed approval of the US government budget until the middle of April 2011. Revenue from continuing operations grew by 25% to a record £745.3 million. Approximately one third of this growth was organic#, with strong contributions from both our Counter-IED and Munitions operations. There were excellent performances from NIITEK, which delivered a further 77 ground penetrating radars for the Husky Mounted Detection Systems (HMDS) to the US Army for counter-IED operations, and from our European ammunition prime contractors, Mecar and Simmel, which both substantially expanded their Middle East exports. The Group revenue continued to be second-half weighted, with £415.5 million of revenue (56%) generated in the second six months of the year, a little lower than the average phasing achieved over the last five years.

It was disappointing however that, as a result of unexpected last-minute delays in customer approvals of product lot acceptance, £37 million of revenue associated with finished product manufactured in September and October slipped out of the last week of October into the first few months of the current financial year. The largest element of the delay (36%) was associated with the final negotiation on the 64 system HMDS contract awarded to NIITEK in January 2011. All of the HMDS systems and spares had been manufactured and were ready for delivery but negotiations on the final contract pricing under open book requirements took many months longer than expected and were finally completed in November 2011, just after the end of the financial year. The revenue achieved in 2011 was, therefore, about 5% lower than the Board's expectations.

The order intake for the Group during the year was £819.1 million, 1% lower than the previous year, reflecting a balance between strong growth in two of our divisions and contraction in the other two.

Our Counter-IED division generated £207.4 million of order intake, up 16% on the previous year, of which £46.1 million relates to the successful capture of the contract to manufacture the MK7 MOD 2 Anti-Personnel Obstacle Breaching System (APOBS) for the US Army and Marine Corps. Our Munitions division also had an excellent year, with an increase of 42% in order intake to a new record of £349.4 million, £244.3 million of which was awarded by Middle Eastern customers. Our Countermeasures division, however, saw a contraction of 29% in its order intake to £154.9 million, mainly driven by budgetary control actions in the US, particularly at Kilgore where our backlog levels are high. Order intake in our Pyrotechnics division was also lower than expected, down 41% to £107.4 million, with UK and US customers deferring annual purchases as part of their austerity and deficit reduction programmes.

The closing order book for the Group, therefore, reached £878.3 million, an increase of 9% on the previous year, although substantially lower than it was at the time of our third quarter interim management statement on 30 August 2011. Timing of orders from our Middle East customers and the impact on US orders from another year of Continuing Resolution budget management by the US government were the principal contributors. The 9% increase does, however, still provide a solid foundation for the growth expected in 2012.

The composition of the order book changed substantially during 2011, with a significant shift to non-NATO customers. Orders from NATO customers now make up only 58% of the order book, with the Middle East reaching 27%. Order intake from UK customers has been disappointing, and our UK order book dropped 30% to only 13% of the Group total at the year end.

Our Counter-IED division had another excellent year, achieving a 46% increase in revenue to a record level of £167.6 million, reflecting strong growth in various detection and disable sub-segments of the markets. NIITEK had an outstanding year, increasing its revenue by 24% to

£126.9 million, driven by high level of demand for spares and support for the 200+ HMDS systems in service with the US and Canadian Armies on peacekeeping operations. Chemring Ordnance also had a successful breakthrough into the "defeat" part of the US counter-IED market by winning the multi-year competition for the manufacture of the APOBS for the US Army and Marine Corps. This system is designed to safely clear a footpath through anti-personnel mines and multi-strand wire obstacles. Production under the contract, which is worth up to \$150 million over the next four years, will start in the second half of 2012.

Our Munitions division also had a tremendous year, with revenue up 104% to a new record of £237.0 million and growing demand for our products from a variety of Middle East customers. Our two prime contract activities grew very strongly, with sales of our ammunition for Light Armoured Vehicles (LAVs) up 198% to £158.2 million and our naval ammunition revenues up 122% to £20.4 million. Our prime contract business now represents 75% of this division, compared to 53% in the previous year.

Our Countermeasures division delivered a steady performance, achieving a 3% increase in revenue to £200.8 million, including the full year contribution from Roke, which was acquired in 2010. The expendable countermeasures revenues, however, dropped by 17%, with a 29% reduction in demand from our principal customers for decoys used to protect helicopter and transport aircraft, in anticipation of the planned withdrawal from Afghanistan in 2014. Two upgraded naval countermeasure rounds completed their development and qualification programmes during the year and production deliveries are expected to contribute to growth from 2012 onwards.

Our Pyrotechnics division generated revenue of £139.9 million, 18% lower than last year, with a large number of annual orders placed at reduced volumes, or deferred completely, as European and US governments reduced expenditure as

part of their deficit control programmes. However, we did successfully capture the competitive, multi-year contracts for the improved submarine distress signals for both the UK and US Navy customers. These will put us in a strong position to address the global market, where the demand for diesel submarines continues to grow.

The underlying operating margin* achieved by the Group was 19%, lower than the 23% achieved last year, and took the underlying operating profit* to £141.8 million, which was 3% higher than the previous year. Half of this change in margin is attributable to recent acquisitions, which are generating lower margins than the continuing businesses. The other half came from margin deterioration in two of our divisions. The operating margin in the Counter-IED division reduced to 19%, with Chemring Detection Systems contributing four months of post-acquisition revenue at 15% margin. The largest reduction, however, was generated at NIITEK, where the very late cost auditing of the HMDS contracts disallowed any gains from risk mitigation and efficiency performance. Operating margins in our Countermeasures division reduced to 23%, with Roke contributing a full year of post-acquisition revenue at 10% margin and our expendable decoys business providing a 27% margin. This was a lower margin than last year (2010: 30%) because of lower decoy production volumes at Alloy Surfaces, in the US, and at Chemring Countermeasures, in the UK. Operating margins in the Pyrotechnics and Munitions divisions were similar to last year at 23% and 17% respectively.

Health and safety

It is with great regret and sadness that I have to report that one of our employees, who was injured during the September 2010 incident at our subsidiary Kilgore Flares in Tennessee, was taken back into hospital during 2011 and subsequently died. We have supported her and her family through very difficult times and continue to extend our support and deepest sympathies to her family and friends.

As Chief Executive, I am fully aware of our responsibility to ensure that every single

one of our employees returns safely home at the end of every working day, and we continue to invest heavily in safety-related plant and equipment improvements to reduce the exposure of our employees to danger. During the year, we spent more than £7 million specifically targeted at further improvements in safety.

With the exception of the businesses acquired in late 2010 and 2011, all Chemring sites are certified to the environmental management system ISO14001 and the health and safety management system OHSAS18001. The outstanding sites are scheduled for certification during 2012. In addition to this external validation and surveillance, we continue to use recognised consultancies to support our audit programme to test the compliance and quality of our systems.

I am pleased to report that we had no major incidents in the year.

Our lost time incident rate (calculated using the US OSHA rules) reported in the last Annual Report was 1.06 per 100 employees. When the historical data for the September 2010 acquisitions was included the rate increased to 1.67, and we worked hard during the year to drive the rate downwards and closed at 1.32. Eight of our sixteen businesses (six last year) reported no lost days in the year, which is an excellent achievement.

The Board recognises that the highest levels of safety are required to protect our employees, our customers and the general public. We believe that all injuries and incidents are preventable and we will continue to strengthen our long-term strategies to ensure that the Group improves its safety performance and reduces risk.



Review by the Chief Executive

continued

I would like to extend my personal thanks to all members of staff for their personal achievements and hard work during the year.

Acquisitions

The Group made only one acquisition during the year. In July 2011, the Group completed the acquisition of the Detection Systems operations and certain related assets of General Dynamics Armament and Technical Products, a subsidiary of General Dynamics Corporation, for a cash consideration of \$90 million (£56 million).

The business, now renamed Chemring Detection Systems, Inc. (CDS), is based in Charlotte, North Carolina. It is a US leader in chemical and biological threat detection and has advanced capability in the stand-off detection of improvised explosive devices. CDS is the incumbent supplier for two major US military vehicle-mounted detection programmes: the Joint Biological Point Detection System (JBPDS) and the Joint Service Lightweight Stand-off Chemical Agent Detector (JSLSCAD). In addition, its products include a stand-off IED and explosives detector and the Juno hand-held chemical detector.

The acquisition substantially enhances our Counter-IED business activities with leading-edge US technology for biological, chemical and stand-off explosive detection. It provides a complementary capability to our existing subsidiaries, NIITEK and Chemring EOD, and will help us expand our growing global market position.

During the summer, we were in discussions with a third party regarding a significant acquisition that would have made a major impact to our market position. However, the restructuring required to deliver the full benefit was considerable, and we felt that the vendor's valuation of the business was too high. Although we are no longer pursuing this opportunity, the core strategy of the Group remains focused on organic growth that is augmented by small bolt-on acquisitions.

Electronics

In line with the Group's strategy, electronics, including electronic countermeasures and IED detection systems, is of growing importance across our four market segments. With the acquisition of Chemring Detection Systems and Roke, we have significantly enhanced our capabilities in

electronic systems design, development and integration. In 2011, electronics contributed 40% of the Group revenue, and this is expected to grow to 50% over the next five years. These electronic capabilities are in five niche areas:

- **Initiation** - delays, sequencing and safety/arming
- **Detection** - radar and infra-red stand-off technologies
- **Electronic warfare** - interception of communications and electronic attack
- **Electronic countermeasures** - active jamming systems
- **Network protection** - legal intercept and anomaly detection

Roke has become a strategic European centre-of-excellence for product and technology development of electronic systems. It is heavily engaged in the system engineering and software development of our CENTURION countermeasure launcher; it is designing low-cost, active-jamming technology for our air and naval expendable markets; and it has completed the design of our new SPLINTER hand-held mine detector.

In 2011, Roke was given the Queens Award for Innovation for its RESOLVE modular, man-portable, electronic warfare system for the exploitation and suppression of hostile communication equipment. RESOLVE is now in service with the UK Ministry of Defence and a number of customers in the global export market. Roke has produced and demonstrated a vehicle-mounted RESOLVE capability, and there is strong interest from Europe and the Middle East in vehicle-mounted surveillance systems for dedicated electronic surveillance applications.

Research and development

Our strategy for future growth continues to rely on technology leadership and the rapid development of new products that meet the changing needs of our customers and displace those of our competitors. Our total expenditure on research and development grew by 74% to £59.6 million, which represents 8% of the total Group revenue. Internally-funded research and development grew by 56% to £21.2 million, reflecting the

strategic emphasis we continue to place on product innovation. Our long-term partnership with Cranfield University continues to expand, and we now have sixteen programmes running across areas of interest relevant to all four of our divisions.

Roke now represents our largest concentration of research and development expenditure, with around 50% of the total funding directed at electronic rather than energetic products and technology.

Capital investment

Capital investment in the year grew by 19% to £48.6 million, which represents nearly 7% of Group revenue. £19.7 million of the investment relates to the continuing build of the new countermeasures manufacturing facilities at Salisbury in the UK and at Lara in Australia. The UK facility has not yet been completed and has been delayed by technical issues with the safety critical software. These have recently been resolved, and initial production is scheduled for the end of 2012. Better progress has been made on the facility in Australia, and the first locally manufactured flares were produced in 2011. Low rate initial production is scheduled for March 2012, but it will take at least another six months to work up to full volume manufacture.

A second principal area of investment was associated with the development of our Chemring Energetics facility in Scotland, where we spent £4.7 million on the completion of four facilities: the primary explosives facility for the manufacture of detonators and initiators; the plastic explosives pressing facility for the manufacture of demolition stores; the Meccanite expansion facility for the manufacture of propellants; and the high explosive pressing facility for warhead manufacture. All of these facilities provide new manufacturing capabilities to the site and the capacity to meet the substantial growth in revenue that is expected in the future.

Staff and employees

At the end of 2011, the Group employed a total of 4,679 people, 396 (9%) higher than the previous year end, although 109 of them were associated with our latest acquisition,

Chemring Detection Systems. In addition, the year end figure included a significant number of short-term contractors engaged within our UK operations during the last quarter of the financial year. Excluding these contractors reduces the year-on-year growth to around 4%. 1,798 employees (38%) are located within the UK and 2,047 employees (44%) are located in the US.

I would like to extend my personal thanks to all members of staff for their personal achievements and hard work during the year. The Board understands how important our employees are to the success of this fast-changing business.

Future prospects

Market conditions

During 2011, the defence market faced greater uncertainty than in previous years, with the Eurozone crisis and European government deficit reduction programmes continuing to have a negative impact on defence budgets. Most of our European customers continue to delay their annual procurements by six months, and are looking for reduced volumes of consumables to save money. The UK Ministry of Defence, in particular, has substantially reduced its procurement of flares and decoys for the protection of helicopters and transport aircraft.

The UK defence market continues to be challenging, with a contracting budget, significant changes to procurement structures, and substantial reductions in personnel. The impact of last year's Strategic Defence & Security Review has gradually become clear but the structural reforms proposed by Lord Levene are only just starting to get underway. Of particular importance to the defence industry is the restructuring of the acquisition organisation, which may cause a significant disruption to the future procurement process whilst it is being implemented. A number of options for reform have been submitted to Ministers but a decision is unlikely to be announced until the middle of 2012.

However, it is the US market that has been far more challenging during the past year. No agreement was reached between the President and Congress on the size and

constitution of the FY2011 budget, and Continuing Resolution funding of the US government continued all the way through the first half of our financial year. This mechanism maintains the funding for the government employees but prohibits new programme starts or increases in funding compared to the previous year. The Pentagon was hesitant to release funds for procurement until the full year budget was known, as they were concerned about the number of programmes that would have to be adjusted. The majority of our annual contracts were delayed into the second half of the year, reducing the opportunity for early deliveries from these contracts. Revenues from our US businesses were, therefore, heavily second-half weighted and greatly increased the risk of slippage into 2012.

The US government started its 2012 financial year with further Continuing Resolutions, and there was a real threat that a twelve month Continuing Resolution might be adopted. This would have had a significant effect on the timing of annual contract placement, resulting in a stronger than usual second-half bias to our revenues, and a risk that sales would slip past October 2012. However, in late December, the US FY2012 base defence budget was approved at \$520 billion, and the Overseas Contingent Operations (OCO) budget, which funds peacekeeping operations in Afghanistan, was set at \$115 billion. The funding contains a substantial year-on-year reduction in expendable countermeasures that will affect the Group, but this appears to be offset by opportunities in counter-IED and chemical/biological threat detection, and by strong growth in important niche product areas, such as demolition stores, pyrotechnics and medium calibre ammunition.

Details of the US FY2013 budget should be announced in February 2012. US Department of Defense guidance has focused on a base budget of \$523 billion and OCO funding of \$83 billion, which is a 5% reduction on this year. However, President Obama recently announced that he was looking for \$263 billion of cuts over the next five years against the FY2011

baseline, which equates to a base budget of \$517 billion. If implemented, the US budget will reduce by 6% in FY2013 and then return to slow growth of a few per cent each year thereafter.

However, the 2011 Budget Control Act, passed in the US in August 2011, contains a "sequestration" clause that will automatically reduce US defence spending by a further \$54.7 billion per year and threatens to reduce the FY2013 base budget to \$465 billion. This will be very difficult to achieve without cancellation of important major programmes and may lead to serious cutbacks in all aspects of procurement. Although Congress has started to make plans to repeal the sequestration clause, the President has threatened to veto any attempts by Congress to block the automatic spending cuts. There is, therefore, considerable continuing uncertainty about the US market.

Non-NATO markets, on the other hand, remain buoyant with more attractive economic growth rates and lower fiscal deficits. The International Monetary Fund¹ forecasts that real Gross Domestic Product in India/Asia will grow by 7.5%, Latin America by 3.9% and in the Middle East by 3.6%. Defence spending in these regions continues to strengthen and they represent a very attractive market for the Group. Customers are looking to upgrade their products to near-NATO standards, to develop local manufacturing, and to eventually develop an indigenous design capability. The Group is finding considerable opportunities in all four of our market segments, but the specialist capabilities that we have in direct fire ammunition, in particular, are proving to be a significant attraction.

Counter-IED

Our HMDS ground penetrating radar continues to operate successfully during counter-IED operations in Afghanistan and has saved the lives of many US and coalition soldiers. During 2011, NIITEK delivered 77 HMDS systems to the US Army taking the number of systems supplied to over 240. Negotiations with the US Army for a multi-year sustainment contract, covering systems, spares and support and potentially

¹ World Economic Outlook, September 2011 published by the International Monetary Fund

Review by the Chief Executive

continued

The Board anticipates that organic growth will continue at a similar rate to that achieved in 2011.

worth in excess of \$500 million, has been underway for many months, and the contract is expected to be received by the end of the second quarter. This will support the operation of the HMDS fleet until withdrawal from Afghanistan in 2015.

Good progress has also been made in developing the export market for HMDS. Agreement has been reached with MBDA Italy to provide the Italian Army with a modified ground penetrating radar system to go on the Calife pushed trailer and the IVECO VTMM multi-role tactical vehicle. Full development will be completed in 2012 and production is expected in 2012 and 2013. The Australian Defence Force has also selected HMDS for its counter-IED operations, and is looking to procure systems through the US Foreign Military Sales channels.

The US Army's acquisition of a next-generation IED detection system, involving more advanced multi-sensor technology and data fusion, will probably take place in 2013, and they have confirmed that they expect to purchase in excess of 500 systems over a five year period.

In 2012, the US Army will take the Milestone C decision to start full rate production of the nuclear, biological and chemical reconnaissance vehicle - Stryker Suite. An additional 100 vehicles will be built in 2012 and a further 50 in 2013. This will boost demand for both the biological (JBPDS) and chemical detection systems (JSLSCAD) supplied by our new subsidiary, Chemring Detection Systems, and will generate good growth over the next few years.

The Group has also continued work on a customer-funded development programme for stand-off explosives detection. Three systems were manufactured and delivered for early user testing during 2011. Additional work is expected in 2012 to continue early user testing, to complete a production readiness phase of the current generation system, and to work on a next generation system for vehicle-mounted applications with on-the-move capability.

The qualification of our range of insensitive demolition stores is making good progress, and considerable export interest has been

generated, both within and outside NATO, by our SABREX flexible linear cutting charge. The global market for products used to "defeat" the threat remains steady at £300 million, and represents an important area for future growth. The award of the multi-year APOBS contract to Chemring Ordnance by the US Army was a strong endorsement of the investment in technology and facilities. Technology transfer of our next generation demolition stores to the US should help capture a sizable share of the global market.

The order book for our Counter-IED division was £127.1 million at the end of the year, 28% higher than the previous year. The growth has been driven by the APOBS contract. The HMDS multi-year sustainment contract has taken many months to negotiate, and the delay is reflected in the reducing order book. The delayed timing of the new contract will impact revenues at NIITEK in 2012. However, revenue from Chemring Detection Systems will offset this reduction, and overall, the Board expects good growth from this segment in 2012.

Countermeasures

In Afghanistan, the total NATO deployment is still 130,000 troops. However, coalition forces have announced their intention to withdraw their troops by 2015, starting with a reduction of nearly 40,000 by the end of 2012. In anticipation of this withdrawal and, under pressure from budget constraints, most of our customers have cut back significantly on the purchase of flares and decoys needed for the protection of helicopters and transport aircraft. A combination of reductions in the volumes ordered and delays in order placement is quickly reducing the current stock piles. Further reductions are anticipated in 2012, which will take production on some decoys down to a minimum sustainable level.

The major growth in expendable countermeasures over the next five years will, however, be associated with the supply of flares and countermeasures to protect fast jets. These are principally used in operations against sophisticated opponents, where war stocks need to be in place for high volume usage during intense battle conditions. Two aircraft, Typhoon

and the F-35 Joint Strike Fighter (JSF), will dominate the market over the next ten to fifteen year period. A technical problem with the dispenser, manufactured by a third party, has delayed volume production of the Typhoon units, and we are still in low rate initial production with the JSF flare set. With the approval of the US government, Chemring Australia has been identified as a second source supplier for JSF countermeasures and, after the US Department of Defense qualifies production in Australia, will compete with Kilgore for a share of the long-term production.

Another major area of growth over the next few years is naval countermeasures. These are designed to protect ships against incoming missiles, particularly in circumstances when rapid-fire gun systems cannot be used, such as in shallow water next to other friendly vessels. During 2011, the Group completed development of a range of new payloads to meet the changing threat and is now starting to manufacture these next generation products. The Group has also purchased, from Lockheed Martin, the manufacturing assets and intellectual property for certain legacy US naval rounds. Our new designs and the detailed knowledge of current US in-service rounds will position us strongly for a new US Navy procurement programme which will run from 2013 onwards.

The Group has also made good progress in the development of its new trainable launcher system, Centurion. A series of land-based firing demonstrations were successfully undertaken last year, and a fully operational prototype is now in manufacture. Discussions with the Royal Navy on sea trials are underway, and the Italian Navy has recently expressed strong interest in undertaking an extended sea trial of the system on one of their San Antonio Landing Platform Dock vessels. Considerable interest has been shown by a number of US, Middle East, Far East and South American customers.

The order book for our Countermeasures division decreased by 12% to £234.0 million during 2011. Although this is normally a reliable lead indicator of trends over the next twelve months, it does not take into

account the high level of backlog at Kilgore or the delays in order placement caused by the US government's Continuing Resolution funding. Strong growth in deliveries of decoys for combat aircraft programmes are, therefore, expected to compensate for the reduction in demand for those used on helicopters and transport aircraft, and a stable level of revenue can be expected for this segment.

Pyrotechnics

There continues to be strong interest in illuminating payloads for use in peacekeeping operations. We have developed a family of "white light" and "black light" payloads for the full range of mortar calibres, large calibre ammunition and for low signature, hand-held rockets that can be used by individual soldiers. These are all expected to enter into volume manufacture during 2012 and 2013.

We have also completed the initial development of a payload for the replacement of white phosphorous in smoke/screening payloads. A 120mm spotting round has completed development and will be qualified by the US Army in 2012 for sale to Middle East customers under the Foreign Military Sales programme.

The overall order book for the Pyrotechnics division reduced by 16% to £145.5 million, with large reductions in the smoke, illumination and training parts of the market. However, the Pyrotechnics order book has a much shorter coverage, and the opening order book does not adequately characterise the scale of in-for-out orders that make up the full year performance. Lower demand for training and aircraft safety products is expected in 2012 but further growth in revenues for smoke, illumination and space products means that revenues approaching 2010 levels can be expected.

Munitions

The naval ammunition market continues to grow, principally driven by the number of 76mm guns fitted to new naval ships. There is considerable interest in our products from Middle East and South American customers. A live-firing demonstration is planned in Italy to demonstrate its capability against pirate boats or fast attack craft to a number of Middle East customers.

The Middle East and South America are also growing markets for our 90mm, 105mm and 115mm ammunition. In particular, the CMI 90mm Mk8 gun is often fitted to the LAVs prevalent in these regions, and offers the Group a substantial opportunity to develop new customer relationships and markets. Discussions are also underway with the Brazilian government for the supply of 90mm ammunition for the 400 new IVECO LAVs which they are planning to acquire over the next ten years.

The Group is under contract with General Dynamics Land Systems, Canada for the supply of vehicle-based 120mm mortar systems for sale under a US Foreign Military Sales programme. System deliveries will commence in 2012 and will involve production testing by the US Army during 2012 and 2013, using Mecar supplied ammunition. New inspection requirements from the US government have delayed the expected delivery programme and the majority of deliveries are now scheduled for 2013. Annual ammunition contracts are then expected.

The order book for the Munitions division grew by 39% to £371.7 million in 2011, with strong growth in both the land and naval prime contract markets. Growth in 2012 revenues is expected to be good, albeit at a lower rate than would be implied by the increase in the opening order book.

Non-NATO growth

The Group sells to a wide variety of military customers in 80 countries around the world. Over the last four years, revenues from non-NATO customers have grown by 360% and now represent 29% of the Group revenue. Economic growth and lower fiscal deficits offer attractive markets for companies willing to quickly develop new products for their specific needs, to establish local entities, transfer the technology for local manufacture, and develop over the long term the capability to incrementally upgrade products for the future.

We believe that we are well-positioned to develop our non-NATO business to 40% of Group revenue over the next five to ten years. Our niche ammunition products have

provided the foundation for negotiations in a number of countries but interest is also high in our countermeasures, counter-IED and electronics technologies.

During 2011, we announced that we had reached agreement with the Hinduja Group to form a joint venture in India. Initially, the focus has been on a marketing joint venture, which will be pursuing a number of major opportunities during 2012. However, we expect to obtain Indian government approval for a defence manufacturing joint venture in due course, which will address the full range of the Group's products and technologies. Similar discussions with potential joint venture partners are taking place in Saudi Arabia and Brazil, and the Group expects to announce more detailed information later in the year.

Outlook

Over the next two years, the NATO market will face considerable uncertainties and revenues will be constrained by government deficit reduction actions. Non-NATO markets, on the other hand, still offer good growth prospects but the timescales for successful implementation often take some time. Over the short term, therefore, the Board anticipates that organic growth will continue at a similar rate to that achieved in 2011.

In the medium term, there are good opportunities in all four of our business segments. The Group focuses on short term developments of products that match important and constantly changing customer needs. This agility and its wide breadth of technology allows the Group to target a number of well-funded, specialist niches and growth in market share at the expense of weaker competitors.


D J Price
Chief Executive
24 January 2012

Our strategy

Our strategy is to develop and build on our core competencies in energetic materials and electronics for sensors, electronic warfare and network protection.

Vision

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

Counter-IED

Establish technology leadership

- Become the world leader in IED, chemical and biological threat detection
- Maintain technological lead in ground penetrating radar and counter-IED jamming
- Become world leader in IED neutralisation and demolition stores

Countermeasures

Maintain market share

- Exploit lead in special material, spectral and thrusted flares
- Develop a market lead in naval launchers and decoys
- Become the world leader in dismounted and vehicle electronic warfare equipment
- Establish niche position in network protection

Pyrotechnics

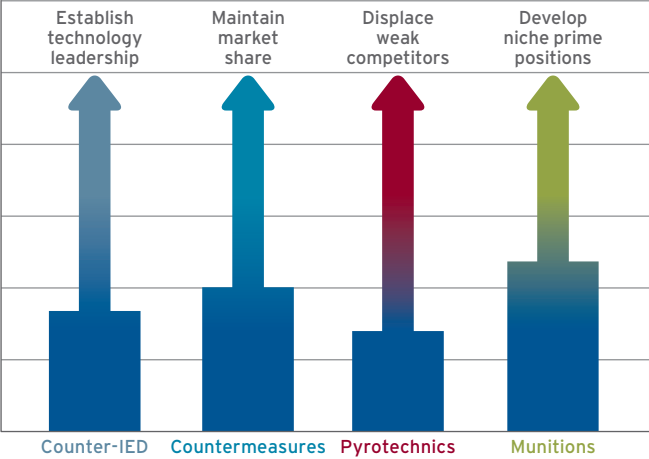
Displace weak competitors

- Establish undisputed world lead
- Develop new products to transform user operations

Munitions

Develop niche prime position

- Become a leading prime contractor for non-NATO
- Become a supplier of choice for NATO primes



Group strategy
The Group strategy is focused on our four market segments - Counter-IED, Countermeasures, Pyrotechnics and Munitions. With the growing importance of electronics throughout our business, our future vision statement includes a broader definition of "protection systems", including electronic countermeasures and IED detection systems.

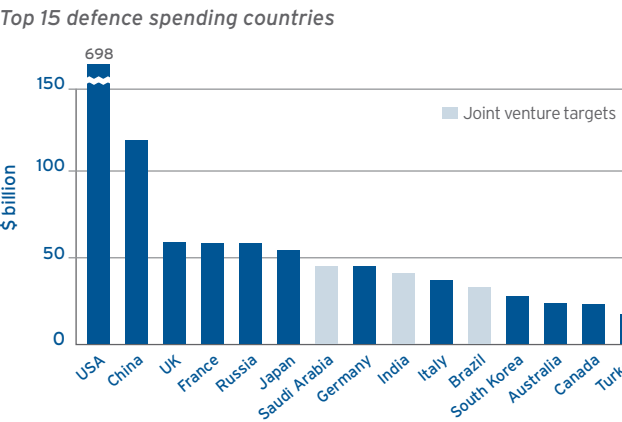
Our core strategy over the next five years is to develop and build on our key core competencies:

- Energetic materials** - We will focus on products where we can exploit our extensive knowledge and expertise in explosive, pyrotechnic and pyrophoric materials. We will address niche, highly profitable markets with significant value-added manufacture/assembly where barriers to entry are high. We will exploit the commonality of technology and design expertise to generate a broad centre-of-expertise that can be maintained over the long-term future.
- Electronics for sensors, electronic warfare and network protection** - A growing proportion of our business will be based on high integrity, high-speed electronics for detecting and analysing threats as well as enabling a timely response. Many of these electronic systems will be network-based.

Organic strategy
Our organic growth strategy is based on two elements:

- Geographic expansion outside NATO**
- New product development**

Our geographic strategy is to establish a strong local manufacturing presence in the world's leading defence spending countries and to export vigorously around the world. We have businesses in the US and Europe's top five spending countries (UK, Germany, France, Italy and Spain), and export to over 80 countries around the world. As the emphasis of global defence spending migrates from NATO to the Middle East, Far East and South America, we will develop our presence in these regions. We are in the process of establishing joint ventures in India, Saudi Arabia and Brazil.



Secondly, we will maintain a strong focus on developing world-leading products. As a growing proportion of our business is based on advanced electronics, we have developed parallel energetics and electronics technology strategies.

Our energetics technology strategy is focused on materials technology and applications engineering in five key areas:

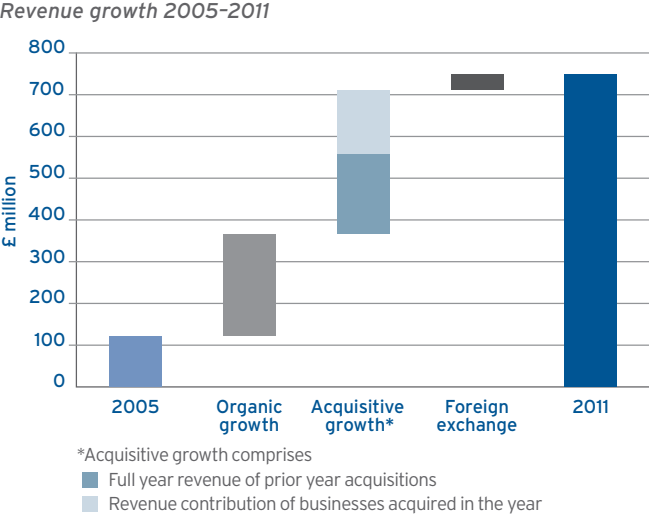
- Explosive materials** - We will develop and optimise material formulations to improve their performance and safety.
- Warheads** - We will build a lead in missile warheads and will offer insensitive munitions (IM) variants of our ammunition products.
- Propellants** - We will develop a new generation of low vulnerability ammunition (LOVA) propellants and will build a capability in composite rocket motors.
- Pyrotechnic countermeasures and illumination** - We will maintain our world lead in air countermeasures and will develop a full range of spectrally-optimised pyrotechnic payloads.
- Pyrotechnic obscurants** - We will lead development of safer, multi-spectral smokes and less-lethal technologies.

Our electronics technology strategy builds on our leadership in key niches:

- Initiation** - Is the interface to energetic products, and we will extend the application of electronics to improve the performance of our munitions and pyrotechnic products.
- Detection** - We will maintain our lead in stand-off threat detection technologies and will enhance these with sensor fusion and advanced algorithm development.
- Electronic warfare (EW)** - We will extend our lead in man-portable electronic intelligence equipment, and will develop vehicle-mounted variants of our products.
- Electronic countermeasures** - We will establish a world lead in active off-board decoys, and will develop a step-change in portable counter-IED jammers.
- Network protection** - We will apply our leading capability in fast electronic hardware to lawful intercept applications and the protection of wirelessly networked military systems.

We will maintain an underpinning technology base to enable a cycle of rapid product development and technology insertion through internal research and partnerships with universities, research institutions and technology companies. Where we cannot quickly develop critical capabilities and technologies organically, we will supplement this with targeted acquisitions.

Acquisition strategy
Acquisitions have been an important element of the recent growth of the business. The successful completion of eighteen acquisitions over the last six years has broadened our capabilities, diversified our segmental and geographic activities, and has directly contributed to the overall growth of the Group.

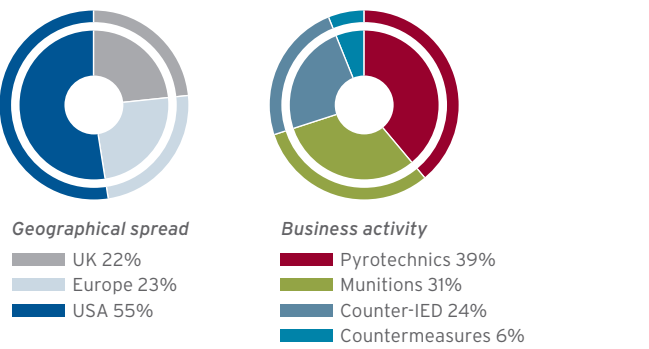


Our strategy for acquisitions is to continue to target opportunities which add capability, technology and market access. We will exploit synergies from such acquisitions by creating centres-of-excellence, investing in new products and selling our products through our worldwide channels to market.

We intend to maintain a balance of acquisition investment across all our segments, markets and technologies.

Our acquisition investments over the last six years can be analysed as follows:

Total investment on acquisitions 2005-2011 c.£480 million



Counter-IED

The closing order book for Counter-IED was £127 million, up 28% on 2010, and a clear indicator of continued revenue growth in 2012.

Highlights in 2011

- Revenue 46% higher than 2010
- NIITEK delivered 77 complete HMDS and range of spares, increasing its revenue by 24%
- Acquisition of Chemring Detection Systems provides world-leading capability in chemical and biological detection
- Chemring Ordnance won US production contract for Anti-Personnel Obstacle Breaching System (APOBS), worth up to \$150 million
- Closing order book for Counter-IED was £127 million, up 28% on 2010

Key information

Orders

£207m

Revenue

£168m

Operating profit

£32m

Operating margin

19%

Strategy

Our strategy is to become the world leader in the global counter-IED (improvised explosive device) market with high technology products to detect, disable and defeat the threat posed by IEDs, as well as chemical and biological agents. We will invest in advanced sensor technology for the detection of explosive, biological, chemical and nuclear threats, as well as the data fusion necessary to deliver high reliability detection performance. We will also develop portable wide-band adaptive jamming capabilities to disable remotely controlled devices, and will develop and qualify advanced technology disruptors and the full range of safer demolition stores to defeat them.

Analysis

The global market for counter-IED equipment is estimated to be £3 billion. Our revenue in 2011 was £168 million, 46% higher than the previous year, which equates to a market share of 6%. The Group's strongest focus is on detection systems, and revenue from this part of the business increased by 51% to £149 million, representing a 25% market share of this key high technology area. Our success has been driven by the demand from the US Army for highly effective ground penetrating radar (GPR). In July, the acquisition of Chemring Detection Systems was completed and, in the last four months of the financial year, the business contributed £15 million of revenue.

The closing order book for Counter-IED was £127 million, up 28% on 2010, and a clear indicator of continued revenue growth in 2012.

Activities during the year

Detect

The detection of IEDs continued to dominate the activities of our Counter-IED division during the year, with continued growth at NIITEK in support of the Husky Mounted Detection System (HMDS) ground penetrating radars currently deployed in Afghanistan. During 2011, NIITEK delivered 77 complete radar systems, over 2,700 radar panels, and a wide variety of spares

for operational maintenance in-theatre, generating an increase in revenue of 24% compared with the previous year.

In the middle of the year, a system upgrade was introduced to all new HMDS radar systems. This upgrade provided greater sensitivity and a higher ground clearance mount to minimise panel damage during transit. A remote-controlled version of the Husky system was also deployed to Afghanistan and is currently undergoing operational evaluation.

NIITEK also won a contract from the US Army for a Talon-based GPR system with an embedded metal detector coil. The system has successfully completed US trials and safety testing. It is expected to start operational evaluation during 2012 and production should commence shortly thereafter.

Roke has been funded by the UK Ministry of Defence to develop a family of new hand-held detector systems, called SPLINTER. An early prototype system was deployed to Afghanistan during the year and the results achieved were described as "very encouraging". A fully functional product has recently been completed and a rapid qualification programme is expected in 2012.

The acquisition of Chemring Detection Systems provides the Group with a world-leading capability in chemical and biological detection, as it is the incumbent supplier for two major US military vehicle-mounted detection programmes: the Joint Biological Point Detection System (JBPDS) and the Joint Service Lightweight Stand-off Chemical Agent Detector (JSLSCAD). Chemring Detection Systems continued its customer-funded development programme during the year and moved on to Phase 3 of the Biological Detection System Upgrade Program. These updates will be implemented into new production systems, as well as retrofitted into existing field units.

Chemring Detection Systems also launched a commercially available variant of the JSLSCAD. This product provides ground platforms, fixed sites and shipboard installations with state-of-the-art remote



Chemical/biological detection

JUNO hand held detector in use

chemical agent detection capabilities. A recent test demonstrated its ability to detect stimulants out to a full 5km range. A first export contract has been received from a Far East country, and strong interest has been expressed by a number of Middle East customers.

Chemring Detection Systems also continued work in 2011 on a customer-funded development for the Lightguard stand-off explosives detector. Three systems were fabricated and delivered for early user testing. Additional work is expected in 2012 to continue user testing, to complete a production readiness phase of the current generation system, and to work on a next generation system for vehicle-mounted applications with on-the-move capability.

Defeat

In June 2011, our US subsidiary Chemring Ordnance won a highly competitive contract to produce the MK7 MOD 2 Anti-Personnel Obstacle Breaching System (APOBS) for the US Army and Marine Corps. The contract is for three years and is worth up to \$150 million. The APOBS is a self-contained, one-shot, expendable linear demolition charge, which can be transported and deployed by a two person team. The system is capable of safely clearing a footpath through anti-personnel mines and multi-strand wire obstacles. This contract award expands our position in the US demolition stores market. A new production facility, to assemble the product, is now nearing completion.

This year has seen the successful development and qualification of a new generation of Bangalore Torpedo under contract from the UK Ministry of Defence. Although the concept of the Bangalore Torpedo is over 100 years old, our development has produced a substantial improvement in performance whilst ensuring that it meets the criteria for an insensitive munition.

The development of the SABREX flexible linear cutting charge has continued throughout the year with final design, to meet the underwater performance requirements, being achieved in the summer. A commercial qualification

programme, to meet the needs of our export and commercial customers, has commenced, and UK qualification will follow in summer 2012. A number of export customers have already placed orders and there continues to be strong interest in the product from all parts of the global market.

Our business units and companies

Chemring Energetics UK Ltd

Specialises in the design and manufacture of energetic materials, detonators, and demolition stores.

Chemring EOD Ltd (UK)

Manufactures a range of products for detection, assessment and neutralisation of threats from improvised explosive devices and unexploded ordnance.

Chemring Ordnance, Inc. (USA)

Supplies Anti-Personnel Obstacle Breaching System (APOBS), a rocket-deployed mine clearance system, to the US Army.

Chemring Detection Systems, Inc. (USA)

Leading US developer and supplier of vehicle-mounted chemical and biological detection systems for the US Army.

Non-Intrusive Inspection Technology, Inc. (USA)

The leading manufacturer of vehicle-mounted ground penetrating radar mine detection systems.

Roke Manor Research Ltd (UK)

A world-class developer of electronic countermeasures and threat detection technologies.

Our products

Detect

- Vehicle-mounted IED detection systems
- Chemical and biological detection systems
- Stand-off IED detectors
- Remote IED inspection equipment
- Under-vehicle surveillance systems

Disable

- Electronic countermeasures

Defeat

- Remote initiators
- Detonators
- Explosive charges
- Minefield breaching systems
- Recoilless de-armers/disruptors

Countermeasures

Kilgore Flares, one of our US subsidiaries, had an excellent year, with revenue up 5% to a new record.

Highlights in 2011

- Revenues from fast jet decoys increased by 7% to £97 million
- Chemring Countermeasures supported peacekeeping operations over Libya, delivering enhanced capability to protect UK combat aircraft
- Two key naval decoy upgrade programmes completed
- Roke completed deliveries of the RESOLVE man-portable electronic warfare system to the UK Army

Key information

Orders

£155m

Revenue

£201m

Operating profit

£47m

Operating margin

23%

Strategy

The core strategy for our Countermeasures division is to maintain our share of the expendable countermeasures market and to expand the business in line with the market, which is expected to grow over the next five to ten years. We will continue to invest in new products and technologies that build on our current leadership in special materials, spectral and thrust flare technologies. We will also invest significantly in both decoy and launcher technologies for the naval market, which we expect to grow rapidly in the future. A new generation of active off-board decoys will be developed, building on our world-leading position in expendable countermeasures and our capabilities in advanced, miniaturised radio frequency (RF) electronics. We will build on our strong position in man-portable electronic warfare equipment to establish ourselves as a world leader in dismounted and vehicle-mounted systems. We will also establish a niche position in network protection, based on our capabilities in fast electronic hardware and Network Enabled Capability.

Analysis

The market for expendable countermeasures is estimated to be £360 million. In 2011, our revenue was £201 million, up 3% on the previous year, but this included a full year of revenue from Roke which was acquired in 2010. Excluding Roke, organic revenue fell 18%, reflecting reduced demand for flares for the protection of helicopter and transport aircraft, as customers reduce stockpiles in anticipation of withdrawal from Afghanistan. This reduction was larger than expected as both US and UK governments have continued to delay order placement because of the tight budgetary constraints. Sales at our US subsidiary, Alloy Surfaces, and at our UK subsidiary, Chemring Countermeasures, were most affected. On the other hand, sales of decoys used on fast jets increased by 7% to £97 million, despite the fact that there was no production of the MJU-7 flares used to protect the F-15 and F-16 fighters. Revenue from naval countermeasures was lower than 2010, due to the extended time taken to complete development of two key naval round upgrade programmes, which prevented volume production in the year.

Our land-based electronic warfare business grew substantially, reflecting the full year contribution of Roke and the success of its RESOLVE product in the UK and export markets.

The closing order book for the Countermeasures division was £234 million, down 12% on the previous year. This reflected lower orders for helicopter and transport applications, and slower growth in demand for fast jet flares, as Typhoon war stock procurement for European and Middle East customers was delayed by dispenser issues.

Activities during the year

During the year, Chemring Countermeasures provided strong support for the UK peacekeeping operation over Libya, rapidly delivering enhanced capability to protect both Typhoon and Tornado fast jets. These products were made available to operational aircraft within days of issue of the requirement, ensuring that platforms sent to Libya were protected from a variety of potential surface-to-air missile threats. Overall, production volumes remained stable at around 450,000 decoys.

Kilgore Flares, one of our US subsidiaries, had an excellent year, with revenue up 5% to a new record on steady production volumes of around 1 million flares. This was principally driven by a four-fold growth in the production volumes of flares used to protect the B-52 aircraft. Following final qualification of the Joint Strike Fighter (JSF) flare set, Kilgore will continue with low rate production over the next two years while the overall aircraft programme is completed. Although currently a sole source provider, Kilgore has entered into a manufacturing license agreement which will facilitate the transfer of production of a JSF flare to Chemring Australia in the coming years. BAE Systems, Lockheed Martin, the US Navy Program Office, and the JSF Program Office are all part of a joint effort to establish this important industrial participation program for Australia.

Following the September 2010 incident at Kilgore, we are rebuilding the final assembly building that was damaged in the incident. The building will have numerous safety



Dispensing flares
F-22 aircraft deploys flares

and productivity improvements, including increased automation, and is on schedule for commissioning by the end of the first half of this financial year. Production of the MJU-7 flare, used to protect the F-15 and F-16 aircraft, will then recommence.

Our other US subsidiary, Alloy Surfaces, had a more difficult year, with a substantial reduction in revenue from lower production volumes of 1.3 million decoys, 32% down on last year. This was principally driven by the 50% reduction in volumes of MJU-50 decoys that are mainly used by the US Air Force on transport aircraft. This reduction in volumes had an adverse impact on our operating margin, and resulted in the closure of one of Alloy Surfaces' three production sites in Philadelphia and a reduction of over one hundred staff.

Alloy Surfaces has, however, made progress with its development of two next generation decoys for the protection of helicopters. The business has received a contract to deliver 1,500 developmental units of one decoy for US Air Force effectiveness testing in early 2012, with a production order expected later in the year. The other decoy is designed for the protection of small signature rotary aircraft. Flight tests have shown excellent performance, and further effectiveness testing is expected to begin in the second quarter.

Alloy Surfaces has also been developing a new pre-emptive, long duration, infra-red countermeasure with exceptional performance. It will expand countermeasure protection capabilities for both the F-16 and F-18 aircraft. Initial US Navy tests were completed in September 2011 and further flight tests are scheduled for early 2012.

Chemring Australia's new manufacturing facility is currently being commissioned. The first flare has been manufactured and volume production is scheduled to be underway by summer 2012. Further upgrades to support the JSF programme will be implemented over the next few years.

The acquisition of Roke in September 2010 significantly enhanced the Group's electronics capabilities for the design of the next generation active-RF expendable countermeasures, for the design and

integration of the Centurion trainable launcher, and for a range of electronic warfare systems for land forces. Deliveries to the UK Army of our RESOLVE electronic warfare system, designed to be carried by an individual soldier, were completed during the year. Operational feedback has been extremely positive and export interest has grown substantially, particularly from Middle East customers. Roke has also demonstrated a vehicle-mounted system, which is attracting strong export interest.

In 2011, Roke developed Battlefield Connect, the world's first wide area military 3G base station. Capable of 40km range and high bandwidths, Battlefield Connect is interoperable with existing military command infrastructure systems and can support defence applications including streaming video to unmanned air vehicles, imagery and biometric information exchange, and simultaneous voice and data communications. This year, Roke has partnered with a major international defence communications supplier to bring the full product to market.

Roke is also part of the industry consortium that has been awarded a contract to deliver the UK Ministry of Defence's Intelligence, Surveillance, Target Acquisition and Reconnaissance (ISTAR) Information Integration and Management (I3M) programme, which sits at the heart of the capacity of the armed forces to effectively use the information gleaned from their many platforms and sensors.

Roke has successfully deployed a number of next generation Aquila Deep Packet Inspection probes into our existing customer base with positive feedback to date. Aquila's patented search technology has the highest density data processing capability on the market, with less than half the footprint of comparable platforms. Network protection is a fast growing market for Roke, providing key expertise and research and development technology to a number of long term UK government programmes.

Our business units and companies

Alloy Surfaces Company, Inc. (USA)

The world's only manufacturer of special material decoys for the US Department of Defense and militaries worldwide. Alloy's patented technology employs pyrophoric materials to decoy attacking enemy missiles.

Chemring Australia Pty Ltd

Australia's only on-shore manufacturer of aircraft expendable countermeasures.

Chemring Countermeasures Ltd (UK)

A world leader in the design, development and manufacture of advanced expendable countermeasures for air and sea platforms, and is also developing next generation launchers for deploying naval decoys.

Kilgore Flares Company LLC (USA)

Develops and produces airborne expendable IR countermeasure decoys and naval decoys.

Roke Manor Research Ltd (UK)

A world-class developer of electronic countermeasures, electronic intelligence and network protection technologies.

Our products

Air countermeasures

- Conventional and advanced flares
- Special material decoys
- Chaff

Naval countermeasures

- RF decoys
- IR decoys
- Naval decoy launchers

Land/EW

- Electronic intelligence equipment
- Electronic countermeasures
- Lawful intercept equipment

Pyrotechnics

In September, Chemring Ordnance won two new marine pyrotechnic production contracts, worth up to \$31 million, from the US Navy.

Highlights in 2011

- US Army declared the M992 “black light” illumination round produced by Chemring Ordnance as one of its top ten inventions
- Chemring Energetics UK selected to deliver components associated with the emergency oxygen deployment system for the Boeing 787
- Chemring Energetic Devices completed initial deliveries of its Joint Combined Aircraft Systems Testers (JCAST), for testing life-support systems for F-16 and F-22 aircraft

Key information

Orders
£107m

Revenue
£140m

Operating profit
£32m

Operating margin
23%

Strategy

Our strategy is to become the world leader in pyrotechnics, through focused investment in new products that displace existing incumbents and which better meet our customers’ requirements and transform their operational capabilities. We intend to expand our activities in the space sector by developing improved products for initiation, stage separation, and satellite and sub-system deployment for military and commercial customers. This will address the US, European and emerging international markets. We intend to expand our safety systems activities, both in military and civil aircraft.

Analysis

The global market for pyrotechnics is currently estimated to be £1.6 billion. Our revenue in 2010 was £140 million, which is 18% lower than the previous year and represents a reduction in global market share to 9%. The majority of this decline was driven by reduced sales of smoke and illumination products, which were 25% lower than the previous year. Sales of training and simulation products were down 5%, reflecting reduced European sales which were partially offset by increased deliveries of US training grenades.

The closing order book was £145 million, down 16% on the previous year due to delayed order placement from many of our customers. However, demand is recovering in this sector and revenues are expected to recover to pre-2011 levels.

Activities during the year

Smoke and illumination

The Group continues to focus on the development of advance “blacklight” and visible illumination payloads for a wide variety of ordnance rounds and missiles. During the year, volume production was started on 105mm ammunition payloads and this has generated considerable interest with the US Army. A number of air-launched products are also under development and should enter production in the next few years.

Production of US 40mm pyrotechnic rounds slowed in 2011, when the US Army

took six months to hold the competition for the 40mm prime contract covering the next five years. This extended period forced re-qualification of all production lines, and the Army decided to give priority to its non-pyrotechnic requirements. Production is restarting in 2012 with good volumes for M662 Red Star and M992 Blacklight rounds. In September, the US Army declared the M992 was one of its top ten award-winning inventions.

Mecar has completed the initial development of a 120mm mortar spotting round, which is used to improve long-range firing accuracy as well as operator and forward observer training. This new product uses a proprietary composition that replaces the conventional white phosphorus payload. In 2012, Mecar will also develop an infra-red and visible light screening round for towed and turreted 120mm mortar systems.

In September, Chemring Ordnance won two new marine pyrotechnic production contracts, worth up to \$31 million, from the US Navy. The first was for Mk 140 series day/night signals that are launched from submarines to signal surface vessels or aircraft. The second was for the MK124 day/night pyrotechnic marking signal, a hand-held device utilised by the US Navy and US Air Force aircrew in air and sea rescue and recovery operations. These new contracts establish Chemring as one of the largest suppliers of submarine location markers.

Training

In 2010, Chemring Ordnance upgraded the M228 training grenade to incorporate the confidence clip fitted to live grenades used by the US Army to prevent accidental removal of the firing pin. During 2011, the automated production line was increased to 20 units per minute and over two million units were made. The company also passed several pre-qualification tests for a next generation pyrotechnic simulator, which provides a safe and realistic visible effect to orientate air and ground personnel to the launch of a MANPADS surface-to-air missile. The MANPADS simulator will be utilised to train personnel involved in rotary wing close air support and UAV operations.

Safety systems

Chemring Energetics UK has been selected by BE Aerospace to deliver components associated with the emergency oxygen deployment system for the Boeing 787. The initial components have been delivered as part of the qualification programme for the system, and we have signed a long-term agreement with BE Aerospace to deliver these components over an extended period. We are also supporting proposals for an emergency oxygen delivery system on the Airbus 350.

In early September, Chemring Energetic Devices completed initial deliveries of its Joint Combined Aircraft Systems Testers (JCAST), which are used to test oxygen systems, helmets, noise reduction headsets and chemical defence systems on F-16 and F-22 aircraft. These testers were used by the US Air Force to assess the quality of the oxygen systems that grounded the F-22 fleet during 2011. Each of the F-22 squadrons now has an onsite test capability. We are also under contract to provide additional systems to the US Air Force Air Combat Command for its F-16 units in 2012, and have started working with the Air Force on defining the modifications necessary to service the multi-national F-35 Joint Strike Fighter programme.

Space

Our commercial launch and satellite segment continues to grow, and defence customers are combining their requirements with the commercial side to realise cost savings. The constant need for weather, navigation and increased communications bandwidth will have a positive impact on this marketplace. The market is becoming more global with both Europe and Asia increasing their rate of launches, and in order to exploit this change, Hi-Shear and Chemring Energetics UK have entered into an agreement to expand Chemring’s space presence in Europe. We are solidifying our relationship with both ANA and Mitsubishi in Japan, and we have begun to explore relationships in India.

Our business units and companies

Chemring Australia Pty Ltd
Supplies a range of pyrotechnics, military training and marine safety products.

Chemring Defence (Europe)
Centre-of-excellence for the design, development and production of smoke and illumination pyrotechnics and payloads for military, OEM and safety customers.

Chemring Energetics UK Ltd
A leading supplier of rocket motors, canopy cutting cords and pyromechanisms for safety and aircrew egress.

Chemring Energetic Devices, Inc. (USA)
Supplier of pyrotechnic and electromechanical systems for space, safety and military training applications.

Chemring Marine Ltd (UK)
The world’s leading supplier of marine distress signals to commercial and leisure markets, under the brand names Pains Wessex and Comet.

Chemring Ordnance, Inc. (USA)
Leading US manufacturer of military training pyrotechnics and pyrotechnic rounds for 40mm grenade launchers.

Hi-Shear Technology Corporation (USA)
Leading supplier of space qualified initiators and low shock satellite separation systems, and a range of pyromechanisms for aircrew egress.

Troop concealment
Training with smoke grenades

Munitions

The closing order book for the Munitions division was £372 million, an increase of 39% on the previous year.

Highlights in 2011

- Revenue up 104% on 2010
- Large calibre ammunition sales grew strongly with revenues up 198%
- New microwave fuze, jointly developed with Oto Melara, recently completed NATO qualification
- Continued growth in demand for 40mm grenades, with a 200% increase in production
- Closing order book for Munitions was £372 million, an increase of 39% on 2010

Key information

Orders

£349m

Revenue

£237m

Operating profit

£41m

Operating margin

17%

Strategy

Our principal strategy is to develop our position as a niche prime contractor of specialist ammunition products for European and non-NATO markets. We will build on our world-leading position in naval ammunition, our growing strength in the supply of ammunition for light armoured vehicles (LAVs), and our broad range of mortar and 40mm grenade products. We will focus on new product development and investment in facilities that will allow us to expand our presence in a growing international market. We intend to build our position as a key strategic supplier of energetic material components and sub-systems to the key prime contractors for ammunition and missiles in Europe and the US. This will be achieved by developing and qualifying components for next generation weapon systems, displacing poorly performing incumbents on legacy products, investment in automated manufacturing facilities, and by further complementary acquisitions where there is a clear opportunity to enhance shareholder value.

Analysis

The global market for ammunition, excluding small calibre, is estimated to be £4 billion. Our total revenue in 2011 was £237 million, a 104% increase on the previous year and equating to a market share of 6%. Our highest growth comes from the sale of ammunition for LAVs, which increased by 198% to £158 million of revenue. Naval ammunition sales increased by 122% to £20 million, as deliveries of 76mm ammunition started to ramp upwards. The global market for munitions components is estimated to be £2 billion. In 2011, our revenue from components was £58 million, representing 24% of our total Munitions revenue, an increase of 8% compared with the previous year and equating to a market share of 3%.

The closing order book for the Munitions division was £372 million, an increase of 39% on the previous year, and a clear indication of further growth in 2012. About 71% of the order book is from non-NATO customers.

Activities during the year

Naval

76mm naval ammunition continued to be in demand during the year, with production volumes up 83% to 13,000 rounds. There has been strong interest from many of our naval customers in Europe, the Middle East, the Far East and South America. A new microwave fuze, jointly developed with Oto Melara, has recently completed NATO qualification and a live-firing demonstration for a number of Middle East customers is scheduled to take place shortly in Italy.

Land

Our sales of large calibre ammunition grew strongly during the year with revenues up 198% for Middle East and Far East customers. Demand for advanced 90mm and 105mm ammunition for LAVs has continued to increase with more and more non-NATO countries upgrading their fleets to make them more effective. Demand for 81mm and 120mm mortar products also increased and we recently signed our first contract with an important Middle East Navy customer.

Demand for our range of 40mm grenades has also continued to grow, with a 200% increase in production volumes for Australian and Middle East customers. Our US subsidiary, Chemring Ordnance, continues to develop, qualify, and field advanced products for the US market and this year we qualified a family of extended range, low velocity rounds and the next generation door-breaching round used by special forces for forced entry operations.

Components and sub-systems

Demand for our high performance, high reliability components and sub-systems continues to grow with increased sales to both US and European prime contractors. During the year, there was a substantial increase in the deliveries of warheads to MBDA for use on their Sea Viper air defence missile, that protects the UK's Daring class destroyers. There was also strong growth in sales of fuzing and safety/arming systems that initiate warheads and rocket motors with over 20,000 ordnance fuzes delivered to Far East customers.



105mm tank ammunition
105mm MGS Stryker BCT vehicle

The Group also manufactures critical components of fuzing systems used in a large number of US missiles and ammunition rounds. A new 25mm airburst round, called the XM-25, was qualified during the year and then evaluated in the field by US Special Forces. Highly automated manufacturing systems will be set up during 2012 to handle the start of full rate production in 2014.

Our business units and companies

Chemring Energetics UK Ltd

A leading supplier of detonators, actuators, rocket motors, high explosive filling and pyromechanical sub-assemblies.

Chemring Energetic Devices, Inc. (USA)

Manufactures a range of materials, components and sub-systems for leading missile and ammunition prime contractors.

Chemring Military Products, Inc. (USA)

Provides load, assemble, pack and procurement services to the US government and prime contractors.

Chemring Nobel AS (Norway)

Manufactures niche energetic materials with insensitive munitions (IM) characteristics for munition and oil-field applications.

Chemring Ordnance, Inc. (USA)

Niche supplier of 40mm grenade ammunition.

Hi-Shear Technology Corporation (USA)

Develops advanced sub-systems for ballistic missile defence and tactical weapons.

Mecar S.A. (Belgium)

A niche supplier of medium and large calibre ammunition for light armoured vehicles.

Simmel Difesa S.p.A. (Italy)

A leading supplier of naval ammunition, advanced fuzing technology and missile components.

Our products

Naval ammunition

- Medium and large calibre ammunition

Land forces ammunition

- Medium and large calibre ammunition
- 40mm grenades
- Mortar ammunition

Components

- Propellants and rocket motors
- Fuze and safe/arm units
- Pyromechanisms and actuators
- Energetic materials

Review by the Finance Director

Underlying profit before tax* was up 6% to £125.6 million, and underlying profit after tax* was up 10% to £96.8 million.

Financial highlights

- Revenue up 25% to £745.3 million
- Underlying profit before tax* up 6% to £125.6 million
- Net finance expense down 14% to £16.3 million
- Underlying operating cash flow of £124.6 million, representing an 88% conversion from underlying operating profit*
- £150.1 million of undrawn borrowing facilities at the year end

Key information

Underlying operating profit*

£141.8m

+3%

Research and development expenditure

£59.6m

+74%

Divisional operating margin

20%

* Before non-underlying items (see Note 6)
 * The 2010 figures have been restated to reflect the reclassification of certain items from underlying costs to non-underlying costs (see Note 6)
 ~ Organic growth at constant US dollar excludes growth from contracts and customers acquired with Roke, Mecar and Chemring Detection Systems

Results

An analysis of the underlying results is set out below:

	2011 £m	2010 £m
Total revenue	745.3	597.1
Divisional operating profit	151.8	147.9
Unallocated corporate costs	(10.0)	(10.4)
Underlying operating profit	141.8	137.5
Share of post-tax results of associate	0.1	0.1
Finance income	0.1	0.5
Finance expense	(16.4)	(19.4)
Underlying profit before tax	125.6	118.7
Tax on underlying profit before tax	(28.8)	(30.7)
Underlying profit after tax	96.8	88.0

Total revenue was £745.3 million (2010: £597.1 million), an increase of 25%. Revenue arising from the acquisition of Chemring Detection Systems in 2011 was £14.6 million, 2% of the increase. Organic revenue growth~ was 9%. Roke and Mecar, which were acquired in September 2010, contributed 17% of the Group revenue increase. During the year, the US dollar depreciated against sterling, which reduced the reported sterling revenues of US subsidiaries by £15.1 million, equivalent to 3%.

An analysis of revenue and divisional operating profit* by segment is set out below:

Division	Revenue £m	Underlying operating profit* £m	2011 Underlying operating margin	Revenue £m	Underlying operating profit** £m	2010 Underlying operating margin
Counter-IED	167.6	31.9	19%	114.9	28.1	25%
Countermeasures	200.8	46.7	23%	196.3	58.8	30%
Pyrotechnics	139.9	32.4	23%	170.0	40.1	24%
Munitions	237.0	40.8	17%	115.9	20.9	18%
Divisional results	745.3	151.8	20%	597.1	147.9	25%

Counter-IED revenue increased 46% to £167.6 million, due to increased revenue at NIITEK for HMDS spares and support, together with a £14.6 million contribution from Chemring Detection Systems. Operating margins reduced to 19%, largely due to pricing pressure on NIITEK's products. Chemring Detection Systems' 15% margin also diluted the overall margin for this segment.

Countermeasures revenue grew by 3% but underlying operating profit* reduced 21%, largely due to lower demand for decoys at Alloy Surfaces, which was only partially offset by revenue from Roke at a lower margin of 10%.

Pyrotechnics revenue decreased 18% to £139.9 million and underlying operating profit* decreased 19% to £32.4 million, principally due to lower demand for 81mm illumination products.



Analysis of non-underlying items

The Board monitors underlying operating profit and underlying profit before tax for reporting purposes so as to not distort year-on-year comparisons, hence certain items are classed as non-underlying as set out below:

	2011 £m	2010* £m
Acquisition related costs	5.7	6.7
Restructuring and incident costs	7.2	4.3
Provision release	-	(2.4)
(Gain)/loss on fair value movements on derivatives	(2.4)	4.0
Intangible amortisation arising from business combinations	24.3	17.0
Total non-underlying items	34.8	29.6

Acquisition related costs include the external costs incurred in acquiring businesses in 2010 and 2011, together with costs associated with an aborted bid and the establishment of joint ventures.

In 2011, the restructuring and incident costs related to the closure of Plant 3 at Alloy Surfaces (£1.1 million) and the start-up of production at Mecar following the incident that occurred in September 2010 (£2.3 million). At the end of October 2011, the Board decided to exit some loss-making munitions product lines in the US, and in addition to minor losses, a provision has also been made for excess inventory and fixed assets (£3.8 million).

In 2010, the restructuring and incident costs included the restructuring of the Group's UK Counter-IED business at a cost of £1.5 million. As a result, one of the two sites out of which it operated was closed. Also, there were two separate incidents that stopped production at the Kilgore Flares facility in Tennessee and Mecar in Belgium. As a result of these incidents, £2.8 million of non-recurring costs were incurred in respect of the write-off of damaged stock and destroyed assets.

During 2010, part of the provision held in respect of the environmental liabilities associated with the Chemring Energetic Devices site in Illinois was released, following a third party assessment of the provision. This resulted in a £2.4 million non-recurring credit to the Income Statement.

A gain on derivatives of £2.4 million arose this year, due largely to the movement in the sterling/dollar exchange rate during the year.

Intangible amortisation arising from business combinations increased in the year, with a full year amortisation of assets acquired with the Mecar and Roke acquisitions, and four months' amortisation arising from the acquisition of Chemring Detection Systems.

Munitions grew the most, with revenue increasing 104% to £237.0 million following a strong second half performance from Mecar. Mecar's margin grew to 10% in the second half from a negative margin at the half year.

Unallocated corporate costs were £10.0 million, slightly down on 2010. In 2010, two non-recurring cost items, which netted out at £1.9 million (£4.3 million charge, £2.4 million credit) were included in unallocated corporate costs but with the reformatting of the Income Statement this year these items have now been reclassified as non-underlying items in order to be consistent year-on-year. The impact of this reclassification is an increase in underlying operating profit* for 2010 to £137.5 million from £135.6 million, although divisional operating profits are unchanged.

Total underlying operating profit* was £141.8 million (2010: £137.5 million), an increase of 3%. Underlying operating profit* generated by Chemring Detection Systems was £2.2 million. Roke and Mecar contributed £9.0 million. The impact of the depreciation of the US dollar against sterling reduced the US subsidiaries' reported sterling profits in 2011 by £3.6 million. Without this depreciation, growth in total underlying operating profit* in 2011 would have been 6%.

Total underlying operation margin* reduced to 19% from 23% last year. Approximately half this reduction is attributable to lower margins at Alloy Surfaces and NIITEK, with the other half reflecting the impact of acquired businesses with lower margins than the Group average.

Finance income in the year was £0.1 million (2010: £0.5 million). Finance expense for the year was £16.4 million (2010: £19.4 million), a decrease of 15%. Included within finance expense is £0.7 million (2010: £1.2 million) for retirement benefit obligations. Net finance expense was covered 8.7 times (2010: 7.3 times) by underlying operating profits.

Underlying profit before tax* was £125.6 million (2010: £118.7 million*), an increase of 6%.

Tax on underlying profit before tax* was £28.8 million (2010: £30.7 million), representing an underlying rate of 23% (2010: 26%). The reduction in the tax rate arises from the utilisation of research and development tax credits across the Group, particularly at Roke, together with the partial utilisation of tax losses within our European businesses which had not previously been recognised.

Underlying profit after tax* was £96.8 million (2010: £88.0 million*), an increase of 10%.

Review by the Finance Director

continued

Research and development expenditure totalled £59.6 million, 74% higher than last year, reflecting the Group's investment in future growth.

Shareholder returns

Underlying basic earnings per ordinary share* was 52.1p (2010: 49.8p*), an increase of 5%. Basic earnings per share were 39.8p (2010: 37.8p), an increase of 5%.

The total dividend per ordinary share of 14.8p (2010: 11.8p) is covered 3.5 times (2010: 4.2 times) by the underlying earnings per share*.

The Group's underlying return on capital employed was 19% (2010: 22%).

Shareholders' funds at the year end were £475.4 million (2010: £323.2 million), an increase of 47%.

Pensions

The deficit on the Group's defined benefit schemes before associated tax credits, as defined by IAS 19 *Accounting for pension costs*, was £25.2 million (2010: £23.0 million).

The Chemring Group Staff Pension Scheme is a defined benefit scheme, with the assets held in a separate trustee-administered fund. A full actuarial valuation for the Staff Pension Scheme as at 6 April 2009 has been prepared and updated to 31 October 2011 by a qualified actuary, using the projected unit credit method.

The Group has given a bank guarantee and letters of credit totalling £27.2 million (2010: £7.2 million) to the Staff Pension Scheme. The guarantee and letters of credit may be drawn upon in certain events of default by the Company. The increase in this contingent funding during the year resulted in the release of the £15.0 million of previously restricted cash pledged to the Staff Pension Scheme, with £5.0 million of the increase being provided in line with the agreed funding plan.

The Group is currently consulting with active members of the Staff Pension Scheme on the proposed closure of the scheme to future accrual.

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

Research and development

Research and development expenditure totalled £59.6 million (2010: £34.2 million), 74% higher than last year. The increase reflects the Group's investment in future growth, and includes the significant full year impact of Roke's customer-funded research and development. An analysis of expenditure is set out below:

	2011 £m	2010 £m
Customer-funded research and development	38.4	20.6
Internally-funded research and development	21.2	13.6
Total research and development expenditure	59.6	34.2

£12.4 million (2010: £7.8 million) of the internally-funded research and development costs were capitalised in the year.

The Group's policy is to write-off capitalised development costs over a three year period. Amortisation of development costs was £2.4 million (2010: £2.1 million).

Cash flow

Underlying operating cash flow* was £124.6 million (2010: £128.0 million*), which represents a conversion rate of underlying operating profit* to operating cash of 88% (2010: 93%).

Fixed asset expenditure across the Group was £61.7 million (2010: £48.7 million), which includes £19.7 million related to the construction of new facilities at our sites in Salisbury and Australia, and £4.5 million relating to new facilities in Scotland.

Tax payments were lower than last year due to the availability of research and development tax credits and lower tax rates, combined with the timing of payments.

Interest was higher due to the timing of interest payments relating to some of the US loan notes.

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

	2011 £m	2010 £m
Underlying operating cash flow	124.6	128.0
Fixed asset expenditure	(61.7)	(48.7)
Tax	(17.2)	(30.0)
Interest	(17.8)	(14.0)
Underlying free cash flow	27.9	35.3

Working capital

A summary of working capital balances is set out below:

	2011 £m	2010 £m	Variance £m
Inventories	146.8	141.3	5.5
Trade receivables	164.1	139.1	25.0
Trade payables	(105.3)	(100.1)	(5.2)
Advance payments	(48.7)	(52.8)	4.1
Total working capital	156.9	127.5	29.4
Total working capital days	77	78	

Overall working capital increased by 23% on 2010, slightly lower than the increase in revenue. Total working capital days were consistent with last year at 77 days (2010: 78 days). Trade receivables were 18% higher than 2010, although lower than the rate of revenue growth. At the end of 2010, trade payables were high as a result of payables acquired with Mecar. During the first half of 2011, these trade payables were settled. It is anticipated that working capital will reduce in 2012.

Acquisitions

On 1 July 2011, the Group completed the acquisition of the Detection Systems operations and certain related assets of General Dynamics Armament and Technical Products, a subsidiary of General Dynamics Corporation, for a cash consideration of \$90 million (£56.1 million). The business, which has been renamed Chemring Detection Systems Inc., is based in Charlotte, North Carolina, and is a US leader in chemical and biological threat detection. It also has advanced capability in the stand-off detection of improvised explosive devices.

A summary of the business acquired, together with the provisional fair value adjustments made on acquisition is set out below:

	Book value £m	Provisional fair value adjustments £m	Fair value £m
Intangible assets	4.8	30.3	35.1
Property, plant and equipment	4.2	(0.7)	3.5
Overdraft assumed	(1.9)	-	(1.9)
Working capital	8.0	(2.1)	5.9
Net assets acquired	15.1	27.5	42.6
Goodwill			13.5
Total			56.1
Total cash consideration			56.1

During the year, the provisional fair value adjustments made to the 2010 acquisitions were finalised. As a result, the net assets of the acquired companies increased by £5.4 million, with a commensurate reduction in goodwill. As required by accounting standards, the 2010 balance sheet has been restated. Full details can be found in Note 33 of the financial statements.

Share split

At the Annual General Meeting on 24 March 2011, the shareholders approved the subdivision of the Company's ordinary shares of 5p each into ordinary shares of 1p each.

Equity issue

On 20 April 2011, the Group placed 17,405,183 new ordinary shares at 645p per share, raising approximately £112 million before costs. The placing represented in the region of 9.8% of the Group's market capitalisation, and it was anticipated that the capital raised would be used to fund two acquisitions. Approximately £56 million of the placing proceeds was used to fund the acquisition of Chemring Detection Systems but the Board did not pursue the second acquisition and the funds remain within the Group's balance sheet.

Net debt, facilities and going concern

Net debt at the year end was £262.7 million (2010: £307.5 million), a decrease of 15%. The Group had £150.1 million (2010: £104.6 million) of undrawn borrowing facilities at the year end.

On 14 January 2011, the Group completed a refinancing of its bank facilities with a syndicate of five banks. The new Group facilities, which are unsecured, total £230 million, a £55 million increase on the previous secured facilities. The term of the facilities is now through to April 2015.

Gearing at the year end was 55% (2010: 95%). A summary of debt is set out below:

	2011 £m	2010 £m
Cash	91.9	58.4
Loans and finance leases	(94.4)	(104.7)
Loan notes	(260.2)	(261.2)
	(262.7)	(307.5)

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



P A Rayner
Finance Director
24 January 2012

Key performance indicators

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

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

Orders received and order book

	Orders received		Order book	
	2011 £m	2010 £m	2011 £m	2010 £m
Counter-IED	207.4	178.5	127.1	99.3
Countermeasures	155.0	219.2	234.0	265.4
Pyrotechnics	107.4	181.4	145.5	171.9
Munitions	349.3	245.2	371.7	266.7
Total	819.1	824.3	878.3	803.3

The closing order book at the year end of £878.3 million represents a 9% increase on the previous year end. This reflects an increase in demand for the Group’s products during the year, and provides a solid base for the growth expected in the current financial year. Since most of the Group’s contracts are annual contracts with delivery periods from six to twelve months following receipt of order, the order book represents a good leading indicator of the revenues that will be traded in the following twelve months.

Divisional operating profit**

	2011 £m	2010 £m
Counter-IED	31.9	28.1
Countermeasures	46.7	58.8
Pyrotechnics	32.4	40.1
Munitions	40.8	20.9
Total	151.8	147.9

** Operating profits of the divisions are stated before charges for unallocated corporate costs and non-underlying items (see Note 5)

The divisional operating profit provides a consistent year-on-year measure of the trading performance of the divisions within the Group. It does not include significant non-recurring or exceptional costs that would distort a comparative assessment nor does it include unallocated corporate costs associated with operating a public company. The divisional operating profit increased by 3% during the year.

Return on sales

	2011 %	2010 %
Counter-IED	19	25
Countermeasures	23	30
Pyrotechnics	23	24
Munitions	17	18
Total	20	25

The return on sales percentage is a vital measure that provides an assessment of the profitability of the business and allows a comparison to be made of management performance and trading effectiveness independent of revenue size. Such a measure provides a clear indicator of whether revenue growth has occurred at the expense of profit or whether market conditions, such as competitive pressures, have made an impact. The divisions have largely maintained their return on sales at core businesses consistent with last year. However, the Counter-IED division was impacted by lower margins at NIITEK, where the very late cost auditing of the HMDS contracts disallowed any gains from risk mitigation and efficiency performance, and the Countermeasures and Munitions divisions were affected by the full year impact of the 2010 acquisitions of Roke and Mecar respectively, which both have lower margins.

Underlying earnings per share*

	2011	2010 As restated ^a
Total	52.1p	49.8p
Growth rate	5%	15%

Underlying earnings per share is a key measure for the Group and forms the basis for executive incentive plans. Growth in earnings per share is considered the key measure in assessing the increase in shareholder value.

Interest cover

	2011	2010
Total	8.7 times	7.3 times

Interest cover provides a clear and simple metric of the ratio between the operating profit generated by trading, compared with the funding requirement to maintain the current debt. It is an important indicator for the Group and forms the basis of one of our specified banking covenants, which requires us to maintain at all times interest cover of at least 4 times. Net finance expense was covered 8.7 times by underlying operating profit* at the year end. The Board aims to keep interest cover at a prudent level.

Underlying operating cash flow

	2011 £m	2010 £m As restated ^a
Total cash flow	124.6	128.0
Conversion from operating profit	88%	93%

Operating cash flow provides a simple measure of the cash generated by trading within the businesses. It represents the money available to fund capital expenditure, interest payments, tax and shareholder dividends. In our short cycle business, operating cash conversion closely follows operating profit and the Group usually targets a rate above 90%. The Group operating cash flow decreased by 3% to £124.6 million during the year. This represents a conversion rate of underlying operating profit* to operating cash of 88% (2010: 93%).

* Before non-underlying items (see Note 6)
^a The 2010 figures have been restated to reflect the reclassification of certain items from underlying to non-underlying (see Note 6)

Principal risks and uncertainties

As described on page 51 and 52, the Board is responsible for the Group’s systems of internal control and its risk management systems. The Board has constituted a Risk Management Committee, which meets quarterly, to review the key risks associated with the achievement of the annual budget and the five year plan for each business; the top five health and safety risks identified at each site; and the risk control procedures implemented. The Committee reports biannually to the Audit Committee and the Board and, through this process, the Board has identified the following principal risks currently facing the Group. The mitigating actions taken by the Group management to address these risks are also set out below. The Group mitigates its risk exposure through an insurance programme that covers property and liability risks, where it is appropriate and cost effective to do so.

Risk	Mitigation actions
Health and safety risks The nature of those Group operations which utilise energetic materials is such that the Board considers health and safety to be a key area of focus in managing risk.	Health and safety is included on the agenda at every Board meeting and is discussed at the monthly Group Executive Committee meeting. The Board believes that responsibility for the delivery of world class safety standards is an integral part of operational management accountability, and managers are therefore expected to embrace a positive safety culture and to demonstrate leadership and commitment in the workplace. All employees are encouraged to report potential hazards, and to raise any health and safety concerns through the appropriate channels. Our stated aim is to achieve zero injuries and to reduce health and safety risks, where they cannot be eliminated altogether, to a level which is “as low as reasonably practicable”. All businesses are expected to proactively manage their own risks but in addition, the top five site risks at each business and their associated mitigation programmes are reviewed on a monthly basis by the Group Executive Committee and quarterly by the Risk Management Committee. Technology and automation roadmaps support the Group’s strategy for risk reduction through increased automation and remote operations, and this strategy is reflected in the Group’s five year plan. Further details on the Group’s approach to health and safety are set out in the Corporate Responsibility Review.
Possible defence budget cuts We recognise that with large budget deficits and the prevailing economic conditions, there will be continued downward pressure on many countries’ budgets and consequently defence expenditure could be severely impacted. In particular, the Group has significant exposure to the US defence market, where there is currently considerable uncertainty in relation to the defence budget for 2013.	In recognition of the issues affecting our traditional NATO markets, we are focusing our growth strategy on non-NATO markets, where defence expenditure is forecast to grow strongly over the next five to ten years. We are making good progress on the establishment of a joint venture in India, and we are also in discussions with potential joint venture partners in Saudi Arabia and Brazil. We also continually assess whether our planned organic growth strategies and product developments align with government priorities for future funding. Most of our product development programmes take between six and twelve months to complete, and we believe that this gives the Board the agility to quickly re-deploy engineering staff to product areas where funding is more secure. We continue to closely monitor the position in all the key markets in which we operate.
Timing of orders The Group has a strong order book. In general, the majority of the Group’s contracts are of a relatively short duration and, with the exception of framework contracts with key customers, do not usually cover multi-year requirements. This means that an unmitigated delay in the receipt of key orders could affect the Group’s earnings, and achievement of its growth targets, in any given financial year. We have already experienced delays in the placement of orders by our traditional NATO customers, due to budgetary constraints, and this is likely to continue in the short to medium term.	As referred to above, we are focusing on expanding our business in non-NATO markets, where defence expenditure is forecast to increase, and the composition of our current order book reflects a higher level of orders from non-NATO customers. Maximising order intake remains a key objective for our businesses, and we continue to address this through the strengthening of our sales and marketing resources, both within individual businesses and at a divisional level. The development of world class manufacturing facilities, with the ability to transfer manufacturing across sites and with an efficient enterprise resource planning system, also provides us with the flexibility to change our manufacturing schedules, if anticipated orders are delayed and need to be replaced at short notice, and to satisfy our customers’ surge requirements. We continue to pursue long term, multi-year contracts with our major customers wherever possible.

Principal risks and uncertainties

continued

Risk	Mitigation actions
Political risks It is recognised that political unrest and changes in the political structure in certain non-NATO countries to which we currently sell could impact on their future defence expenditure strategy and our ability to export products to these countries, thereby reducing our opportunities for growth. It is also recognised that the nature of the current military operations around the world may change over the next three to five years.	Our businesses strive to maintain relationships at all levels within the political structure of certain key countries, in order to ensure that we are aware of and can counter proposed changes if and when they occur. We do not believe that the Group's Countermeasures business will be significantly impacted by a change in current military operations, as our products will still be required to provide defensive protection during continuing peacekeeping activities. Growth in the Countermeasures division will be delivered as our proprietary products are fitted to a range of new platforms in Europe and the US. The Group's Counter-IED, Pyrotechnics and Munitions businesses are less dependent on active military operations, particularly as our electronics activities expand and our product portfolio continues to grow in areas such as IED-detection, space, safety systems, training, munitions components and naval ammunition.
Introduction of new manufacturing facilities We are currently investing significant capital expenditure in the establishment of new manufacturing facilities in the UK, the US, Italy and Australia. We need to ensure that these facilities are completed within budget and on time, in order to maximise our manufacturing capacity for our future growth expectations.	Progress on all of the significant capital investment projects is being closely monitored by the Group Executive Committee and the Board. A Senior Project Director has been appointed to oversee the design and construction activities for the new countermeasures facilities in the UK and Australia, and dedicated project managers have been appointed to oversee the other major programmes in the US and continental Europe. The new countermeasures facilities have taken slightly longer to complete than originally expected, principally due to the significant challenges associated with the new automated processes which are being installed, but both the UK and Australian facilities should now be commissioned during 2012.
Introduction of new products The Group's approach to innovation and continued emphasis on research and development activity ensure that we are continually adding new products to the range. We need to ensure that this new product development is completed in a timely manner to a standard which allows us to undertake volume manufacturing, and to produce products against high reliability and safety criteria to meet our customers' requirements.	We continue to strengthen our engineering resources to ensure that we have the right people in place to deliver the product development activities in support of our five year plan. In the UK, we have a five year research partnership with Cranfield University, looking at new technologies and products for future development. We also have smaller partnerships with a number of US universities, including the Georgia Technology & Research Institute, University of Massachusetts, Penn. State University, Duke University, University of Florida, University of Louisville, Missouri University, South Dakota School of Mines, and the New Jersey Institute of Technology. We continue to build new manufacturing facilities to accommodate the production of new products, and to increase capacity on our existing production lines. This necessitates careful management of contractors - where construction work is being undertaken; suppliers - where new components have to be qualified for use in our products; and employees - where training in new skills is required. We continue to introduce Six Sigma techniques as appropriate within the organisation to improve our manufacturing capabilities. This investment in new facilities will continue over the course of our five year plan.

Risk	Mitigation actions
Competitive risks Defence is a global industry, which is constantly challenged to counter ever-changing threats. The Group's strategy is to focus on targeted niche markets in energetic materials and protective systems, where the nature of the products and the requisite production and qualification processes provide significant barriers to new entrants. However, as threats evolve, new businesses offering new solutions may enter the market.	The nature of the threat from missiles and other weapons is continually changing, particularly as new platforms are introduced in different countries, and countermeasure solutions need to develop on an ongoing basis to meet the enhanced requirements. The number of countermeasures manufacturers is currently small, however, as technologies change, existing manufacturers are able to compete for new products and new businesses can also enter into the market. The Group is currently the world leader in the supply and manufacture of expendable countermeasures, with a number of proprietary products. We intend to maintain this position through our continued investment in research and development, and world class manufacturing facilities. The competitive threats to our Pyrotechnics and Munitions businesses are generally lower, as the markets are fragmented and our competitors are generally companies with national market positions and limited product ranges. Our Counter-IED businesses need to continually develop next generation systems in order to address emerging threats, and this provides an opportunity for new competitors to emerge. However, the detection systems produced by NIITEK in particular are extensively used in-theatre, and this provides a good platform from which to capture the future market. Our core strategy is to grow our business by taking market share and we are, therefore, strongly focused on our research and development activities to ensure we have next generation products available at the right time. We also invest substantial funds to enhance our manufacturing capabilities, in order to maintain our leading position in our niche technologies and markets.
Management resource The Group requires competent management if it is to achieve its growth expectations, successfully integrate its acquired businesses and meet its order capture targets. The Board has identified, in particular, that the Group needs to strengthen its sales and marketing resources, in order to maximise order intake as explained above, and its engineering resources, in order to undertake the product development activities needed to support the Group's five year plan.	The Group Executive Committee reviews the strengths and weaknesses of the management team at each business twice a year, and the Board undertakes an annual review of future requirements and succession planning as part of the strategic planning process. We continue to strengthen the management organisation across the Group, and a number of additional senior appointments have been made during the year. We undertake a specific detailed review of our future sales and marketing and engineering resource requirements each year, and we are actively recruiting in each of these areas. During the year, we also undertook a review of the future requirements for our finance and IT functions, and we have implemented a new long term IT strategy that will respond to the future expansion of the Group.
Compliance and corruption risks The Group operates in over eighty countries worldwide, and is subject to the laws and regulations of each of these countries. The Group must ensure that all of its businesses, its employees and third parties acting on its behalf comply with their legal obligations, and do not expose the Group to financial penalties or reputational damage.	The Group has a central legal and compliance function which assists and monitors all Group businesses, assisted by dedicated internal legal resource in the US. The Group's internal audit activities also incorporate a review of legal risks. The Group has a Global Code of Business Principles, which stipulates the standard of acceptable business conduct required from all of our employees and third parties acting on our behalf. The Group has also adopted a Bribery Act Compliance Manual, incorporating all of our anti-bribery policies and procedures. A significant proportion of the Group's management have received training in relation to ethics and anti-corruption.
Financial risks Details of the financial risks to which the Group is potentially exposed are set out in Note 25 of the financial statements.	

Corporate Responsibility Review

Our approach

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

The Board has overall responsibility for establishing and maintaining the Group's policies in this area, and the Chief Executive is accountable to the Board for ensuring that the Group's businesses adhere to these policies.

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

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

We intend that our corporate responsibility approach should be fully embedded within our businesses, and our senior management bonus plan incorporates specific objectives in the above areas.

Further details of our approach are set out below.

In the workplace

Health and safety

Our policy and practices

The Board recognises that the highest levels of safety are required in order to protect our employees, product end users and the general public, whilst achieving growth and maintaining leadership in the Group's chosen markets. The Board believes that all incidents and injuries are preventable, and that all employees have the right to return home safely at the end of every working day. The long term strategies we have adopted are designed to ensure that we continually improve our performance and reduce risk.

The Chief Executive has overall responsibility for health, safety and environmental matters across the Group. The Group Director of Safety reports directly to the Chief Executive, and is responsible for the effective administration and implementation of the Group's health, safety and environment strategy. The Group Director of Safety is a member of the Group Executive Committee and reports on the performance of all businesses against agreed targets and objectives. The Chief Executive reports monthly to the Board on all key health and safety issues.

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

We recognise that a key element in the continual improvement of health and safety management is sharing best practice and lessons learnt from incidents across all of the Group's companies. An alert system is in place that formally ensures key findings from incidents are quickly communicated to all operational sites and actions taken as appropriate. All accidents, incidents and near misses are investigated, with actions generated to prevent recurrence. A Health, Safety and Environment Technical Group, with representatives from across all our businesses, supports continual improvement through the development and promotion of good health and safety practice.

Compliance audits are conducted at all Group facilities using external consultancy firms. All findings are subject to corrective action reviews to ensure closure, and added to a findings database which is shared across the Group.

The Group's policy is to have all of our businesses certified to the international health and safety management system OHSAS18001, with all newly acquired businesses certified within two years of acquisition. We are fully compliant with this objective.

Safety is a major item for consideration by the Group's Risk Management Committee. All businesses are required to produce a risk register, from which the top five health and safety risks and improvement actions to reduce the risks to as low as reasonably practicable are reviewed on a monthly basis.

The Group has committed to substantial investments in manufacturing facilities that will, in addition to improving productivity, improve the safety of the workforce by reducing the levels of risk. We apply particular attention to those facilities that compare unfavourably with their peers, and systems and processes are in place to facilitate the sharing of information across the Group. Our ongoing safety improvement activities are focused on ensuring that our buildings, processes and products are as safe as reasonably practicable for our employees and product users.

Our performance

Energetic events causing injury

Whilst we take all incidents seriously, we pay particular attention to those where employees sustain injury due to an energetic event.

In September 2010, a fire at our Kilgore facility in Toone, Tennessee resulted in three employees sustaining serious injury. Sadly, one of the employees passed away in September 2011. Since the incident, we have worked hard at Kilgore, and other related sites, to ensure that all lessons learnt are fully implemented.

During the year under review, we had one incident involving an energetic event that resulted in lost time. At our Chemring Ordnance facility in Perry, Florida, an operator was hurt when a trip flare ignited inside her booth, causing a flash which burned the operator's hand and fingers. She returned to work after seven days.

Energetic events not causing injury

We had no energetic events during the year that caused significant damage to buildings or equipment.

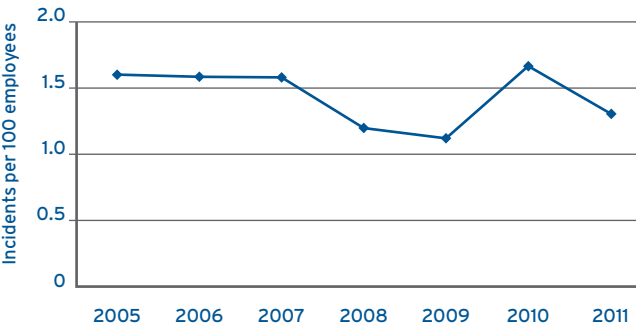
Other lost time events

We collect and report lost time incident rates using the US Occupational Safety and Health Administration (OSHA) rules. Last year we reported a lost time incident rate of 1.06 incidents per 100 employees. When the statistics for the businesses acquired in 2010 were included, this rate increased to 1.67.

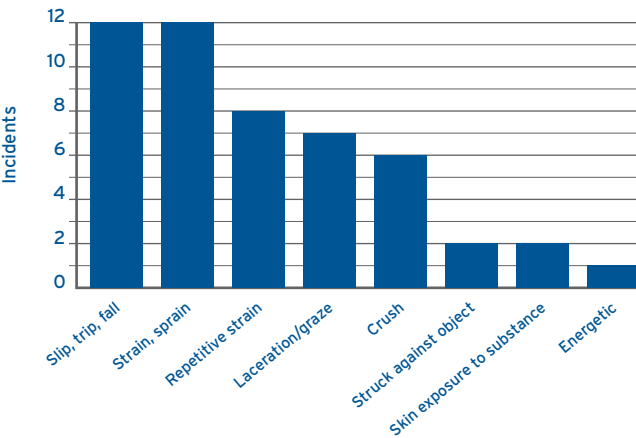
After considerable time and attention (and excluding the newly acquired Chemring Detection Systems business), the Group's lost time incident rate improved by 20% from 1.67 to 1.32 incidents per 100 employees during the year. With the inclusion of the Chemring Detection Systems business, the rate reduces to 1.28. Eight of our sites (six last year) reported no lost work days in the year, which is an excellent achievement.

Our historical lost time incident rate performance is shown below:

Lost time incident rate performance



A total of fifty lost time incidents were recorded in the year, categorised as follows:



Employees

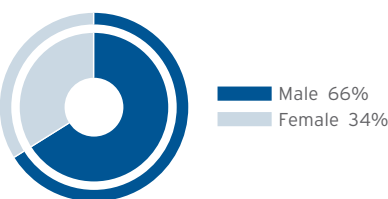
The Board recognises the valuable contribution that the Group's employees continue to make to its success, and aims to provide a working environment that reflects and rewards this. The Group now has 4,679 (2010: 4,283) employees based in eight countries.

Employment practices

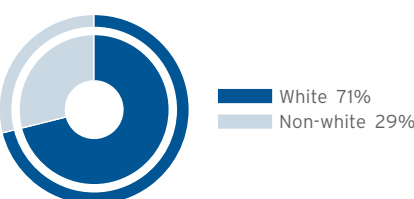
The Group's policy is to provide equal opportunities for all employees, irrespective of race, nationality, gender, sexual orientation, marital status, religion or political belief, disability or age. The Group is committed to meeting, at a minimum, the labour rights and legislation requirements in each country in which it operates and, in practice, often exceeds these. Our employment practices policies are introduced at newly-acquired businesses at the earliest opportunity after they join the Group.

In 2011, two new female directors were appointed to the Board. The Board recognises the importance of promoting diversity across the Group, and is committed to achieving a minimum of at least 25% female representation on the Board by 2013.

Gender diversity



Ethnic diversity



Development and training

We continue to address training and development requirements for employees at all levels within the organisation. All of our businesses consider training needs for their employees at a local level, in order to ensure that they have the right skill base to deliver their five year strategic plan. The Board also undertakes a detailed review of the future management requirements and succession plans as part of the annual strategic planning process. Specific plans have been developed in relation to sales and marketing, and engineering resources, in order to identify the requirements for future recruitment and development of our existing employees in these areas, and to ensure that we have the right capabilities to meet our future growth targets.

Our undergraduate "year in industry" placement scheme continues to be successful, and we aim to extend this programme each year. We are developing our graduate recruitment initiatives, and our acquisition of Roke, which has a well-established and highly successful graduate programme, has been of considerable benefit in this area.

Benefits

We aim to provide all of our employees with an attractive and competitive benefits package. Almost all of our businesses offer occupational pension scheme arrangements and our US employees receive health care. A number of our businesses offer health screening services and other health-related initiatives such as "stop-smoking" clinics.

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

Communications

The Group pursues a policy of employee communication through meetings (including team briefings and works councils) and in-house magazines by which employees are made aware of the progress of the Group and the companies in which they work. We also engage with our employees through representative bodies and trade unions.

Employee surveys are undertaken in relation to specific matters, such as health and safety, from time to time.

A Group magazine, The Chemring Eye, is published on a quarterly basis and distributed to all of our employees.

Corporate Responsibility Review

continued

In the environment

Our policy and practices

The Board believes that protecting the environment by minimising our environmental impact will help to secure the long term future of our businesses.

The Group's policy is to have all of our businesses certified to the environmental management system ISO14001, with all newly acquired businesses certified within two years of acquisition. We are fully compliant with this objective. ISO14001 requires the setting of environmental goals and objectives focused on local aspects and impact and in addition, we set expectations and monitor performance across the Group.

Land quality

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

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

The Group carries a £2.7 million provision in respect of these pre-acquisition environmental liabilities, which the Board considers to be adequate (see Note 26 of the financial statements).

Incidents

There were no significant environmental incidents in the year.

Performance

Energy and emissions

We have calculated that business travel represents less than 3% of our overall carbon footprint, and we therefore focus our efforts on energy utilisation in our facilities. We do not include emissions from our supply chain nor use or disposal of products in our carbon footprint calculation.

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

Source	2011 (tonnes CO ₂)	2010 (tonnes CO ₂)	2009 (tonnes CO ₂)	2008 (tonnes CO ₂)
Electricity	46,459	38,303	36,334	29,128
Gas	14,676	14,033	12,512	12,384
Oil	7,222	3,111	2,008	2,351
Total	68,357	55,447	50,854	43,863

The Group's total emissions increased by 20% against a strong increase in revenue, which means that our overall carbon intensity reduced as follows:

	2011	2010	2009	2008
Total emissions (tonnes)	68,357	55,447	50,854	43,863
Group revenue (£million)*	730	571	504	354
Tonnes of CO ₂ per £million of revenue	94	97	101	124

* Group revenue for 2011 and 2010 excludes revenue attributable to acquisitions

We are increasing our efforts to address energy conservation and thus indirect emissions. All sites have analysed their top energy consuming plant or buildings and created energy reduction programmes for the top five. Together, these represent more than 30% of the Group's total energy consumption.

All UK facilities participate in the Carbon Reduction Commitment programme, with the exception of Chemring Energetics UK at Ardeer in Scotland, which operates under a Climate Change Agreement.

The Group participated in the 2011 Carbon Disclosure Project.

Waste

Our total waste generation, excluding the recently acquired Chemring Detection Systems, increased during the year as a result of the inclusion of the businesses acquired during 2010 and our ongoing construction and renewal programmes.

	2011 (tonnes waste)	2010 (tonnes waste)	2009 (tonnes waste)
Recycled, non-hazardous	1,684	712	Not available
Recycled, hazardous	415	369	Not available
Not recycled, non-hazardous	1,018	1,161	Not available
Not recycled, hazardous	388	360	Not available
Total	3,505	2,602	1,876

Many of our facilities are permitted to burn waste materials on site within closely controlled facilities. We offer a collection service in the UK for time-expired marine pyrotechnics, including those produced by other manufacturers and these are transferred to an accredited third party for disposal.

The Group is currently investing in a new demilitarisation facility in Italy, which will allow the return of time-expired and obsolete munitions for decommissioning and disassembly. The individual materials will then be recycled back into the supply chain.

Water

Despite substantial revenue growth during the year, our absolute water consumption (excluding Chemring Detection Systems) continued to decline.

	2011 (m ³)	2010 (m ³)	2009 (m ³)
Total water consumption	1,441,000	1,550,000	1,762,000

In the community

Helping others

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

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

- Donations to a range of charities including Help for Heroes, SSAFA, The Army Benevolent Fund, Supporting Royal Marines, Queen Alexandra Hospital Home for Ex-Service Personnel, Houses for Heroes Appeal, various health and cancer charities, local hospitals and schools.
- Sponsorship of the 7 Air Assault Battalion Royal Electrical and Mechanical Engineers (REME) Field Gun Crew, the Red Devils, the Combined Services Under 23 Rugby Team and the Royal Artillery Gold Cup Day - all part of Team Army.
- Sponsorship of the UK Aerospace Youth Rocketry Challenge.
- Sponsorship of Portsmouth Festivities.

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

The Group is involved with a number of educational initiatives, notably including the sponsorship of various local schools. The Group has a partnership agreement with Cranfield University, under which the Group has committed to the provision of significant funding for students' research activities over a five year period.

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

In the marketplace

Policy on the Sale of Goods and Services

The Group's vision is to become the leading producer of protection systems and energetic products for the global defence market, and we continue to deliver growth in this area through a combination of organic development and acquisitions. The scope of the Group's activities has broadened significantly in recent years, particularly with regards to the supply of components and sub-systems for various types of munitions, and there is increasing demand for the supply to our customers of third party products. Consequently, the Board has adopted a Policy on the Sale of Goods and Services, which provides guidance to all stakeholders on the products and services that the Group will supply, to which customers and to which countries, and sets out a clear definition of what we will not supply. All Group businesses are required to comply with this policy, which addresses both legal and ethical considerations with regards to certain products.

Ethics and business conduct

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

The managing directors of each business are required to report to the Chief Executive on compliance with the Global Code of Business Principles on an annual basis.

Anti-bribery and corruption

Following implementation of the UK Bribery Act 2010, the Group adopted a Bribery Act Compliance Manual, consolidating our previous anti-corruption policies and procedures which were aligned to the European Aerospace and Defence Association's Common Industry Standards on Anti-Corruption. Our anti-bribery programme now incorporates the following:

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

Our US businesses have also adopted an ethical compliance programme to satisfy US government requirements for ethical training for employees, compliance audits, a confidential reporting line for employees, and related investigation procedures.

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

Directors and corporate information



Peter C F Hickson~+ Dr David J Price CBE DSc PhD CEng CSci Paul A Rayner FCA Sarah L Ellard FCIS David R Evans

Non-Executive Chairman
Joined the Group as a non-executive director on 1 July 2010 and was appointed Chairman of the Board on 1 October 2010. Currently Chairman of Communis plc and a non-executive director of UK Coal plc. He has had senior management experience with a number of large international companies, and previous appointments include Chairman of Anglian Water Group, Senior Independent Director of London & Continental Railways Ltd, Finance Director of Powergen plc and non-executive directorships of Scottish Power plc, Marconi Corporation plc, RAC plc and Kazakhmys PLC. He is also a trustee and Board member of Orbis Charitable Trust, the international sight saving charity, and a Fellow of the Institute of Chartered Accountants. Aged 66.

Chief Executive
Joined the Group in April 2005 as Chief Executive. He is also a non-executive director of AZ Electronics Materials S.A. and a member of the Council for Southampton University. Formerly Managing Director, Naval Marine at Rolls-Royce plc and Managing Director of Thomson (UK) Holdings Ltd (now part of the Thales Group). Fellow of the Institute of Engineering & Technology, the Institute of Marine Engineering, Science & Technology, the Institute of Directors, and Companion of the Chartered Management Institute. Aged 56.

Finance Director
Joined the Group in June 1994 and acted as Finance Director to several Group companies before being appointed to the Board in August 1999. Formerly a Senior Audit Manager with Deloitte LLP. Fellow of the Institute of Chartered Accountants. Aged 50.

Group Legal Director & Company Secretary
Joined the Group in 1994, and was appointed as the Group Company Secretary in 1998. She was appointed to the Board on 7 October 2011. Prior to joining the Group, she trained and worked at Ernst & Young LLP. Fellow of the Institute of Chartered Secretaries and Administrators. Aged 41.

Non-Executive Director
Joined the Group in 1987 as Managing Director of the Countermeasures business and appointed to the Board in 1988. Prior to joining the Group he was a Managing Director of GEC-Marconi's division responsible for torpedos. He took up his current position as a non-executive director in April 2005, after stepping down as Chief Executive, a position he had held since January 1999. Currently a non-executive director and Chairman designate of Avon Rubber plc, and previously a non-executive director of Whatman PLC. Aged 65.



The Rt Hon Lord Freeman~* Ian F R Much*~+ Air Marshal Sir Peter Norriss KBE CB AFC MA FRAeS*~+ Vanda Murray OBE*~

Non-Executive Director
Joined the Group as a non-executive director in May 2006. Chairman of the Audit Committee. Currently a Consultant (formerly Partner) to PricewaterhouseCoopers, Chairman of Thales UK Advisory Board and a non-executive director of Savile Group PLC. He is also on the main Board of Thales S.A., France. Partner with Lehman Brothers Investment Bankers between 1969 and 1985. Member of Parliament from 1983 to 1997. Made a Privy Councillor in 1993. Minister 1985-1997. Aged 69.

Non-Executive Director
Joined the Group as a non-executive director in December 2004. Senior Independent Director and Chairman of the Remuneration Committee. Previous appointments include Chief Executive of De La Rue plc and T&N plc, and non-executive directorships of Admiral plc, Camelot plc, Manchester United plc and Simplyhealth Group Ltd. Currently Senior Independent Director and Chairman of the Remuneration Committee of Senior plc, and Chairman of the Remuneration Committee of BTG plc. Aged 67.

Non-Executive Director
Joined the Group as a non-executive director in May 2004. Currently a consultant to Tessella plc and a Senior Adviser to Newton. He is also a member of major programme review teams for the Office of Government Commerce and an adviser or court member at four universities. Formerly Deputy Chief of Defence Procurement (Operations) and Controller Aircraft on the Air Force Board. Past President of the Royal Aeronautical Society (2003-4). Aged 67.

Non-Executive Director
Joined the Group as non-executive director on 1 November 2011. Currently holds a portfolio of non-executive directorships, including Carillion plc, where she chairs the Remuneration Committee, The Manchester Airport Group plc and Microgen plc. She has also been appointed to the Board of Fenner plc as senior non-executive director and takes up this role in January 2012. Previous appointments include Deputy Chairman of the North West Regional Development Agency, non-executive director of SIG plc, Chief Executive Officer of Blick plc and UK Managing Director of Ultraframe PLC. She is a Fellow of the Chartered Institute of Marketing, and in 2002 was appointed OBE for Services to Industry and to Export. Aged 51.

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Registrars
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Membership of Board committees: * Audit, ~ Remuneration, + Nomination

Directors' Report

for the year ended 31 October 2011

The directors present their annual report, together with the audited financial statements of the Group and the Company for the year ended 31 October 2011.

Principal activities

The principal activities of the Group are the design, manufacture and sale of counter-IED equipment, countermeasures, pyrotechnics and munitions.

Business review

The Statement by the Chairman, the Review by the Chief Executive and the Review by the Finance Director, together with the sections of the annual report on each of the business segments, key performance indicators and principal risks, and the Corporate Responsibility Review on pages 4 to 33, provide a review of the Group's business development, performance and position during and at the end of the financial year; its strategy and likely future development; key performance indicators; and a description of the principal risks and uncertainties facing the business. Further information regarding financial risk management policies and financial instruments is given in Note 25 of the financial statements. There have been no significant events since the balance sheet date.

Results and dividends

The profit attributable to the Group's shareholders for the year was £73.9 million (2010: £66.7 million). The directors recommend a final dividend of 10.8p per ordinary share, which together with the interim dividend of 4p per ordinary share paid in August 2011 gives a total for the year of 14.8p (2010: 11.8p*). The final dividend is subject to approval by shareholders at the Annual General Meeting on 21 March 2012, and accordingly has not been included as a liability in these financial statements.

Directors and their interests

The present directors are shown on pages 34 and 35.

Mrs S L Ellard was appointed as a director on 7 October 2011 and Mrs V Murray was appointed as a director on 1 November 2011. Both of these directors will be seeking re-appointment under Article 87.1 of the Company's Articles of Association at the forthcoming Annual General Meeting. Details of Mrs Ellard's service contract with the Company are set out in the Directors' Remuneration Report on page 44. Mrs Murray does not have a service contract with the Company.

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

Details of the service contracts between the Company and the executive directors are set out in the Directors' Remuneration Report on page 44. The non-executive directors do not have service contracts with the Company.

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

None of the directors had a beneficial interest in any contract of significance to which the Group was a party during the year ended 31 October 2011.

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

Substantial shareholdings

At 23 January 2012 the following substantial holdings in the ordinary share capital of the Company had been notified to the Company in accordance with Chapter 5 of the Disclosure and Transparency Rules of the Financial Services Authority:

Name	% Interest
Invesco Limited	29.90
Cantillon Capital Management LLC	5.18
Old Mutual Asset Managers	5.13
Ameriprise Financial, Inc.	5.07
JP Morgan Chase & Co.	4.94
AXA S.A. and its group of companies	4.84
Standard Life Investments Ltd	4.57
Legal and General Group PLC	3.97
BT Pension Scheme Trustees Ltd as Trustees of the BT Pension Scheme	3.84
Hermes Equity Ownership Services Ltd	2.94

Employees and employee consultation

Details of the Group's employment policies and employee consultation practices are set out in the Corporate Responsibility Review on page 31.

Charitable and political donations

Charitable donations amounting to £129,000 (2010: £98,400) were made during the year. No political donations were made during the year £nil (2010: £nil).

Contractual arrangements

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

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

Policy on payment of suppliers

It is the policy of the Group that each of the Group companies should agree appropriate terms and conditions for its transactions with suppliers. These will range from standard written terms to individually negotiated contracts. Creditor days of the Group as at 31 October 2011 amounted to 49 days (2010: 61 days).

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

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

Date of award	Total number of shares awarded	Number of participants receiving awards
19 January 2011	693,720*	36
24 October 2011	17,492	1
Total	711,212	37

* Restated to reflect subdivision of 5p ordinary shares into 1p ordinary shares

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

On 29 July 2011, options were granted over 182,629 ordinary shares. Options over 85,885 ordinary shares were exercised during the year and options on 40,680 shares lapsed. Additional information is set out in Note 32.

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

On 29 July 2011, options were granted over 40,635 ordinary shares. Options over 42,111 ordinary shares were exercised during the year and options on 20,089 shares lapsed. Additional information is set out in Note 32.

Approach to share ownership

The Group actively encourages its employees to share in the future success of the Group. A fourth grant of options under the UK Sharesave Plan and the US Stock Purchase Plan, which were launched in 2008, took place during the year. The Board is considering the establishment of similar schemes for employees in Group companies outside of the UK and the US.

Share capital and shareholder rights

General

At the Annual General Meeting on 24 March 2011, the shareholders approved the subdivision of the Company's ordinary shares of 5p each into ordinary shares of 1p each. The Company's share capital now consists of ordinary shares of 1p each and preference shares of £1 each, which are fully paid-up and quoted on the main market of the London Stock Exchange. Full details of the movements in the issued share capital of the Company during the financial year are provided in Note 28 of the financial statements.

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

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

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

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

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

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

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

Issue of shares

Under the provisions of section 551 of the Act, the Board is prevented from exercising its powers under the Articles to allot shares without an authority in terms of the Act contained either in the Articles or in a resolution of the shareholders in general meeting. The authority, when given, can last for a maximum period of five years, but the Board proposes that renewal should be sought at each Annual General Meeting. Such proposal is set out as resolution 13 in the Notice of the Annual General Meeting.

Section 561 of the Act requires that an allotment of shares for cash may not be made unless the shares are first offered to existing shareholders on a pre-emptive basis in accordance with the terms of the Act. In accordance with general practice, to ensure that small issues of shares can be made without the necessity of convening a general meeting the Board proposes that advantage be taken of the provisions of section 571 of the Act to not apply the Act's pre-emptive requirements. Accordingly, a special resolution (set out as resolution 14 in the Notice of Annual General Meeting) will be proposed which, if passed, will have the effect of granting the directors the power to allot not more than 5% of the present issued ordinary share capital free of the requirements of section 561 of the Act. No issue of these shares will be made which would effectively alter the control of the Company without prior approval of the shareholders in general meeting.

Purchase of own shares

During the year, the Company purchased 300,000 (2010: 634,400*) of its ordinary shares, and 456,855 (2010: 500,055*) ordinary shares were distributed following vesting of awards under the Chemring Group Performance Share Plan. At 31 October 2011, the Company held a total of 1,343,145 ordinary shares in treasury (representing 0.69% of the ordinary shares in issue on 1 November 2011).

During November 2011 and prior to the start of the close period leading up to release of the Company's full year results, the Company purchased 1,000,000 additional ordinary shares for treasury. At 23 January 2012, the Company therefore held a total of 2,343,145 ordinary shares in treasury (representing 1.2% of the ordinary shares in issue on 23 January 2012). All purchases of ordinary shares were made by way of market purchases on the London Stock Exchange. Further details can be found in Note 30 of the financial statements.

A special resolution (set out as resolution 15 in the Notice of Annual General Meeting) will be proposed at the forthcoming Annual General Meeting, to renew the Company's authority to purchase its own shares in the market up to a limit of 10% of its issued ordinary share capital. The maximum and minimum prices are stated in the resolution. The directors believe that it is advantageous for the Company to have this flexibility to make market purchases of its own shares. The directors of the Company may consider holding repurchased shares pursuant to the authority conferred by this resolution as treasury shares. This will give the Company the ability to re-issue treasury shares quickly and cost effectively, and will provide the Company with additional flexibility in the management of its capital base. Any issues of treasury shares for the purposes of the Company's employee share schemes will be made within the 10% anti-dilution limit set by the Association of British Insurers.

* Restated to reflect subdivision of 5p ordinary shares into 1p ordinary shares.

Directors' Report

continued

The directors will only exercise this authority if they are satisfied that a purchase would result in an increase in expected earnings per share and would be in the interests of shareholders generally.

Statement of Directors' Responsibilities

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

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

- select suitable accounting policies and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

In preparing the Group financial statements, International Accounting Standard 1 requires that directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

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

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

Directors' Responsibility Statement

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Statement by the Chairman, the Review by the Chief Executive, the Review by the Finance Director, together with the sections of the annual report on each of the business segments, key performance indicators and principal risks, and the Corporate Responsibility Review, which are cross-referred from the Directors' Report, include a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Provision of information to auditors

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

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

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Close company provisions

As far as the directors are aware, the close company provisions of the Taxes Acts do not apply to the Group nor has there been any change in that respect since 31 October 2011.

Auditors

A resolution to re-appoint Deloitte LLP as auditors will be proposed at the Annual General Meeting.

Annual General Meeting

The resolutions to be proposed at the Annual General Meeting to be held on 21 March 2012, together with explanatory notes, appear in the separate Notice of Annual General Meeting sent to all shareholders.

Approved by the Board of Directors on 24 January 2012

Signed on behalf of the Board

S L Ellard

Group Legal Director & Company Secretary

Directors' Remuneration Report

for the year ended 31 October 2011

This report sets out the information required by the Companies Act 2006, and Regulation 11 and Schedule 8 to the Large and Medium Sized Companies and Groups (Accounts and Reports) Regulations 2008. The Report also satisfies the relevant requirements of the Listing Rules of the Financial Services Authority, and describes how the Board has applied the principles and complied with the provisions relating to directors' remuneration in the UK Corporate Governance Code. The Directors' Remuneration Report will be submitted to shareholders for approval at the Annual General Meeting on 21 March 2012.

The Companies Act 2006 requires the auditors to report to the Company's members on certain parts of the Directors' Remuneration Report and to state whether, in their opinion, those parts of the report have been properly prepared in accordance with the applicable accounting regulations. The report has therefore been divided into separate sections for the audited and unaudited information.

UNAUDITED INFORMATION

Remuneration Committee

During the year under review the Remuneration Committee comprised:

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

Mr Hickson, the Non-Executive Chairman of the Board, was considered to be independent on appointment.

Mrs V Murray was also appointed as a member of the Committee on her appointment as a non-executive director on 1 November 2011.

The Committee's principal responsibilities are:

- determining, agreeing with the Board and reviewing from time to time the overall policy for the remuneration of the Chairman, the executive directors, the Company Secretary, members of the Executive Committee and the first tier of senior management below the Executive Committee, and their individual remuneration packages and any changes thereto;
- reviewing the market competitiveness of the remuneration policy and arrangements;
- overseeing salary levels and remuneration packages for the second and third tiers of management;
- approving the terms and conditions of employment, and any changes thereto, of the executive directors;
- approving any compensation payments for executive directors;
- approving the design of, and determining targets for, any performance-related pay schemes operated by the Group;
- reviewing the design of all share incentive plans for approval by the Board and the Company's shareholders;
- providing oversight of potential remuneration-related risks arising across the Group; and
- overseeing any major changes in employee benefits structures across the Group.

With the exception of Mr Hickson, whose remuneration is determined by the Committee, none of the Committee members has any personal financial interest in the matters reserved for the Committee nor do they have any conflicts of interest arising from cross-directorships, and they are not involved in the day to day running of the Group's business. Therefore, they are regarded by the Board as independent. Mr Hickson does not participate in any discussions regarding his own remuneration.

The Committee met six times during the year. The Chief Executive attends meetings by invitation but no executive director or other employee is present during discussions relating to their own remuneration.

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

Advisers

During the year, the Committee retained New Bridge Street (an Aon Hewitt company) to advise on remuneration and incentive-plan related matters. The Company received no other services from New Bridge Street, or any other part of the Aon group of companies, during the year.

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

Remuneration policy for executive directors

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

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

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

Directors' Remuneration Report

continued

There were a number of important influences on the Committee's key decisions during the year:

- The Group completed two major acquisitions, Mecar S.A. and Roke Manor Research Limited, towards the end of the 2010 financial year, and in April 2011, the acquisition of the General Dynamics Armament and Technical Products' Detection Systems business (now Chemring Detection Systems, Inc.) was announced.
- The acquisition of Mecar has resulted in a significant increase in the Group's sales to non-NATO countries, and Roke has substantially augmented the Group's engineering capabilities in electronics, software and systems engineering. The Chemring Detection Systems acquisition creates substantial opportunities to enhance the Group's existing IED detection capabilities.
- These three new businesses have increased the Group's revenue by over £149 million on an annualised basis and, as a result, the operational complexity of managing the Group has intensified. These important factors were taken into account when the Committee adjusted salary levels for the executive directors with effect from 1 April 2011.
- Prospects within the defence sector were reasonably optimistic in the first half of the year. This was reflected in highly challenging earnings per share and cash flow targets set by the Committee for the annual bonus plan for the year ended 31 October 2011 and the equally demanding earnings per share targets set for the awards made under the Chemring Group Performance Share Plan in January 2011.
- However, the immediate outlook for the sector became increasingly uncertain towards the end of 2011. This has been an important influence on the Committee's thinking on a number of issues during the last few months, resulting in:
 - the imposition of a salary freeze for the executive directors for 2012;
 - the award of zero bonuses for the year ended 31 October 2011; and
 - reduced earnings per share growth targets for Performance Share Plan awards to be made during 2012.

Full details on the Committee's key decisions are set out below.

Comparator groups

The constituents of the sector-based comparator group utilised by the Committee for remuneration benchmarking purposes during the year were as follows:

Bodycote plc	Melrose PLC	Senior plc
Charter International plc	Morgan Crucible Company	Spectris plc
Domino Printing Services plc	QinetiQ Group PLC	Spirax-Sarco Engineering plc
Fenner PLC	Renishaw plc	Ultra Electronics Holdings plc
Halma plc	Rotork PLC	

The Committee also considered a general comparator group of forty nine FTSE companies with a similar market capitalisation and turnover of half to double that of the Group.

Base salaries and benefits

The executive directors' base salaries are reviewed annually by the Committee, and adjustments made, if appropriate, taking into account individual performance and comparable salary levels in the comparator groups set out above. The Committee refers to published salary surveys and data provided by its remuneration advisers, New Bridge Street, and also reviews the remuneration information presented in the annual reports of companies in the comparator groups.

The Committee has considered two annual salary reviews since the last Directors' Remuneration Report was published:

- *2011 adjustment (effective 1 April 2011):* As explained above, a key consideration for the Committee when it carried out the salary review in early 2011 was the enhanced complexity of the most senior executive roles following the expansion of the Group. The Committee also took into account the outstanding and sustained Group performance over a number of years and the demand for talented executive management with a proven track record in the industry. The Group has a relatively small executive management team, and the current members of this team have been critical to the Group's recent success. The Committee was keen to ensure that these individuals were motivated to remain with the Group. Accordingly, salaries for the executive directors were increased by 9.4% with effect from 1 April 2011. Revised salaries were, therefore, Dr Price £525,000 and Mr Rayner £328,125.
- *2012 adjustment (effective 1 April 2012):* In light of the increasingly difficult immediate trading outlook for the Group, given the current worldwide pressure on defence budgets, the Committee has determined that there should be no adjustment to the executive directors' salaries for 2012. The executive directors' salaries will, therefore, remain at the levels outlined above for 2012.

Mrs Ellard's base salary was increased from £180,000 to £200,000 on her appointment as an executive director on 7 October 2011.

The executive directors' base salaries will next be reviewed on 1 April 2013.

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

The main taxable benefits for executive directors are fully-expensed company cars and private medical insurance.

Annual bonuses

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

- a maximum bonus potential for the executive directors of 100% of base salary;
- three quarters of the bonus potential linked to two separate financial performance conditions, namely earnings per share and cash flow (with equal weighting). The conditions, which are set by the Committee, take into account a number of factors including budget, market expectations, long term growth prospects and the previous year's out-turn. No bonus is payable for achievement of less than 90% of target, with bonuses being earned thereafter on a straight-line basis up to the maximum for 110% or better achievement of target;
- one quarter of the bonus potential may be achieved in connection with the satisfaction of personal objective criteria set at the beginning of the financial year. These comprise a mixture of short term and longer term objectives linked to the delivery of the Company's strategic plan. No part of this element of bonus is payable unless threshold performance of both the financial conditions described above is achieved. The personal objectives set for the executive directors during the year were linked to the following strategic objectives:
 - improvements in the Group's operational efficiency
 - capture of key new programmes and delivery of new product development required for future organic growth
 - expansion of the Group's non-NATO activities
 - consolidation of previous acquisitions;
- 40% of any bonus payable is deferred as a conditional award of the Company's shares, with vesting subject to continued employment (save in good leaver scenarios) three years from the award of bonus; and
- the payment of any bonus remains ultimately at the discretion of the Committee.

Bonuses are non-pensionable.

The issues experienced by the Group right at the end of the financial year, resulting in delays in revenue, meant that the tough pre-set targets on earnings per share and cash flow were missed and no bonus was payable in respect of these elements. Although many of the personal objectives were successfully achieved, nothing is payable under this element of the bonus plan unless threshold performance is achieved under both the earnings per share and cash flow measures. In summary, the Committee's belief in rigorous target setting meant that despite the Group achieving 5% year-on-year underlying earnings per share growth and successfully implementing a number of key strategic developments for the longer-term benefit of the Group, no bonuses were payable to the executive directors for performance in the year under review.

The Committee has consistently set highly challenging bonus targets for the achievement of maximum bonuses. Despite the outstanding levels of earnings per share growth and returns to shareholders delivered by the Group in recent years, the executive directors did not receive maximum bonuses in any of the four years prior to the year under review, as evidenced by the chart below.

Year	2011	2010	2009	2008	2007
Growth in underlying EPS ¹	5%	15%	33%	43%	56%
Return to shareholders in year	-13%	15%	70%	-27%	41%

Executive	All	D J Price	P A Rayner	D J Price	P A Rayner	D J Price	P A Rayner	D J Price	P A Rayner
Maximum bonus potential (% of salary)	100%		100%		100%		100%		100%
Bonus paid (% of salary)	0%	61.81%	61.31%	94.13%	94.38%	52.1%	54.3%	46.1%	44.6%

¹Source: Statutory accounts for the years ended 31 October 2011, 2010, 2009, 2008 and 2007

The basic structure of the bonus plan will remain unchanged for the current financial year, namely with a maximum bonus potential of 100% of base salary, with 40% of any bonus satisfied by the award of deferred shares. Clawback provisions exist in the bonus plan, which will enable the Company to clawback the deferred shares prior to vesting in the event of subsequent discovery of material misstatement of the Company's financial results for the financial year in respect of which the deferred shares were awarded. Bonuses will continue to be determined by a mixture of earnings per share, cash flow and personal objectives.

Directors' Remuneration Report

continued

Long term incentives

Performance share plan

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

- conditional awards can be made of the Company's shares worth no more than 150% of base salary each year under normal circumstances (200% of salary in exceptional circumstances);
- awards will vest three years after grant subject to the extent to which a demanding performance condition has been achieved over a single three year performance period (with no ability to re-test the performance condition). The performance condition is based on the growth of the Company's earnings per share in excess of RPI over three consecutive financial years. The Committee considers an earnings per share condition to most closely align the interests of participants with those of the Company's shareholders;
- the vesting schedules for awards granted to date are as follows:

	Awards to executive directors	Total earnings per share growth per annum (not compounded) over three financial years	
		Threshold vesting	Full vesting
Awards made prior to 23 January 2007	100% of salary	RPI +5% p.a. (33% vests)	RPI+15% p.a.
Awards made on 24 January 2007	100% of salary	RPI +7.5% p.a. (33% vests)	RPI+20% p.a.
Awards made on or after 23 January 2008	100% of salary	RPI +10% p.a. (25% vests)	RPI+30% p.a.
Awards made on or after 23 January 2010	125% of salary	RPI + 10% p.a. (25% vests for awards up to 100% of salary)	RPI + 25% p.a. (for awards up to 100% of salary)
		RPI + 25% p.a. (for any additional awards over 100% of salary)	RPI + 30% (for awards up to 125% of salary)
Awards made on or after 19 January 2011	150% of salary	RPI + 10% p.a. (25% vests for awards up to 100% of salary)	RPI + 25% p.a. (for awards up to 100% of salary)
		RPI + 25% p.a. (for any additional awards over 100% of salary)	RPI + 35% p.a. (for awards up to 150% of salary)*

* For awards of up to 150% of base salary, 100% will vest at RPI + 25%, with the additional 50% vesting on a straight-line basis between RPI + 25% and RPI + 35%
No shares vest for growth below the threshold vesting target. Vesting is calculated on a straight-line basis for growth between the threshold and full vesting targets;

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

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

Date of award	Total number of shares awarded	Number of participants receiving awards
19 January 2011	693,720*	36
24 October 2011	17,492	1
Total	711,212	37

* Restated to reflect subdivision of 5p ordinary shares into 1p ordinary shares

Details of the awards made to executive directors during the year are set out on page 46.

Clawback provisions apply to all awards under the plan from 2011 onwards, which will enable the Company to clawback awards prior to vesting in the event of subsequent discovery of material misstatement of the Company's financial results, and after having first clawed back any unvested deferred shares awarded as part of the annual bonus for the financial year in which the results were misstated.

The Committee has historically set highly challenging earnings per share targets, reflecting the Board's confidence in the strong growth prospects for the Group but also the Committee's firm commitment to align the interests of shareholders with the executive management through the use of significant levels of potential variable pay triggered by exceptional levels of performance.

In considering the performance condition for awards which will be made in 2012, the Committee has remained consistent with its commitment to tough target setting. However, with defence budgets around the world under significant pressure, growth prospects for the Group are considerably more uncertain and this is reflected in the lower target growth range selected by the Committee.

The following vesting schedule will therefore apply for awards made in 2012:

Total earnings per share growth per annum (not compounded) over three financial years	Value of award that will vest
Less than 3% p.a.	0%
3% p.a.	15% of base salary
5% p.a.	25% of base salary
10% p.a.	100% of base salary
10% p.a. up to 12.5% p.a.	100% to 150% of base salary

Given the fluctuating nature of inflation over recent years, the Committee feels that it is more appropriate going forward to set a robust target that is expressed as a simple growth percentage (rather than a target expressed as RPI+x%). The Committee believes that this simpler structure will be more transparent for both shareholders and executives.

The Committee is satisfied that, although lower than for previous awards, this target range is still highly challenging given the current prospects for the Group and for the sector.

The Committee reviews, from time to time, the basis of the performance condition but continues to believe that the earnings per share metric mostly closely aligns the interests of executives and shareholders, and therefore remains an appropriate metric for the Group.

During the year under review, the Company purchased 300,000* (2010: 634,400*) treasury shares at a cost of £1.5 million for use in the plan. 456,855* shares were transferred from treasury to participants in the plan during the year on vesting of the awards made on 23 January 2008.

The executive directors are expected to build-up, over a five year period following appointment, and maintain a shareholding in the Company equivalent to one year's base salary. All of the executive directors currently hold shares in excess of this requirement. Other participants in the plan are expected to retain a shareholding equivalent to up to 50% of their base salary following vesting of the awards.

Other schemes

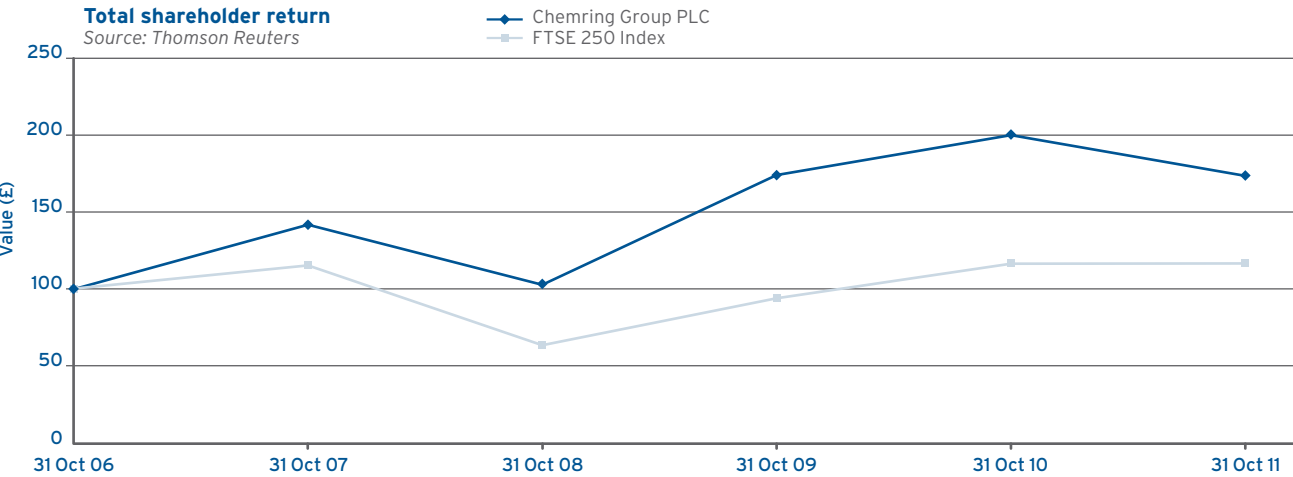
The Company operates all-employee savings-related share schemes in the UK (The Chemring Group 2008 Sharesave Plan) and the US (The Chemring Group 2008 US Stock Purchase Plan). There are no performance criteria for these arrangements, and options are issued to all participants in accordance with UK HM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

The Company complies with the dilution guidelines contained within the "ABI Principles of Remuneration". At 31 October 2011, awards outstanding and issued under all share schemes during the previous ten years amounted to 3.07% of the ordinary share capital of the Company. At 31 October 2011, awards outstanding and issued under executive share schemes during the previous ten years amounted to 2.67% of the ordinary share capital of the Company.

* Restated to reflect subdivision of 5p ordinary shares into 1p ordinary shares.

Performance graph

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



This graph shows the value, by 31 October 2011, of £100 invested in Chemring Group PLC on 31 October 2006 compared with the value of £100 invested in the FTSE 250 Index. The other points plotted are the values at intervening financial year ends.

Directors’ Remuneration Report

continued

Pensions

The executive directors were members of the Chemring Group Staff Pension Scheme (“the Staff Scheme”) until 6 April 2010. This is an approved final salary scheme, which is contracted out of the State Second Pension, and which provides, at retirement, a pension of up to two-thirds of salary, subject to Inland Revenue limits. The pension arrangements for the executive directors under the Staff Scheme (1/80ths accrual rate only as far as the notional earnings cap) were well below market norms. The Committee therefore agreed that with effect from 6 April 2010, the executive directors would cease to participate in the Staff Scheme, and would instead, for all future service, receive a salary supplement of 20% of base salary.

Service contracts

The executive directors all have rolling service contracts, as follows:

	Date of commencement	Notice period
S L Ellard	7 October 2011	12 months
D J Price	4 April 2005	12 months
P A Rayner	27 August 1999	12 months

The contracts may all be terminated by the Company without notice, by making a payment in lieu of notice equal to the sum of the salary due for the unexpired notice period plus the fair value of any contractual benefits. The contracts for Mrs Ellard and Dr Price provide that any such sum may be paid in instalments, and in these circumstances there is a requirement to mitigate loss. Mr Rayner’s contract does not include such a provision.

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

Policy on outside appointments

With the specific approval of the Board in each case, executive directors may accept external appointments as non-executive directors of other companies, provided that they do not detract from their responsibilities to the Group, and may retain any related fees paid to them. Mr Rayner and Mrs Ellard do not currently hold any such external appointments. Dr Price is currently serving as a non-executive director of AZ Electronic Materials S.A., for which he receives and retains an annual fee of £55,000.

Non-executive directors

Mr Hickson’s letter of appointment provides for a three year appointment at a fixed fee of £170,000 per annum. The appointment may be terminated on six months’ notice by either party. It is anticipated that Mr Hickson will devote four to five days each month to his role, subject to the overriding requirement that he allocates sufficient time to the role as is reasonably necessary for the proper performance of his duties.

The other non-executive directors are all appointed for three year terms under letters of appointment covering, amongst other items, their terms of appointment and expected time commitment. The appointments may be terminated earlier by and at the discretion of either party upon three months’ written notice. The Rt Hon Lord Freeman is currently serving his second three year term as a non-executive director, which will expire on 25 May 2012. Mr Evans’ current appointment as a non-executive director will terminate on 30 March 2012, and he has advised the Board that he intends to retire and will not therefore seek reappointment at the Annual General Meeting on 21 March 2012. Mr Much and Air Marshal Sir Peter Norriss are currently serving their third terms, under letters of appointment which have been extended on a rolling basis. Mrs Murray’s first three year term will expire on 31 October 2014.

Following a review of time commitment and market rates, the basic fees for the non-executive directors were adjusted during the year. The basic fee payable to each of the five non-executive directors is now £55,000 per annum. The Rt Hon Lord Freeman and Mr Much each receive an additional fee of £8,000 per annum, in respect of their Chairmanship of the Audit Committee and Remuneration Committee respectively. Mr Much also serves as the Senior Independent Director but he receives no additional fee for this role. Fees for the non-executive directors have been fixed for the next three years.

The Company provides private medical insurance for Mr Evans, Mr Hickson and Air Marshal Sir Peter Norriss, and their respective spouses.

The non-executive directors do not participate in the Company’s pension, bonus or share-based incentive schemes. However, Mr Evans does receive a pension from the Chemring Group Staff Pension Scheme, which he accrued during his former employment with the Company.

AUDITED INFORMATION

Directors’ emoluments

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

	Salaries and fees		Bonuses (cash and deferred shares)		Cash pension supplement		Taxable benefits		Total	
	2011 £000	2010 £000	2011 £000	2010 £000	2011 £000	2010 £000	2011 £000	2010 £000	2011 £000	2010 £000
Executives										
D J Price	506	455	-	297	101	56	34	35	641	843
P A Rayner	316	284	-	186	63	35	22	21	401	526
S L Ellard (appointed 7 Oct 2011)	17	-	-	-	3	-	1	-	21	-
Non-executives										
D R Evans	50	43	-	-	-	-	1	1	51	44
R N Freeman	58	51	-	-	-	-	-	-	58	51
P C F Hickson	170	57	-	-	-	-	2	-	172	57
I F R Much	58	51	-	-	-	-	-	-	58	51
P C Norriss	50	43	-	-	-	-	2	2	52	45
Total remuneration	1,225	984	-	483	167	91	62	59	1,454	1,617

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

Aggregate directors’ remuneration

The total amounts for directors’ remuneration were as follows:

	2011 £m	2010 £m
Salaries, fees, bonuses and benefits in kind	1,287	1,526
Cash pension supplement	167	91
Gains on exercise of share options and vesting of awards under long-term incentive schemes	1,084	877
	2,538	2,494

Directors’ share interests

The interests of the directors in the ordinary shares of the Company at 1 November 2010, or date of appointment if later, and 31 October 2011 are shown below. All are beneficial holdings.

	2011 Number	2010 Number*
S L Ellard	75,035	75,035
D R Evans	75,000	75,000
R N Freeman	1,750	1,750
P C F Hickson	40,000	20,000
I F R Much	26,500	26,500
P Norriss	27,000	27,000
D J Price	641,720	618,815
P A Rayner	212,500	200,000

* Restated to reflect subdivision of 5p ordinary shares into 1p ordinary shares

The directors’ share interests at 31 October 2011 include shares held by the directors’ adult children, as required by the Companies Act 2006.

Mrs Murray has no interests in the ordinary shares of the Company.

During November 2011 and prior to the start of the Company’s close period preceding the release of its annual results, Dr Price purchased an additional 9,000 shares, Mr Rayner 1,000 shares, Mr Hickson 25,000 shares and Air Marshal Sir Peter Norriss an additional 1,000 shares. No other movements have taken place between 31 October 2011 and 23 January 2012.

Directors' Remuneration Report

continued

Performance share plan

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

	Number of shares under award*				At 31 Oct 2011	Date of vesting	Share price on date of award (p)
	At 1 Nov 2010	Awarded during the year	Lapsed during the year	Vested during the year			
S L Ellard	14,785	-	-	14,785	-	24 Jan 2011	379.0
	23,190	-	-	-	23,190	21 Jan 2012	406.2
	16,460	-	-	-	16,460	20 Jan 2013	615.0
	-	25,520	-	-	25,520	19 Jan 2014	636.8
	54,435	25,520	-	14,785	65,170		
D J Price	90,020	-	-	90,020	-	24 Jan 2011	379.0
	100,000	-	-	-	100,000	21 Jan 2012	406.2
	70,990	-	-	-	70,990	20 Jan 2013	615.0
	15,740	-	-	-	15,740	18 Mar 2013	667.8
	-	111,350	-	-	111,350	19 Jan 2014	636.8
	276,750	111,350	-	90,020	298,080		
P A Rayner	56,580	-	-	56,580	-	24 Jan 2011	379.0
	62,500	-	-	-	62,500	21 Jan 2012	406.2
	44,370	-	-	-	44,370	20 Jan 2013	615.0
	9,835	-	-	-	9,835	18 Mar 2013	667.8
	-	69,590	-	-	69,590	19 Jan 2014	636.8
	173,285	69,590	-	56,580	186,295		

* Figures restated to reflect subdivision of 5p ordinary shares into 1p ordinary shares

Awards granted on 23 January 2008 vested in full during the year, as the maximum earnings per share growth target was achieved. The share price on the date of vesting was 666.6p. The value of the vested award, and therefore the gain on vesting, to Dr Price was £600,073.32, to Mr Rayner was £377,162.28, and to Mrs Ellard was £99,156.75.

Awards worth 150% of base salary were granted to Dr Price and Mr Rayner on 19 January 2011; 25% of the shares under these awards will vest if earnings per share growth is RPI+10% p.a. over the three year performance period, rising on a straight-line basis to vesting of the award worth 100% of base salary for growth of RPI+25% p.a, and vesting of an additional award worth 50% of base salary for growth between RPI+25% p.a. to RPI+35% p.a. An award worth 100% of base salary was granted to Mrs Ellard on 19 January 2011.

Share options

The holdings by the directors of share options granted under the Chemring Group 2008 UK Sharesave Plan at 1 November 2010 and 31 October 2011 are shown below.

	Number of share options*				Exercise price(p)	Market price at date of exercise (p)	Date from which exercisable	Expiry date
	At 1 Nov 2010	Granted during the year	Lapsed during the year	Exercised during the year				
S L Ellard	2,515	-	-	2,515	373.6	528.5	1 Oct 2011	1 Apr 2012
		1,776	-	-	508.0	-	1 Oct 2014	1 Apr 2015
D J Price	2,515	-	-	2,515	373.6	528.5	1 Oct 2011	1 Apr 2012
P A Rayner	4,355	-	-	-	373.6	-	1 Oct 2013	1 Apr 2014

* Figures restated to reflect subdivision of 5p ordinary shares into 1p ordinary shares

Options granted on 1 October 2008 became exercisable during the year. The share price on the date of exercise was 528.5p. The gain on exercise to each of Dr Price and Mrs Ellard was £3,896.

The closing market price of the ordinary shares at 31 October 2011 was 510p. During the year, the ordinary shares traded within the range 485p to 736.5p.

Deferred shares

Details of awards of deferred shares made to the executive directors under the annual performance-related bonus plan are set out below (the values of these shares at award are included in the bonus figures in the directors' emoluments table):

	Number of deferred shares under award*				At 31 Oct 2011	Date of vesting	Share price on date of award (p)
	At 1 Nov 2010	Awarded during the year	Lapsed during the year	Vested during the year			
D J Price	10,370	-	-	10,370	-	18 Jan 2011	388.8
	13,015	-	-	-	13,015	13 Jan 2012	400.0
	16,705	-	-	-	16,705	12 Jan 2013	591.6
	-	18,355	-	-	18,355	11 Jan 2014	636.8
	40,090	18,355	-	10,370	48,075		
P A Rayner	6,305	-	-	6,305	-	18 Jan 2011	388.8
	8,485	-	-	-	8,485	13 Jan 2012	400.0
	10,470	-	-	-	10,470	12 Jan 2013	591.6
	-	11,380	-	-	11,380	11 Jan 2014	636.8
	25,260	11,380	-	6,305	30,335		

* Figures restated to reflect subdivision of 5p ordinary shares into 1p ordinary shares

Pensions

The following table sets out the pension benefits accrued by the directors during the year, as a consequence of their former membership of the Chemring Group Staff Pension Scheme.

	Pension (£p.a.)	Total benefit accrued at 31 Oct 2010		Pension (£p.a.)	Total benefit accrued at 31 Oct 2011		Increase in transfer value during year (less members' contributions) (£)
		Cash (£)	Transfer value of accrued benefit at 31 Oct 2010 (£)		Cash (£)	Transfer value of accrued benefit at 31 Oct 2011 (£)	
S L Ellard	19,669	59,006	239,437	19,669	59,006	298,770	59,333
D J Price	7,725	23,175	110,850	7,725	23,175	126,930	16,080
P A Rayner	24,462	73,387	368,480	24,462	73,387	443,574	75,094

- (i) Transfer values represent liabilities of the applicable scheme, and do not represent sums paid to the individuals.
- (ii) Transfer values have been calculated on the basis of actuarial advice in accordance with actuarial professional guidance.
- (iii) All directors left the pension scheme with an entitlement to deferred benefits on 6 April 2010.

Approval of the Directors' Remuneration Report

The Directors' Remuneration Report was approved by the Board on 24 January 2012.

Signed on behalf of the Board

I F R Much

Chairman of the Remuneration Committee

Statement on Corporate Governance

Introduction by the Chairman

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

The detailed statement below sets out how the Company has applied the main and supporting principles of good governance set out in the UK Corporate Governance Code issued in June 2010 by the Financial Reporting Council (“the Code”). I would like to draw your attention to some specific examples of how the principles relating to the role and effectiveness of the Board are applied in practice:

Setting of strategic aims

The Board convenes annually for two days in October to undertake a detailed review of the updated five year plan for the Group, which includes a detailed assessment of the current and future resource requirements for delivery of the plan. Risks to achievement of the five year plan are reviewed regularly by the Group’s Risk Committee and the full Board.

Setting of values

The Board sets the standards of behaviour expected of all employees and third parties acting on our behalf, as set out in our Global Code of Business Principles. This is reviewed on an annual basis.

Role of the Chairman

Following my appointment as Chairman in October 2010, I took the opportunity to consult with each of the directors individually to discuss their views on the operation and effectiveness of the Board meetings and the interaction of its members. We now have an agenda for our meetings which has an increased focus on key strategic issues.

Composition of the Board

Following a review by the Board during the year of its current balance of skills, experience and knowledge of the Company, two new directors were appointed. Sarah Ellard, the Company Secretary since 1998, was appointed as Group Legal Director, and Vanda Murray was appointed as a new non-executive director. Both individuals bring valuable experience and a new perspective to the Board.

Induction

We have implemented a structured induction programme for Mrs Murray, which includes visits to a number of the Group’s sites. Mrs Ellard’s induction requirements are different, as she is already very familiar with the Group’s operations and the workings of the Board, but we have identified other plans for her future personal development in order to enhance her contribution to the Board.

The Company has been in full compliance with the provisions of Code throughout the year ended 31 October 2011.

P C F Hickson
Chairman

The Board

The Board currently comprises three executive directors and six non-executive directors (including the Chairman). The Board considers that the Chairman and four of the other non-executive directors, The Rt Hon Lord Freeman, Mr Much, Mrs Murray and Air Marshal Sir Peter Norriss are independent in character and judgment, and meet the criteria for independence set out in the Code. The directors’ biographical details are set out on pages 34 and 35.

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

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

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

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

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

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

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

In addition to chairing the Board, the Chairman is responsible for ensuring that the Board is kept properly informed and is consulted on all decisions reserved to it; promoting constructive relations between the executive and non-executive directors; ensuring that the training and development needs of directors are identified and the performance of the Board evaluated on a regular basis; ensuring effective communication with shareholders and acting as a conduit to ensure that the views of shareholders are communicated to the Board. The Chairman’s other business commitments, which are detailed on page 34, were fully disclosed to the Board prior to his appointment and the Board is comfortable that he has sufficient time available to commit to his role.

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

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

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

The non-executive directors have letters of appointment covering, amongst other items, their terms of appointment and expected time commitment. These letters of appointment provide for a three year appointment, unless terminated earlier by and at the discretion of either party upon three months’ written notice. Further details are set out in the Directors’ Remuneration Report on page 44, and copies of the letters of appointment are available for inspection on request to the Company Secretary.

In accordance with the Company’s Articles of Association, all directors are required to submit themselves for re-election every three years. However, in order to ensure compliance with the Code, all directors voluntarily submitted themselves for re-election at the Annual General in March 2011, and will do so again at the forthcoming Annual General Meeting.

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

The performance of the Board and its effectiveness are subject to periodic review by the Chairman. The Chairman and the non-executive directors consider the individual performance of the executive directors as part of the annual remuneration review, and the Chairman and the Chief Executive review the performance of the non-executive directors. During the year, a formal evaluation of the Board was also carried out by the Chairman, with the assistance of the Company Secretary. Feedback was sought from each of the directors on topics including: the quality of the Board’s review and monitoring of strategic aims; ways in which the mix of skills and

knowledge on the Board could be improved; the effectiveness of the Board’s interaction with shareholders and with employees; the Board agenda; flow of information to the Board; Board succession; and the operation of the Board Committees. Each director was also invited to propose three objectives for the Board for the forthcoming year. As a consequence of this exercise, a set of key objectives was agreed, which the Board will work towards achieving this year. The Board intends to comply with the Code guidance that its performance evaluation should be externally facilitated at least every three years.

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

Meetings attendance

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

	Board (13 meetings)	Audit Committee (3 meetings)	Nomination Committee (1 meeting)	Remuneration Committee (6 meetings)
P C F Hickson	12(13)	-	1(1)	6(6)
S L Ellard	1(1)	-	-	-
D R Evans	12(13)	-	-	-
The Rt Hon Lord Freeman	12(13)	3(3)	-	6(6)
I F R Much	11(13)	3(3)	1(1)	6(6)
Air Marshal Sir Peter Norriss	12(13)	3(3)	1(1)	6(6)
D J Price	12(13)	-	-	-
P A Rayner	13(13)	-	-	-

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

Board Committees

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

Audit Committee

The Rt Hon Lord Freeman (Committee Chairman)
Vanda Murray (Appointed 1 November 2011)
Ian Much
Air Marshal Sir Peter Norriss

The Rt Hon Lord Freeman, who is a chartered accountant, is Chairman of the Audit Committee; his full biographical details are set out on page 35. The Committee met three times during the year, and operates within formal written terms of reference. As referred to above, the terms of reference are available on the Company’s website. Meetings of the Committee are attended, at the invitation of the Chairman of the Committee, by the external auditors, the Chairman of the Board, the Finance Director and representatives from the Group finance and internal audit function. The Committee meets with the auditors on a regular basis without the executive directors being present. The Company Secretary acts as secretary to the Committee and minutes of meetings are circulated to all Board members.

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

Statement on Corporate Governance

continued

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

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

- reviewing the Group’s draft 2010 financial statements and 2011 interim results statement prior to Board approval, and reviewing the external auditors’ detailed reports thereon;
- reviewing the appropriateness of the Group’s accounting policies, and reviewing various accounting matters raised by management and the external auditors in the context of financial disclosures;
- considering and approving changes to the Group’s accounting policy manual;
- reviewing the potential impact on the Group’s financial statements of certain matters such as impairments of fixed asset values and the adoption of new accounting standards;
- reviewing the external auditors’ plan for the 2011 interim review and the 2011 year end audit, including reviewing the key risks on the accounts, confirmation of auditor independence and the proposed audit fee, and approving the terms of engagement for the audit;
- receiving reports from the Risk Committee and reviewing the Group’s risk register;
- reviewing the Group’s anti-bribery policies and procedures, and the compliance of each of the Group’s businesses with these policies;
- monitoring the Group’s financing structures;
- monitoring the Group’s key financial ratios and credit ratings;
- overseeing the application of the Group’s whistleblowing policy and procedures for employees;
- reviewing the work undertaken by the Group’s internal audit function, assessing the adequacy of the internal audit resource and recommending changes for increasing the scope of the internal audit activities; and
- implementing the Group’s policy on the provision of non-audit services by the auditors, taking into account relevant guidance and best practice.

The Group’s internal audit programme incorporates an annual rolling review of all businesses, and focuses on both financial and non-financial controls and procedures. Newly acquired businesses are subjected to a detailed review by the internal audit function immediately post-completion. The Committee approves the annual internal audit plan and receives regular reports from the internal auditors.

The Committee has considered the likelihood of a withdrawal of the current auditors from the market and noted that there are no contractual obligations to restrict the choice of external auditors.

To assess the effectiveness of the external auditors, the Committee reviewed:

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

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

The Committee keeps under review the level of any non-audit services which are provided by the external auditors, to ensure that this does not impair their independence and objectivity. The Committee has adopted a policy which states that the external auditors should not be appointed to provide services in relation to corporate finance matters, unless the Committee agrees that their appointment would be in the best interests of the Company’s shareholders in particular circumstances and would not create any direct conflict with their role as external auditors. The Committee, in conjunction with the Finance Director, ensures that the Group maintains a sufficient choice of appropriately qualified audit firms. Details of the amounts paid to the external auditors during the year for audit and other services are set out in the notes to the financial statements on page 68.

Nomination Committee

- Peter Hickson (Committee Chairman)
- Ian Much
- Air Marshal Sir Peter Norriss

Mr Hickson is Chairman of the Nomination Committee but, in accordance with the Committee’s terms of reference, is not permitted to chair meetings when the Committee is dealing with the appointment of his successor. As referred to above, the Committee’s terms of reference are available on the Company’s website.

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

During the year, the Board considered the contents of Lord Davies’ Review into Women on Boards published in February 2011, and has since noted the changes to the Code in relation to diversity which will take effect from 1 October 2012. The Board supports the principles set out in the Davies Review, as reflected by the fact that the Board now has two female members. The Board also

recognises the importance of promoting diversity across the Group, and is therefore committed to achieving a minimum of at least 25% female representation on the Board by 2013.

Remuneration Committee

- Ian Much (Committee Chairman)
- The Rt Hon Lord Freeman
- Peter Hickson
- Vanda Murray (Appointed 1 November 2011)
- Air Marshal Sir Peter Norriss

The Remuneration Committee met six times during the year. Further details on the Committee and the Company’s policy on directors’ remuneration and long term incentive schemes are included within the Directors’ Remuneration Report.

Executive Committee

- David Price (Chief Executive)
- Terry Bridgewater (Group Director of Safety)
- Richard Dellar (Managing Director – Chemring International)
- Sarah Ellard (Group Legal Director)
- Stephen Grinham (Managing Director – Roke Electronics)
- Michael Helme (Managing Director – Chemring Europe)
- Daniel McKenrick (President – Chemring North America)
- Rupert Pittman (Director of Communications & Investor Relations)
- Paul Rayner (Group Finance Director)

Dr Price chairs the Executive Committee, which meets monthly. The Executive Committee is responsible for the executive day-to-day running of the Group, submission to the Board of strategic plans and budgets for the Group’s operations, and monitoring the day-to-day performance of the Group as a whole.

Relations with shareholders

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

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

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

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

All substantial issues, including the adoption of the annual report and financial statements, are proposed on separate resolutions at the Annual General Meeting. In line with best practice guidelines, voting at the forthcoming Annual General Meeting will be conducted by way of a poll. This allows all votes to be counted, not

just those of shareholders who attend the meeting. Poll results will be published on the Company’s website as soon as practicable following the conclusion of the meeting. The Notice of the Annual General Meeting is sent to shareholders at least twenty working days before the meeting.

Financial reporting

The Statement of Directors’ Responsibilities in respect of the financial statements and accounting records maintained by the Company is set out on page 38.

Internal control and risk management

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

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

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

- The Board assesses the key risks associated with achievement of the Group’s business objectives as part of the annual strategic planning process. Out of this process, each business establishes a five year plan and annual budget, which are subject to approval by the Board. The performance of each business against budget and prior years is reviewed on a monthly basis at both operational level and by the Board. Achievement of strategic business objectives and the associated risks are monitored by the Board on an ongoing basis.
- All businesses hold monthly operating meetings, which are attended by the respective Divisional Managing Directors. In addition, the Chief Executive and the Finance Director attend operational and strategic review meetings with each of the businesses on a quarterly basis. In the case of the US businesses, formal Board meetings are held quarterly, and these are attended by main Board directors and external non-executive directors appointed in the US. The US non-executive directors are available to provide guidance and monitor governance in the US businesses throughout the year. External non-executive directors are also appointed to the Boards of the Group’s Italian, Norwegian and Australian subsidiaries.
- Each business is required to comply with the Group’s Accounting Policy Manual, which sets out formal procedures for incurring certain types of expenditure and making contractual commitments. Compliance with the accounting policy manual is audited by the internal auditors, who report regularly to the Audit Committee on their findings.
- The Board retains primary responsibility for acquisitions and disposals, and financing arrangements for the Group. Treasury management, IT strategy, insurance and significant legal matters are dealt with centrally from the Group head office, and the Board receives regular reports on each of these items. Reviews of the Group’s pensions, insurance and risk management arrangements are carried out by external advisors on a regular basis.

Statement on Corporate Governance

continued

- The Group Director of Safety, supported by divisional Health and Safety Management Committees, co-ordinates and controls the activities of each business in relation to health and safety and environmental matters, which are a key focus for the Board in view of the nature of the Group's operations. The Chief Executive is the Board member nominated with specific responsibility for health and safety. The Chief Executive meets formally with health and safety professionals from each business on an annual basis.
- The Group has committed to adherence with the European Aerospace and Defence Association's Common Industry Standards on Anti-Corruption, and following the enactment of the UK Bribery Act 2010, the Group introduced a Bribery Act Compliance Manual incorporating its anti-bribery policies and procedures.

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

The Board confirms that it has reviewed the effectiveness of the Group's systems of internal control and risk management which were in place during the financial year ended 31 October 2011, and it confirms that systems of internal control and risk management compliant with the Code and the Turnbull Guidance were in place throughout the year and have remained in place up to the date of approval of these financial statements. Notwithstanding this, the Board will continue to take steps to embed internal control and risk management further into the operations of the Group and to deal with any areas of improvement which come to the attention of management and the Board.

Procedures to deal with directors' conflicts of interest

All directors have a duty under the Companies Act 2006 (the "2006 Act") to avoid a situation in which he or she has or can have a direct or indirect interest that conflicts or possibly may conflict with the interests of the Company. The Company's Articles of Association include provisions for dealing with directors' conflicts of interest in accordance with the 2006 Act. The Company has procedures in place to deal with situations where directors may have any such conflicts, which require the Board to:

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

Going concern

The directors have acknowledged the latest guidance on going concern. They have made appropriate enquiries and taken into account factors, which are further detailed in the Review by the Finance Director, such as:

- the strong order book of £878.3 million as at the year end, despite market conditions and government spending cuts in the US and Europe;
- the Group's underlying operating cash flow of £124.6 million during the year;
- the strong balance sheet at the year end of £475.4 million; and
- the Group's available banking facilities, which amount to £230 million with maturities through to April 2015 (see Note 22 of the financial statements).

The Group's banking covenants were all met during the year, and the expectation is that this will continue. As a consequence, the directors believe that the Company is well-placed to manage its risks. Details of how the Group manages its liquidity risk can be found in Note 25 of the financial statements.

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

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

Approved by the Board of Directors on 24 January 2012.
Signed on behalf of the Board

S L Ellard
Group Legal Director & Company Secretary

Independent Auditors' Report to the Members of Chemring Group Plc

We have audited the Group financial statements of Chemring Group PLC for the year ended 31 October 2011 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Statement of Changes in Equity, the Consolidated Balance Sheet, the Consolidated Cash Flow Statement, the Notes to the Consolidated Cash Flow Statement, and the related Notes 1 to 36. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the Group financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Group financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the Group financial statements:

- give a true and fair view of the state of the Group's affairs as at 31 October 2011 and of its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the Group financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement contained within the Statement on Corporate Governance in relation to going concern;
- the part of the Statement on Corporate Governance relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on directors' remuneration.

Other matters

We have reported separately on the parent company financial statements of Chemring Group PLC for the year ended 31 October 2011 and on the information in the Directors' Remuneration Report that is described as having been audited.

Nigel Mercer ACA (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
24 January 2012

Consolidated Income Statement

for the year ended 31 October 2011

				2011	2010 As restated*		
	Note	Underlying business performance ^a £m	Non- underlying items ^a £m	Total £m	Underlying business performance ^a £m	Non- underlying items ^a £m	Total £m
Continuing operations							
Revenue							
- continuing	4	730.7	-	730.7	597.1	-	597.1
- acquired	4	14.6	-	14.6	-	-	-
Total revenue	4,5	745.3	-	745.3	597.1	-	597.1
Operating profit							
- continuing		139.6	(33.5)	106.1	137.5	(29.6)	107.9
- acquired		2.2	(1.3)	0.9	-	-	-
Total operating profit	5,6	141.8	(34.8)	107.0	137.5	(29.6)	107.9
Share of post-tax results of associate	18	0.1	-	0.1	0.1	-	0.1
Finance income	8	0.1	-	0.1	0.5	-	0.5
Finance expense	9	(16.4)	-	(16.4)	(19.4)	-	(19.4)
Profit before tax	5	125.6	(34.8)	90.8	118.7	(29.6)	89.1
Tax	10	(28.8)	11.9	(16.9)	(30.7)	8.3	(22.4)
Profit after tax		96.8	(22.9)	73.9	88.0	(21.3)	66.7
Earnings per ordinary share*	12						
Basic		52.1p		39.8p	49.8p		37.8p
Diluted				39.4p			37.4p

^a Further information about non-underlying items can be found in Note 6
^{*} Restated figures for prior year to reflect the subdivision of shares (see Note 13) as well as the reclassification of certain items from underlying costs to non-underlying costs (see Note 6)

Consolidated Statement of Comprehensive Income

for the year ended 31 October 2011

	Note	2011 £m	2010 £m
Profit after tax for the year attributable to equity holders of the parent		73.9	66.7
Other comprehensive income			
(Losses)/gains on cash flow hedges		(0.1)	1.0
Exchange differences on translation of foreign operations		(7.4)	0.4
Actuarial (losses)/gains on defined benefit pension schemes	34	(1.8)	4.0
Movement on deferred tax relating to cash flow hedges		-	(0.3)
Movement on deferred tax relating to pension schemes		0.4	(1.4)
Current tax on items taken directly to equity		-	0.1
Deferred tax on items taken directly to equity		0.3	(0.5)
Total comprehensive income for the year attributable to equity holders of the parent		65.3	70.0

Consolidated Statement of Changes in Equity

for the year ended 31 October 2011

	Share capital £m	Share premium account £m	Special capital reserve £m	Hedging reserve £m	Revaluation reserve £m	Translation reserve £m	Retained earnings £m	Own shares £m	Total £m
At 1 November 2010	1.8	120.4	12.9	(2.7)	1.4	(12.4)	209.0	(7.2)	323.2
Profit after tax for the year	-	-	-	-	-	-	73.9	-	73.9
Other comprehensive income for the year	-	-	-	(0.1)	-	(7.1)	(1.4)	-	(8.6)
Total comprehensive income for the year	-	-	-	(0.1)	-	(7.1)	72.5	-	65.3
Ordinary shares issued	0.2	110.2	-	-	-	-	-	-	110.4
Dividends paid	-	-	-	-	-	-	(22.7)	-	(22.7)
Share-based payments (net of settlement)	-	-	-	-	-	-	(2.1)	-	(2.1)
Current tax relating to share-based payments	-	-	-	-	-	-	0.7	-	0.7
Transactions in own shares	-	-	-	-	-	-	-	0.6	0.6
Transfers between reserves	-	-	-	2.8	-	-	(2.8)	-	-
At 31 October 2011	2.0	230.6	12.9	-	1.4	(19.5)	254.6	(6.6)	475.4

	Share capital £m	Share premium account £m	Special capital reserve £m	Hedging reserve £m	Revaluation reserve £m	Translation reserve £m	Retained earnings £m	Own shares £m	Total £m
At 1 November 2009	1.8	120.3	12.9	(3.4)	1.4	(11.7)	157.5	(5.2)	273.6
Profit after tax for the year	-	-	-	-	-	-	66.7	-	66.7
Other comprehensive income for the year	-	-	-	0.7	-	0.4	2.2	-	3.3
Total comprehensive income for the year	-	-	-	0.7	-	0.4	68.9	-	70.0
Ordinary shares issued	-	0.1	-	-	-	-	-	-	0.1
Dividends paid	-	-	-	-	-	-	(18.7)	-	(18.7)
Share-based payments (net of settlement)	-	-	-	-	-	-	0.1	-	0.1
Current tax relating to share-based payments	-	-	-	-	-	-	0.1	-	0.1
Transactions in own shares	-	-	-	-	-	-	-	(2.0)	(2.0)
Transfers between reserves	-	-	-	-	-	(1.1)	1.1	-	-
At 31 October 2010	1.8	120.4	12.9	(2.7)	1.4	(12.4)	209.0	(7.2)	323.2

Consolidated Balance Sheet

as at 31 October 2011

	Note	£m	2011 £m	£m As restated*	2010 £m As restated*
Non-current assets					
Goodwill	14	243.4		231.0	
Development costs	15	23.3		13.3	
Other intangible assets	15	191.8		182.0	
Property, plant and equipment	16	231.1		197.5	
Interest in associate	18	1.5		1.1	
Deferred tax	27	21.7		17.3	
			712.8		642.2
Current assets					
Inventories	19	146.8		141.3	
Trade and other receivables	20	190.8		165.6	
Cash and cash equivalents	21,25	91.9		58.4	
Derivative financial instruments	25	1.9		1.9	
			431.4		367.2
Total assets			1,144.2		1,009.4
Current liabilities					
Borrowings	22	(86.0)		(65.6)	
Obligations under finance leases	23	(2.0)		(2.6)	
Trade and other payables	24	(212.4)		(222.3)	
Provisions	26	(2.5)		(1.9)	
Current tax liabilities		(5.6)		(7.7)	
Derivative financial instruments	25	(1.5)		(1.6)	
			(310.0)		(301.7)
Non-current liabilities					
Borrowings	22	(262.1)		(294.6)	
Obligations under finance leases	23	(4.4)		(3.0)	
Trade and other payables	24	(1.2)		(1.0)	
Provisions	26	(2.4)		(3.1)	
Deferred tax	27	(59.0)		(52.4)	
Preference shares	28	(0.1)		(0.1)	
Retirement benefit obligations	34	(25.2)		(23.0)	
Derivative financial instruments	25	(4.4)		(7.3)	
			(358.8)		(384.5)
Total liabilities			(668.8)		(686.2)
Net assets			475.4		323.2
Equity					
Share capital	28		2.0		1.8
Share premium account			230.6		120.4
Special capital reserve			12.9		12.9
Hedging reserve			-		(2.7)
Revaluation reserve			1.4		1.4
Translation reserve			(19.5)		(12.4)
Retained earnings			254.6		209.0
			482.0		330.4
Own shares	30		(6.6)		(7.2)
Equity attributable to equity holders of the parent			475.4		323.2
Total equity			475.4		323.2

* The restatement above relates to the finalisation of the fair value of acquired assets from prior year acquisitions (see Note 33)

These financial statements of Chemring Group PLC (registered number 86662) were approved and authorised for issue by the Board of Directors on 24 January 2012.
Signed on behalf of the Board

D J PriceP A Rayner

Consolidated Cash Flow Statement

for the year ended 31 October 2011

	Note	2011 £m	2010 £m As restated*
Cash flows from operating activities			
Cash generated from underlying operations	A	124.6	128.0
Acquisition related costs	33	(6.6)	(6.7)
Restructuring and incident costs	5	(6.7)	(1.9)
Cash generated from operations		111.3	119.4
Tax paid		(17.2)	(30.0)
Net cash inflow from operating activities		94.1	89.4
Cash flows from investing activities			
Dividends received from associate		0.1	0.1
Purchases of intangible assets		(12.9)	(7.8)
Purchases of property, plant and equipment		(48.8)	(40.9)
Proceeds on disposal of property, plant and equipment		0.4	-
Acquisition of subsidiary undertakings (net of overdraft assumed)	33	(58.0)	(176.8)
Net cash outflow from investing activities		(119.2)	(225.4)
Cash flows from financing activities			
Dividends paid	11	(22.7)	(18.7)
Interest paid		(17.8)	(14.0)
Proceeds on issue of shares		110.4	0.1
New borrowings		107.2	211.5
Capitalised facility fees		(4.8)	(2.7)
Repayments of borrowings		(112.6)	(41.7)
Proceeds from new finance leases		3.4	4.5
Repayments of finance leases		(2.6)	(0.7)
Purchase of own shares	30	(1.5)	(3.9)
Net cash inflow from financing activities		59.0	134.4
Increase/(decrease) in cash and cash equivalents during the year		33.9	(1.6)
Cash and cash equivalents at start of the year		58.4	61.3
Effect of foreign exchange rate changes		(0.4)	(1.3)
Cash and cash equivalents at end of the year	25	91.9	58.4

* Restated figures for prior year to reflect the reclassification of certain items from underlying costs to non-underlying costs in order to conform with the current year treatment of the corresponding items (see Note 6)

Notes to the Consolidated Cash Flow Statement

for the year ended 31 October 2011

A. Cash generated from operations	2011 £m	2010 £m As restated*
Operating profit from continuing operations	106.1	107.9
Operating profit from acquired operations	0.9	-
	107.0	107.9
Adjustment for:		
Amortisation of development costs	2.4	2.1
Amortisation of intangible assets arising from business combinations	24.3	17.0
Amortisation of patents and licences	0.2	0.3
Loss on disposal of property, plant and equipment	0.5	0.2
Depreciation of property, plant and equipment	17.2	11.6
(Gain)/loss on fair value movements on derivatives	(2.4)	4.0
Share-based payment expense	0.2	2.3
Difference between pension contributions paid and amount recognised in Income Statement	(0.4)	0.7
Decrease in provisions	(0.1)	(1.4)
Operating cash flows before movements in working capital	148.9	144.7
Increase in inventories	(1.2)	(19.2)
Increase in trade and other receivables	(22.5)	(44.0)
(Decrease)/increase in trade and other payables	(13.5)	37.9
	111.7	119.4
Acquisition related costs	5.7	6.7
Restructuring and incident costs	7.2	4.3
Provision release	-	(2.4)
Cash generated from underlying operations	124.6	128.0
Reconciliation of net cash flow to movement in net debt		
Increase/(decrease) in cash and cash equivalents during the year	33.9	(1.6)
Decrease/(increase) in debt and lease financing due to cash flows	9.4	(171.1)
Change in net debt resulting from cash flows	43.3	(172.7)
Acquired debt	-	(5.4)
Foreign exchange differences	3.0	(5.4)
Amortisation of debt finance costs	(1.5)	(1.2)
Movement in net debt in the year	44.8	(184.7)
Net debt at start of the year	(307.5)	(122.8)
Net debt at end of the year	(262.7)	(307.5)

* Restated figures for prior year to reflect the reclassification of certain items from underlying costs to non-underlying costs in order to conform with the current year treatment of the corresponding items

Analysis of net debt	As at 1 Nov 2010 £m	Cash flow £m	Non-cash changes £m	Exchange movement £m	As at 31 Oct 2011 £m
Cash at bank and in hand	58.4	33.9	-	(0.4)	91.9
Debt due within one year	(65.6)	(18.8)	(2.7)	1.1	(86.0)
Debt due after one year	(294.6)	29.0	1.2	2.3	(262.1)
Finance leases	(5.6)	(0.8)	-	-	(6.4)
Preference shares	(0.1)	-	-	-	(0.1)
	(307.5)	43.3	(1.5)	3.0	(262.7)

Notes to the Group Financial Statements

1. General information

Chemring Group PLC is a company incorporated in England and Wales under registration number 86662. The address of the registered office is Chemring House, 1500 Parkway, Whiteley, Fareham, Hampshire, PO15 7AF. The nature of the Group's operations and its principal activities are set out in Note 5 and in the Directors' Report on pages 36 to 38. These financial statements are the consolidated financial statements of Chemring Group PLC and its subsidiaries ("the Group").

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

Going concern

The directors have, at the time of approving the financial statements, a reasonable expectation that the Group and Company have adequate resources to continue to adopt the going concern basis of accounting in preparing the financial statements. Further detail is contained in the Statement on Corporate Governance on page 52.

2. Adoption of new and revised standards

The following IFRIC interpretations, amendments to existing standards and new standards have been adopted in the current year but have not impacted the reported results or the financial position:

- Comparative IFRS 7 *Disclosures for First Time Adopters*
- Amendment to IAS 32 *Classification of Rights Issues*
- IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments*
- Amendment to IFRS 1 *Limited Exemption from Comparative IFRS 7 Disclosures for First Time Adopters*
- Amendment to IFRS 2 *Share-based Payment*
- Amendment to IFRS 3 (revised 2008) *Business Combinations*
- Improvements to IAS 27 *Consolidated and Separate Financial Statement*
- IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments*

At the date of authorisation of these financial statements, the following standards and interpretations which have not been applied in these financial statements were in issue but not yet effective (and in some cases had not yet been adopted by the EU):

- Amendments to IFRS 1 *Severe Hyperinflation and Removal of Fixed Dates for First Time Adopters*
- Amendments to IFRS 7 *Disclosures: Transfers of Financial Assets*
- IFRS 9 *Financial Instruments*
- IFRS 10 *Consolidated Financial Statements*
- IFRS 11 *Joint Arrangements*
- IFRS 12 *Disclosure of Interests in Other Entities*
- IFRS 13 *Fair Value Measurement*
- Amendments to IAS 1 *Presentation of Items of Other Comprehensive Income*
- Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets*
- IAS 19 (Revised) *Employee Benefits*
- IAS 24 (Revised) *Related Party Disclosures*
- IAS 27 (Revised) *Separate Financial Statements*

- IAS 28 (Revised) *Investments in Associates and Joint Ventures*
- Amendment to IAS 34 *Interim Financial Reporting*
- Amendment to IFRIC 13 *Customer Loyalty Programmes*
- Amendment to IFRIC 14 *Prepayments of a Minimum Funding Requirement*
- IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine*

The directors anticipate that the adoption of these standards and interpretations in future periods will have no material impact on the financial statements of the Group, except for:

- IFRS 9 *Financial Instruments* - This will introduce a number of changes in the presentation of financial instruments.
- IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, IFRS 12 *Disclosure of Interests in Other Entities*, IAS 27 (Revised) *Separate Financial Statements* and IAS 28 (Revised) *Investments in Associates and Joint Ventures* - These will restrict the presentation options of the results of joint ventures in the financial statements, which the Group expect to enter into.
- Amendments to IAS 1 *Presentation of Financial Statements* - This will impact the presentation of various items within the Statement of Other Comprehensive Income by requiring the separation of items that will later be reclassified through the Income Statement from those that will never pass through the Income Statement.
- IAS 19 *Employee Benefits* (Revised) - This will impact the measurement of the various components representing movements in the defined benefit pension obligation and associated disclosures, but not the Group's total obligation.

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

3. Accounting policies

Basis of preparation

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

Basis of accounting

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

Accounting convention

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

Notes to the Group Financial Statements

3. Accounting policies continued

Basis of consolidation

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

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

Operating profit

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

Revenue recognition

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

Sale of goods

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

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

Rendering of services

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

Long term contracts

When the outcome of a long term contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion at the Balance Sheet date. This is normally measured by the proportion of contract costs incurred for work performed to date bear to the estimated total contract costs, except where this would not be representative of the stage of completion. Variations in contract work, claims and incentive payments are included to the extent that the amount can be measured reliably and its receipt is considered probable.

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

Investment income

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

(provided that the economic benefits will flow to the Group and the amount of revenue can be measured reliably).

Interest income is recognised when it is probable that the economic benefits will flow to the Group and the amount of revenue can be measured reliably. Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

Acquisitions

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

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

Where cost exceeds fair value of the net assets acquired the difference is recorded as goodwill.

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

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

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

In accordance with IFRS 3 (revised 2008) *Business Combinations*, acquisition costs have been expensed through the Income Statement. Acquisition related costs refer to external costs incurred in acquiring companies, together with the costs of abortive bids and the establishment of joint ventures.

Intangible assets

Goodwill

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

Acquired intangibles

For acquisitions after 1 November 2004, the Group recognises separately from goodwill intangible assets that are separable or arise from contractual or other legal rights and whose fair value can be measured reliably. These intangible assets are amortised at rates calculated to write down their cost or valuation to their estimated residual values by equal instalments over their estimated useful economic lives, which are considered to be:

Technology	- average of 10 years
Customer relationships	- average of 10 years
Orderbooks	- average of 2 years

Development costs

Development costs that qualify as intangible assets are capitalised as incurred, and once the relevant intangible asset is ready for use are amortised on a straight-line basis over its estimated useful life, averaging three years (2010: three years).

Patents and licences

Patents and licences are measured initially at purchase cost and are amortised on a straight-line basis over their estimated useful lives, averaging ten years (2010: ten years).

Property, plant and equipment

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

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

Investments in associates

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

Impairment of non-current assets

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

Inventories

Inventories are recorded at the lower of cost and net realisable value. Cost represents materials, direct labour, other direct costs and related production overheads and is determined using the first-in first-out (FIFO) method. Net realisable value is based on

estimated selling price, less further costs expected to be incurred to completion and disposal.

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

Borrowing costs

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

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

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

Government grants

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

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

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

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

Tax

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

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

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

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is

Notes to the Group Financial Statements

3. Accounting policies continued

probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each Balance Sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered. Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the Income Statement, except where it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

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

Special capital reserve

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

Foreign currencies

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

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

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

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

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

Financial instruments

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

Financial assets

Trade receivables

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

Cash and cash equivalents

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

Financial liabilities and equity instruments

Financial liabilities

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

Bank borrowings

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

Trade payables

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

Derivative financial instruments and hedge accounting

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

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

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

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

Hedges of net investments in foreign operations

Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in the Statement of Comprehensive Income and accumulated in the foreign currency translation reserve that forms part of the revenue reserve. The gain or loss relating to the ineffective portion is recognised immediately in the Income Statement.

Embedded derivatives

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

Retirement benefit costs

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

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

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

Leased assets

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

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

Share-based compensation

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

For grants made under the Group's share-based compensation schemes, the fair value is calculated at the grant date and recognised in the Income Statement on a straight-line basis over the vesting period, based on the Group's estimate of the shares that will eventually vest. The valuation of the options utilises a methodology based on the Black-Scholes model. For equity settled share-based grants, the total amount recognised is based on the fair value of the equity instrument measured at the date the award is made. At each Balance Sheet date the impact of any revision to

vesting estimates is recognised in the Income Statement over the vesting period. Proceeds received, net of any directly attributable transaction costs, are credited to share capital and share premium.

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

Post balance sheet events

Following IAS 10 *Events after the Balance Sheet Date*, the Group continues to disclose events that it considers material and non-disclosure of which can influence the economic decisions of users of the financial statements.

Critical accounting judgements and key sources of estimation uncertainty

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

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

Assessment of long term contractual arrangements

The Group has long term contracts that fall into different accounting periods. In assessing the allocation of revenues and costs to individual accounting periods, and the consequential assets and liabilities, the Group estimates the total revenues and costs forecast to arise in respect of the contract and the stage of completion based on an appropriate measure of performance as described under revenue recognition on page 60. The Group utilises assumptions and projections, principally relating to future material, labour and overhead costs. As a consequence, there is a risk that total contract costs will exceed those originally estimated and the margin will decrease. Changes to initial assumptions, which are reviewed on a regular basis, may result in revisions to estimated costs and anticipated margins. These are recognised in the period in which the estimated costs are determined.

Goodwill impairment review

Determining whether goodwill is impaired requires an estimation of the value-in-use of the cash-generating units to which goodwill has been allocated. The value-in-use calculation requires the entity to determine such assets, to estimate the future cash flows expected to arise from the cash-generating unit and to determine a suitable discount rate in order to calculate present value (see Note 14). In reviewing the carrying value of goodwill of the various businesses the Board has considered the separate plans and cash flows of these businesses consistent with the requirements of IAS 36 *Impairment of Assets* and is satisfied that these demonstrate that no impairment has occurred in respect of continuing operations.

Notes to the Group Financial Statements

3. Accounting policies continued

Tax
The largest category of deferred tax asset which contains significant estimation uncertainty and which requires management judgement in assessing its recoverability relates to tax losses carried forward (see Note 27 for further details).

Applicable accounting standards permit the recognition of deferred tax assets only to the extent that it is probable that future taxable profits will be available to utilise the tax losses carried forward. The assessment of future taxable profits involves significant estimation uncertainty, principally relating to an assessment of management’s projections of future taxable income based on business plans and ongoing tax planning strategies. These projections include assumptions about the future strategy of the Group, the economic and regulatory environment in which the Group operates, future tax legislation and customer behaviour, amongst other variables (see Note 27 for details of tax losses on which deferred tax assets have not been recognised).

Assets and liabilities acquired under business combinations
Under IFRS 3 (revised 2008) *Business Combinations*, it is necessary to separately identify and value any acquired intangible assets. In order to ascertain the values of the separate assets it is necessary for management to estimate the future cash flows attributable to the assets and estimate their useful economic lives (see Note 15). Assets and liabilities are recognised on acquisition when relevant, which include deferred tax assets on losses (see Note 27).

Pensions
The liability recognised in relation to retirement benefit obligations is dependent on a number of assumptions, including discount rate, mortality rate, salary increases and inflation. Any change in these assumptions would change the amount recognised (see Note 34).

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

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

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

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

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

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

4. Revenue

All of the Group’s revenue is derived from the sale of goods, revenue from long term contracts and provision of services. The following table provides an analysis of the Group’s revenue by destination.

	Continuing operations 2011 £m	Acquisitions 2011 £m	Total 2011 £m	Total 2010 £m
Revenue by destination				
UK	129.4	-	129.4	111.6
USA	307.3	12.8	320.1	293.1
Europe	80.1	-	80.1	72.9
Australia and Far East	49.7	1.1	50.8	44.1
Middle East	139.1	-	139.1	51.6
Rest of the world	25.1	0.7	25.8	23.8
	730.7	14.6	745.3	597.1

In addition to the revenues shown above there was finance income of £0.1 million (2010: £0.5 million).

The directors consider the only countries that are considered significant in accordance with IFRS 8 *Operating Segments* are the USA and the UK, as disclosed above, and Saudi Arabia, which is included within the Middle East category and which had revenue of £104.1 million (2010: £12.7 million).

5. Business segments

IFRS 8 *Operating Segments* requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the Chief Executive and the Board of Directors to allocate resources to the segments and to assess their performance. For management purposes the Group has four operating divisions – Counter-IED, Countermeasures, Pyrotechnics and Munitions. These divisions are the basis on which it reports its segmental information and the principal activities are as follows:

Counter-IED:	IED (improvised explosive device) detection equipment; chemical and biological threat detection equipment; IED electronic countermeasures; explosive ordnance disposal equipment; demilitarisation services.
Countermeasures:	Expendable active and passive countermeasures for naval and air platforms; land-based electronic warfare (EW) equipment.
Pyrotechnics:	Signals and illumination devices and payloads; cartridge/propellant actuated devices; pyrotechnic devices for satellite launch and deployment.
Munitions:	Missile and ammunition components; propellants; warheads; fuzes; energetic materials; medium and large calibre ammunition.

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

Business segments	2011 £m	2010 £m
Revenue		
Counter-IED	167.6	114.9
Countermeasures	200.8	196.3
Pyrotechnics	139.9	170.0
Munitions	237.0	115.9
Total revenue from third parties	745.3	597.1

Notes to the Group Financial Statements

5. Business segments continued

	2011 £m	2010 £m As restated*
Operating profit		
Counter-IED	31.9	28.1
Countermeasures	46.7	58.8
Pyrotechnics	32.4	40.1
Munitions	40.8	20.9
Unallocated corporate costs	(10.0)	(10.4)
Total underlying operating profit*	141.8	137.5
Acquisition related costs (see Note 33)	(5.7)	(6.7)
Restructuring and incident costs	(7.2)	(4.3)
Provision release	-	2.4
Intangible amortisation arising from business combinations	(24.3)	(17.0)
Gain/(loss) on fair value movements on derivatives	2.4	(4.0)
Non-underlying items	(34.8)	(29.6)
Total operating profit (see Note 6)	107.0	107.9
Share of post-tax results of associate	0.1	0.1
Finance income	0.1	0.5
Finance expense	(16.4)	(19.4)
Profit before tax	90.8	89.1

* The 2010 figures have been restated by including certain items that were identified separately within unallocated corporate costs, and other costs being moved from within underlying operating profit to non-underlying items in order to be consistent with the current year treatment of the equivalent costs

■ Before non-underlying items (see Note 6)

The accounting policies of the reportable segments are the same as the Group’s accounting policies described in Note 3.

Unallocated corporate costs

Unallocated corporate costs were £10.0 million, slightly down on 2010. In 2010 two non-recurring cost items which netted out at £1.9 million (£4.3m charge, £2.4m credit) were included in unallocated corporate costs, but with the re-formatting of the Income Statement this year these items have now been reclassified as non-underlying items in order to be consistent year-on-year. The impact of this reclassification is an increase in underlying operating profit for 2010 to £137.5 million from £135.6 million.

Intra-group transactions

There are no material intra-group transactions included within the above figures for revenue and profit.

Restructuring and incident costs

In 2011, the restructuring and incident costs related to the closure of Plant 3 at Alloy Surfaces Company, Inc. (£1.1 million) and the start-up of production at Mecar S.A. following the incident that occurred in September 2010 (£2.3 million). At the end of October 2011 the Board decided to exit some loss-making munitions product lines in the US and in addition to minor losses, a provision has also been made for excess inventory and fixed assets (£3.8 million). There is a £0.5 million difference between the expense in the Income Statement and the amount appearing in the Cash Flow Statement which relates to timing differences and non-cash movements.

In 2010, the restructuring costs of £1.5 million included the restructuring of the Group’s UK Counter-IED business. As a result, one of the two sites out of which it operated was closed.

In 2010, there were also two separate incidents that stopped production at the Kilgore Flares facility in Tennessee and Mecar in Belgium. As a result of these incidents, £2.8 million of non-recurring costs were incurred in respect of the write-off of damaged stock and destroyed assets. There is a difference between the expense in the Income Statement and the amount appearing in the Cash Flow Statement for restructuring and incident costs in 2010. This is due to only £0.4 million of the incident costs resulting in cash movements, along with the £1.5 million of restructuring costs.

Provision release

During 2010 part of the provision held in respect of the environmental liabilities associated with the Chemring Energetic Devices site in Illinois was released following a third party assessment of the provision. This resulted in a £2.4 million credit to the Income Statement.

Information about major customers

Included in revenues arising from the segments are revenues of approximately £246.6 million (2010: £236.7 million) and £103.6 million (2010: £12.5 million) which arose from sales to the Group’s two largest customers respectively. The largest customer had sales reported in all four of the Group’s reporting segments, whilst sales to the second largest customer were primarily from the munitions segment. These were the only individual customers where direct sales account for more than 10% of the total Group revenue for the year.

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

	Continuing operations 2011 £m	Acquisitions 2011 £m	Total 2011 £m	Total 2010 £m As restated*
Non-current assets by location				
UK	221.1	-	221.1	200.3
USA	231.5	83.3	314.8	275.7
Europe	150.3	-	150.3	151.0
Australia and Far East	26.6	-	26.6	15.2
	629.5	83.3	712.8	642.2

* See Note 33

6. Operating profit

The following table shows a reconciliation of cost by function:

	2011 £m	2010 £m As restated*
Total revenue	745.3	597.1
Cost of sales	(523.8)	(386.8)
Administrative expenses	(79.7)	(72.8)
Acquisition related costs (see Note 33)	(5.7)	(6.7)
Restructuring and incident costs	(7.2)	(4.3)
Provision release	-	2.4
Intangible amortisation arising from business combinations	(24.3)	(17.0)
Gain/(loss) on fair value movements on derivatives	2.4	(4.0)
Non-underlying items	(34.8)	(29.6)
Total operating profit	107.0	107.9

* The 2010 figures have been restated by including certain items that were identified separately within unallocated corporate costs, and other costs being moved from within underlying operating profit to non-underlying items in order to be consistent with the current year treatment of the equivalent costs

Notes to the Group Financial Statements

6. Operating profit continued

Operating profit is stated after charging/(crediting):		
	2011 £m	2010 £m
Research and development costs		
- customer-funded	38.4	20.6
- internally-funded	8.8	5.8
Amortisation		
- arising from business combinations	24.3	17.0
- development costs	2.4	2.1
- patents and licences	0.2	0.3
Depreciation		
- property, plant and equipment	16.9	11.5
- leased assets	0.3	0.1
Loss on disposal of property, plant and equipment	0.5	0.2
Operating lease rentals		
- plant and machinery	1.5	1.2
- other	1.0	0.7
Government grant	(0.1)	(0.1)
Foreign exchange losses	0.3	2.0
Staff costs (see Note 7)	179.3	133.0
Cost of inventories recognised as an expense	341.7	254.7
Acquisition related costs	5.7	6.7
Restructuring and incident costs (£0.9 million relates to write down of property, plant and equipment)	7.2	4.3
Provision release	-	(2.4)
Auditors' remuneration (see below)	1.3	1.4
A more detailed analysis of auditors' remuneration on a worldwide basis is provided below:		
Auditors' remuneration:	2011 £m	2010 £m
Fees payable to the Company's auditor and its associates for:		
The audit of the Company's annual accounts	0.4	0.4
The audit of the Company's subsidiaries, pursuant to legislation	0.4	0.3
	0.8	0.7
Other services:		
Tax services - compliance	0.1	0.1
Tax services - advisory	0.2	0.3
Corporate finance services	0.2	0.3
	0.5	0.7
	1.3	1.4

Included in the Group audit fees is £0.1 million (2010: £0.1 million) paid in respect of the parent company.

A description of the work of the Audit Committee is set out in the Statement on Corporate Governance on pages 49 and 50 and includes an explanation of how auditor objectivity and independence is safeguarded when non-audit services are provided by the auditors. No services were provided pursuant to contingent fee arrangements.

During the year the Group incurred professional fees with other accountancy firms for the provision of corporate finance services of £0.4 million (2010: £0.4 million).

7. Staff costs

The average monthly number of employees within each category (including executive directors) was:		
	2011 Number	2010 Number
Production	3,445	2,842
Administration, sales and marketing	847	662
	4,292	3,504

At the year end the number of employees was 4,679 (2010: 4,283).

The costs incurred in respect of these employees (including share-based payments) were:		
	2011 £m	2010 £m
Wages and salaries	150.9	113.0
Social security costs	20.6	15.3
Other pension costs	7.8	4.7
	179.3	133.0

The increase in wages and salaries expense since 2010 exceeded the increase in average staff numbers due to the acquisition of Roke Manor Research Limited at the end of the prior year and Chemring Detection Systems, Inc. during the current year. Both companies have higher than average staff costs compared to the Group as a whole, increasing average wages and salaries accordingly.

8. Finance income

	2011 £m	2010 £m
Bank interest	0.1	0.5

9. Finance expense

	2011 £m	2010 £m
Bank overdraft and loan interest	2.2	0.3
Loan notes interest	15.5	15.5
Medium term loan interest	0.5	2.8
Finance lease interest	0.4	0.3
Amortisation of debt finance costs	1.5	1.2
Unwinding of discount on provisions (see Note 26)	0.3	0.3
Interest cost of retirement benefit obligations (see Note 34)	0.7	1.2
Amounts included in the cost of qualifying assets	(4.7)	(2.2)
	16.4	19.4

Borrowing costs included in the cost of qualifying assets during the year are calculated by applying a capitalisation rate of 6% (2010: 7%) to expenditure on such assets.

10. Tax

	2011 £m	2010 £m
Current tax charge	(14.0)	(19.5)
Deferred tax charge (see Note 27)	(2.9)	(2.9)
Total current year tax charge	(16.9)	(22.4)

Income tax in the UK is calculated at 26.83% (2010: 28.00%) of the estimated assessable profit for the year. Tax for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions.

The total charge for the year can be reconciled to the Income Statement as follows:		
	2011 £m	2010 £m
Profit before tax for the year	90.8	89.1
Tax at the UK corporation tax rate of 26.83% (2010: 28.00%)	(24.4)	(24.9)
Income not chargeable for tax purposes	1.0	2.2
Changes in tax rates	2.1	1.3
Research and development tax relief	1.2	-
Utilisation and recognition of tax losses	5.1	0.8
Overseas profits taxed at rates different to the standard rate	(1.9)	(1.8)
Total current year tax charge	(16.9)	(22.4)

Notes to the Group Financial Statements

10. Tax continued

In addition to the income tax expense charged to the Income Statement, a tax credit of £1.4 million (2010: tax debit of £2.0 million) has been recognised in equity in the year.

The effective rate of tax incurred by the Group is 18.6% (2010: 25.1%), and the underlying* effective rate of tax incurred by the Group is 22.9% (2010: 25.9%#). This reduction is principally due to additional research and development tax credits following the acquisition of Roke Manor Research Limited and utilisation of tax losses not previously recognised.

* Before acquisition related costs, restructuring and incident costs, provision release, intangible amortisation arising from business combinations and gain/(loss) on fair value movements on derivatives
The 2010 figure has been restated due to certain costs being moved from within underlying operating profit to non-underlying items in order to be consistent with the current year treatment of the equivalent costs (see Note 6)

11. Dividends

	2011 £m	2010 £m
Dividends on ordinary shares of 1p each*		
Final dividend for the year ended 31 October 2010 8.4p (2009: 7.2p)	14.9	12.7
Interim dividend for the year ended 31 October 2011 4.0p (2010: 3.4p)	7.8	6.0
Total dividends	22.7	18.7

* Restated figures for prior year to reflect the subdivision of each 5p ordinary share into five 1p ordinary shares on 28 March 2011

The proposed final dividend in respect of the year ended 31 October 2011 of 10.8p per share will, if approved, absorb approximately £20.9 million of shareholders’ funds. The dividend is subject to approval by shareholders at the Annual General Meeting and accordingly has not been included as a liability in these financial statements.

12. Earnings per share

On 28 March 2011, the 5p ordinary shares in the Company were subdivided into five 1p ordinary shares. All figures relating to share numbers (including shares in issue, dividends per share and earnings per share) prior to 28 March 2011 have been restated as though the share split had already occurred. This has been done to provide comparable information for the current financial year. (See Note 13 for further detail on the share split).

Earnings per share are based on the average number of shares in issue of 185,633,996 (2010: 176,602,225) and profit on ordinary activities after tax of £73.9 million (2010: £66.7 million). Diluted earnings per share has been calculated using a diluted average number of shares in issue of 187,636,114 (2010: 178,388,435) and profit on ordinary activities after tax of £73.9 million (2010: £66.7 million).

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

	2011			2010		
	Earnings £m	Ordinary shares Number 000s	EPS Pence	Earnings £m	Ordinary shares Number 000s	EPS Pence
Basic	73.9	185,634	39.8	66.7	176,602	37.8
Additional shares issuable other than at fair value in respect of options outstanding	-	2,002	(0.4)	-	1,786	(0.4)
Diluted	73.9	187,636	39.4	66.7	178,388	37.4

The number of shares in issue differs from the number held by third parties due to the fact that the Company holds its own shares in treasury. Further information on the treasury shares holding is given in Note 30.

Reconciliation from basic earnings per share to underlying earnings per share:

Underlying basic earnings are defined as earnings before acquisition related costs, restructuring and incident costs, provision release, intangible amortisation arising from business combinations and gain/(loss) on fair value movements on derivatives. The directors consider this measure of earnings allows a more meaningful comparison of earnings trends.

	2011			2010		
	Earnings £m	Ordinary shares Number 000s	EPS Pence	Earnings £m As restated*	Ordinary shares Number 000s	EPS Pence
Basic	73.9	185,634	39.8	66.7	176,602	37.8
Non-underlying items#	22.9	-	12.3	21.3	-	12.0
Underlying	96.8	185,634	52.1	88.0	176,602	49.8

* Restated 2010 underlying earnings due to reclassification of certain items from underlying costs to non-underlying costs in order to conform with the current year treatment of the corresponding items
Acquisition related costs, restructuring and incident costs, provision release, intangible amortisation arising from business combinations and gain/(loss) on fair value movements on derivatives (after tax)

The reclassification of certain items from underlying to non-underlying in 2010 has resulted in a revised 2010 figure for underlying earnings per share. A reconciliation of the movement from the reported figure in the 2010 financial statements to the figure above is shown below.

	Earnings £m	Ordinary shares Number 000s	2010 EPS Pence
Underlying earnings per share as previously reported	86.9	176,602	49.2
Reclassification of items from underlying to non-underlying (including tax)	1.1	-	0.6
Revised underlying earnings per share	88.0	176,602	49.8

13. Share split and placing

At the Company’s Annual General Meeting on 24 March 2011 a resolution was passed to split the Company’s ordinary shares of 5p each (the “Existing Ordinary Shares”) in issue or held in treasury into ordinary shares of 1p each (the “Ordinary Shares”), resulting in shareholders holding five Ordinary Shares for each Existing Ordinary Share they held prior to the share split. This share split took effect on 28 March 2011.

On 20 April 2011, the Group placed 17,405,183 new ordinary shares at 645p per share, raising £112.4 million before costs. This represented an increase of £0.2 million in the ordinary share capital and £110.2 million in the share premium reserve after costs. The placing represented in the region of 9.8% of the Group’s market capitalisation and it was anticipated that the proceeds would be used fund possible future acquisition opportunities. Approximately £56 million of the placing proceeds were used to fund the acquisition of Chemring Detection Systems. The Board did not pursue any further acquisition opportunities during the year and the funds remain within the Group’s Balance Sheet.

14. Goodwill

	£m
Cost	
At 1 November 2009	149.5
Recognised on acquisition of subsidiary undertakings as restated (see below)	79.5
Foreign exchange adjustments	2.0
At 31 October 2010	231.0
At 1 November 2010	231.0
Recognised on acquisition of subsidiary undertakings*	13.5
Foreign exchange adjustments	(1.1)
At 31 October 2011	243.4
Accumulated impairment losses	
At 1 November 2009, 1 November 2010 and 31 October 2011	-
Carrying amount	
At 31 October 2011	243.4
At 31 October 2010	231.0
Additions to goodwill since 1 November 2009 can be split as follows:	
	£m
Hi-Shear Technology Corporation	47.3
Roke Manor Research Limited, as restated*	28.3
Other acquisitions as restated*	3.9
At 31 October 2010	79.5
Chemring Detection Systems, Inc.	13.5
At 31 October 2011	13.5

Notes to the Group Financial Statements

14. Goodwill continued

Goodwill acquired in a business combination is allocated at acquisition to the cash generating units (“CGU”) that are expected to benefit from that business combination. The carrying amount of the goodwill has been allocated to our principal CGUs. An analysis of the pre-tax discount rates used and the goodwill (after foreign exchange) as at 31 October 2011 by principal CGU is shown below:

	2011 %	2010 %	2011 £m	2010 £m
Hi-Shear Technology Corporation	11.6	7.4	48.9	49.2
Simmel Difesa S.p.A.**	13.7	7.4	48.2	48.5
Chemring Energetic Devices, Inc.	11.6	7.4	28.6	28.7
Roke Manor Research Limited, as restated*	2.9	7.4	28.3	28.3
Chemring Energetics UK Limited	11.7	7.4	18.1	18.1
Non-Intrusive Inspection Technology, Inc.	11.6	7.4	15.4	15.5
Chemring Detection Systems, Inc.*	11.6	-	13.4	-
Other			42.5	42.7
Total goodwill			243.4	231.0

* See Note 33
** Includes £2.9 million goodwill from the acquisition of Chemring Fuze Technology S.r.l. in 2010

The pre-tax discount rate for Roke Manor Research Limited is significantly lower compared to the other CGUs due to the research and development tax credits it receives, which result in post-tax cashflows exceeding pre-tax cashflows.

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

The recoverable amounts of the CGU are determined from value-in-use calculations. The key assumptions for the value-in-use calculations are those regarding the discount rates, the growth rates and expected changes to selling prices and direct costs during the period for which management have detailed plans. Management estimates discount rates using pre-tax rates that reflect current market assessments of the time value of money and the risks specific to the CGU.

Pre-tax discount rates, derived from the Group’s weighted average cost of capital of 9.4% (2010 7.0%), and adjusted for a premium specific to each CGU to account for differences in currency risk, country risk and other factors affecting specific CGUs, have been used to discount projected cash flows.

The calculation has used the Group’s forecast figures for the next five years. At the end of five years, it assumes the performance of the Group companies will grow at a nominal annual rate of 0.5% in perpetuity thereafter. The growth rates are based on management’s view of industry growth forecasts. Having considered the budget cuts in the US and UK, management are still forecasting growth similar to historic rates. Changes in selling prices and direct costs are based on past practices and expectations of future changes in the market. The Group prepares cash flow forecasts derived from the most recent financial budgets approved by management for the next five years and extrapolates cash flows after that period based on growth as described above.

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

There was significant headroom within all the value-in-use calculations. Additionally, stress testing has indicated that no reasonably possible change in the key assumptions used would result in a significant impairment charge being recorded in the financial statements. A 20% fall in the forecast cashflows of all the CGUs was modelled and no impairment was required for any CGU in this scenario.

15. Other intangible assets

	Development costs £m	Acquired orderbook £m	Acquired technology £m	Acquired customer relationships £m	Patents and licences £m	Total £m
Cost						
At 1 November 2009	11.9	22.4	16.8	66.9	1.8	107.9
Additions	7.5	-	-	-	0.3	0.3
Disposals	(0.6)	-	-	-	(0.2)	(0.2)
Recognised on acquisition of subsidiary undertakings*	0.1	30.8	21.3	59.1	0.2	111.4
Foreign exchange adjustments	-	2.7	(0.1)	2.2	-	4.8
At 1 November 2010*	18.9	55.9	38.0	128.2	2.1	224.2
Additions	12.4	-	-	-	0.5	0.5
Disposals	(1.0)	-	-	-	(0.6)	(0.6)
Transfer between categories	-	6.8	(4.1)	(2.7)	-	-
Recognised on acquisition of subsidiary undertakings*	-	0.5	27.8	6.8	-	35.1
Foreign exchange adjustments	(0.1)	(0.4)	(0.4)	(0.8)	-	(1.6)
At 31 October 2011	30.2	62.8	61.3	131.5	2.0	257.6
Amortisation						
At 1 November 2009	4.0	12.0	3.3	8.9	1.2	25.4
Charge for the year	2.1	7.7	2.4	6.9	0.3	17.3
Disposals	(0.5)	-	-	-	(0.1)	(0.1)
Foreign exchange adjustments	-	1.0	(0.7)	(0.7)	-	(0.4)
At 1 November 2010	5.6	20.7	5.0	15.1	1.4	42.2
Charge for the year	2.4	11.3	2.3	10.7	0.2	24.5
Disposals	(1.0)	-	-	-	(0.6)	(0.6)
Transfer between categories	-	2.5	(0.5)	(2.0)	-	-
Foreign exchange adjustments	(0.1)	(1.1)	1.1	(0.3)	-	(0.3)
At 31 October 2011	6.9	33.4	7.9	23.5	1.0	65.8
Carrying amount						
At 31 October 2011	23.3	29.4	53.4	108.0	1.0	191.8
At 31 October 2010*	13.3	35.2	33.0	113.1	0.7	182.0

Acquired intangible assets are recognised at fair value on acquisition and are amortised over their estimated useful lives. Fair values for acquired intangible assets are assessed by reference to future estimated cash flows discounted at an appropriate rate to present value, or by reference to the amount that would have been paid in an arm’s length transaction between two knowledgeable and willing parties. Other intangible assets are recognised at cost and are amortised over their estimated useful lives (see Note 3).

* See Note 33

Notes to the Group Financial Statements

16. Property, plant and equipment

	Land and buildings £m	Plant and equipment £m	Total £m
Cost or valuation			
At 1 November 2009	69.1	124.3	193.4
Additions	14.4	26.5	40.9
Acquired on acquisition of subsidiary undertakings*	22.3	8.5	30.8
Disposals	-	(6.2)	(6.2)
Foreign exchange adjustments	1.0	3.4	4.4
At 1 November 2010*	106.8	156.5	263.3
Additions	11.1	37.5	48.6
Acquired on acquisition of subsidiary undertakings	0.6	2.9	3.5
Disposals	(0.6)	(10.1)	(10.7)
Foreign exchange adjustments	0.5	(0.4)	0.1
At 31 October 2011	118.4	186.4	304.8
Accumulated depreciation			
At 1 November 2009	10.6	47.8	58.4
Charge for the year	0.5	11.1	11.6
Disposals	-	(6.1)	(6.1)
Foreign exchange adjustments	(0.6)	2.5	1.9
At 1 November 2010	10.5	55.3	65.8
Charge for the year	3.2	14.0	17.2
Disposals	(0.4)	(8.5)	(8.9)
Foreign exchange adjustments	-	(0.4)	(0.4)
At 31 October 2011	13.3	60.4	73.7
Carrying amount			
At 31 October 2011	105.1	126.0	231.1
At 31 October 2010*	96.3	101.2	197.5
The carrying amount of the Group's plant and equipment includes an amount of £6.1 million (2010: £5.4 million) in respect of assets held under finance leases. £4.7 million (2010: £2.2 million) of interest has been capitalised (see Note 9) in the year, bringing the cumulative cost to £7.3 million (2010: £2.6 million) since 1 November 2008. In the year £0.5 million (2010: £0.3 million) has been charged as depreciation on completion of the relevant projects. This results in a net book value for capitalised interest of £6.5 million (2010: £2.3 million).			
Land and buildings were revalued at 30 September 1997 by Chestertons Chartered Surveyors, independent valuers not connected with the Group, on the basis of depreciated replacement cost for two pyrotechnic sites, and on open market for the remainder.			
		2011 £m	2010 £m As restated*
30 September 1997 depreciated replacement cost		5.8	5.8
Freehold at cost		112.6	101.0
		118.4	106.8

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

	2011 £m	2010 £m As restated*
Cost	116.4	104.8
Accumulated depreciation	(12.7)	(9.9)
Historical cost value	103.7	94.9

* See Note 33

All other tangible fixed assets are stated at historical cost.

The total amount of additions during 2011, shown above, is different to the figure shown in the Consolidated Cash Flow Statement due to timing of payments.

At 31 October 2011 the Group had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £14.6 million (2010: £18.8 million). Included within this figure were commitments totalling £10.5 million to be spent on conducting two major investment programmes for new countermeasures facilities at Salisbury, UK and Lara, Australia.

17. Subsidiary undertakings

All subsidiary undertakings have been included in the consolidation. The undertakings held at 31 October 2011 which, in the opinion of the directors, principally affected the results for the year or the net assets of the Group are shown below.

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

Notes to the Group Financial Statements

18. Interest in associate

	2011 £m	2010 £m
Interest in associate (including goodwill of £0.5 million (2010: £0.5 million))	1.5	1.1
Amounts relating to associate:		
	2011 £m	2010 £m
Total assets	2.7	1.6
Total liabilities	(0.7)	(0.4)
Net assets	2.0	1.2
Group's share of net assets (excluding goodwill)	1.0	0.6

The results of the associated undertaking for the year ended 30 September 2011 relate to the Group's share of CIRRA S.A. CIRRA S.A.'s financial year ended on 30 September 2011 and there is no material difference between the results as reported and those that would be obtained were CIRRA S.A. to have a year ending on 31 October 2011.

	2011 £m	2010 £m
Total revenue	1.9	1.9
Profit after tax	0.2	0.2
Group's share of profit of associate	0.1	0.1

19. Inventories

	2011 £m	2010 £m
Raw materials	49.1	53.1
Work in progress (2010 figure restated – see Note 33)	70.8	67.4
Finished goods	26.9	20.8
	146.8	141.3

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

20. Trade and other receivables

	2011 £m	2010 £m
Current		
Trade receivables	165.5	141.1
Allowance for doubtful debts	(1.4)	(2.0)
	164.1	139.1
Other debtors (2010 figure restated – see Note 33)	13.4	14.1
Prepayments and accrued income	13.3	12.4
	190.8	165.6

All amounts shown above are due within one year.

The average credit period taken on sales of goods, based on a countback basis, is 45 days (2010: 47 days). No interest is charged on the receivables from the date of invoice to payment.

The Group's policy is to provide in full for debtors greater than 120 days beyond agreed terms, unless extenuating circumstances exist. Due to the nature of the customer base the Group does not experience significant bad debt write-offs and hence no movement schedule for the allowance for doubtful debts has been provided due to its immaterial level in 2011 and 2010. The increase in the year of trade receivables is in part due to the acquisition of Chemring Detection Systems, Inc. during the year, adding £3.0 million to the trade receivables balance. It was also partly due to the timing of invoicing and cash receipts at the end of the current financial year. An ageing analysis has not been shown as all significant overdue receivables are covered by the allowance for doubtful debts provision above. The vast majority of the trade debtor balance is not yet due based on the average credit terms provided to customers.

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

21. Cash and cash equivalents

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

Included within cash is £0.4 million of restricted cash (2010: £31.2 million), of which £nil (2010: £15.0 million) is held in escrow in relation to the Chemring Group Staff Pension Scheme (see Note 34) and £nil (2010: £13.1 million) is held as security against performance related bonds at Mecar S.A..

22. Borrowings

	2011 £m	2010 £m
Bank loans and overdrafts		
- sterling denominated	35.6	59.2
- euro denominated	45.9	2.9
Other loans due in less than one year	4.5	3.5
Borrowings due within one year	86.0	65.6
UK medium term bank loans		
- sterling denominated	1.0	1.1
- euro denominated	-	28.0
- other denominated	-	2.2
Overseas medium term bank loans		
- US dollar denominated	0.2	0.3
Other loans		
- euro denominated	0.7	1.8
Loan notes		
- sterling denominated	12.5	12.5
- US dollar denominated	247.7	248.7
Borrowings due after more than one year	262.1	294.6
Finance leases	6.4	5.6
Preference shares	0.1	0.1
	354.6	365.9

	2011 £m	2010 £m
Analysis of total borrowings by currency:		
Sterling	54.7	48.6
US dollar	248.8	255.6
Euro	51.1	58.0
Other	-	3.7
Total	354.6	365.9

	2011 %	2010 %
The weighted average interest rates paid were as follows:		
Bank overdrafts	4.6	4.9
UK medium term bank loans		
- sterling denominated	4.6	4.9
- euro denominated	5.0	5.0
- other denominated	5.5	5.5
Overseas medium term bank loans		
- US dollar denominated	4.2	4.2
Other loans		
- euro denominated	5.0	5.0
Loan notes		
- sterling denominated	6.8	6.8
- US dollar denominated	5.3 – 6.3	5.3 – 6.3

Notes to the Group Financial Statements

22. Borrowings continued

	Bank loans and overdrafts £m	Loan notes £m	Other loans* £m	2011 Total £m	Bank loans and overdrafts £m	Loan notes £m	Other loans* £m	2010 Total £m
Borrowings falling due within:								
One year	81.5	-	6.5	88.0	62.1	-	6.1	68.2
Borrowings falling due within:								
One to two years	0.5	-	2.6	3.1	30.5	-	4.8	35.3
Two to five years	0.7	-	2.5	3.2	1.1	-	-	1.1
After five years	-	260.2	0.1	260.3	-	261.2	0.1	261.3
	1.2	260.2	5.2	266.6	31.6	261.2	4.9	297.7
Total borrowings	82.7	260.2	11.7	354.6	93.7	261.2	11.0	365.9

* Includes finance leases and preference shares

In January 2011, the Group completed a refinancing of its bank facilities with a syndicate of five banks. The new Group facilities, which are unsecured, total £230 million. In addition, the term of the facilities was extended from April 2012 to April 2015. This revolving credit facility provides access to committed lending and bonding line support.

Other loans represent loans held by certain Group companies to fund working capital.

The directors do not believe the fair value of the Group's borrowings to be materially different to the book values.

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

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

	2011 £m	2010 £m
Undrawn borrowings		
Cash and gross facilities	292.1	219.3
Drawn facilities	(142.0)	(114.7)
Total undrawn borrowings	150.1	104.6

The Group is subject to two key financial covenants which are tested quarterly, relating to the ratio between earnings before interest, tax, depreciation and amortisation (EBITDA) and net debt ('debt ratio'), as well as the ratio between EBITDA and finance costs ('interest cover'). The Group comfortably complied with these covenants throughout the year and the position at the year end is detailed below:

	2011 £m	2010 £m
Debt ratio		
Maximum allowed ratio of net debt to EBITDA	3.0	3.0
Actual ratio of net debt to EBITDA	1.6	2.3
Interest cover		
Minimum allowed ratio of EBITDA to finance costs	4.0	4.0
Actual ratio of EBITDA to finance costs	10.0	8.7

23. Obligations under finance leases

	2011 £m	Minimum lease payments 2010 £m	Present value of minimum lease payments 2011 £m	2010 £m
Amounts payable under finance leases:				
Within one year	2.3	2.8	2.0	2.6
In the second to fifth years	4.7	3.3	4.4	3.0
Less future finance charges	(0.6)	(0.5)	-	-
Present value of lease obligations	6.4	5.6	6.4	5.6
Less amounts due within twelve months shown under current liabilities			(2.0)	(2.6)
Amount due for settlement after twelve months			4.4	3.0

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

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

The Group's obligations under finance leases are secured by the lessors' title to the underlying leased assets (see Note 16).

24. Trade and other payables

	2011 £m	2010 £m
Current		
Trade payables	105.3	100.1
Other payables	33.5	40.5
Other tax and Social Security	4.0	4.6
Advance payments	48.7	52.8
Accruals and deferred income (2010 figure restated - see Note 33)	20.9	24.3
	212.4	222.3
Non-current - Other creditors	1.2	1.0

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. Advance payments are amounts received from customers on larger contracts to fund working capital. The directors consider that the carrying amount of payables approximates to their fair value.

The average credit period taken on purchases of goods is 49 days (2010: 61 days). At the end of 2010 trade payables were high, in terms of days, due to excess trade payables acquired with the Mear acquisition (impact of 9 days). During the first half of 2011 these trade payables were settled. It is anticipated that working capital will reduce in 2012. No interest is charged on the payables from the date of invoice to payment.

25. Financial instruments and risk management

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

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

- Forward foreign exchange contracts and foreign exchange structures to manage the exchange risk arising from transactional foreign exchange exposures within the Group.
- Interest rate swaps to mitigate the risk of the movement in interest rates.

Foreign currency risk management

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

- Transactional risk: The Group policy is to hedge significant transactional currency exposures via the use of forward foreign exchange contracts and structures. The measurement and control of this risk is closely monitored on a Group-wide basis.
- Translation risk: The Group translates overseas results and net assets in accordance with the accounting policy in Note 3. The translation risk on net assets is mitigated by the transfer of currencies between Group companies and the appropriate use of foreign currency borrowings.

Notes to the Group Financial Statements

25. Financial instruments and risk management continued

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

	US\$	Euro	NOK	2011 AU\$	US\$	Euro	NOK	2010 AU\$
Monetary assets (million)	143.9	108.3	44.6	8.4	154.6	69.2	48.7	10.5
Monetary liabilities (million)	314.4	99.6	11.1	3.7	312.5	105.1	17.5	6.9

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

	US\$	Euro	NOK	2011 AU\$	US\$	Euro	NOK	2010 AU\$
Borrowings (million)	405.0	53.1	-	-	405.0	53.1	35.0	-

The Group uses foreign exchange contracts to hedge its currency risk, most with a maturity of less than one year from the year end. The most significant exchange rates to manage, as far as the Group is concerned, are the US dollar and Euro exchange rates.

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

	Average exchange rate 2011	2010	Expiring within one year 2011 £m	2010 £m
US dollar	1.56	1.65	48.5	84.2

At the year end, there were two US dollar structures in place which were set up to protect the Income Statement from currency fluctuations during 2012 and so provide an economic hedge. The structure involves a cap and a collar, which lock in the exchange rates to give the Group the appropriate protection against transactional flows. Hedge accounting was not adopted for this structure.

The principal amounts of the Group's Euro and US dollar bank loans and loan notes have been accounted for as net investment hedges on the European and US businesses. These hedges are effective throughout the year and the losses arising on translation have been offset against the gains on re-translation of the subsidiaries in reserves.

Foreign currency sensitivity analysis

The following table details the Group's sensitivity to a 10 cents movement in the relevant foreign currencies against sterling with regards to its monetary assets and liabilities. 10 cents represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the year end for a 10 cents change in foreign currency rates.

	+10 cents				- 10 cents			
	US dollar impact 2011 £m	2010 £m	Euro impact 2011 £m	2010 £m	US dollar impact 2011 £m	2010 £m	Euro impact 2011 £m	2010 £m
Gain/(loss)	10.1	13.4	(0.6)	2.5	(11.4)	(15.2)	0.7	(3.0)
Other equity	10.1	13.4	(0.6)	2.5	(11.4)	(15.2)	0.7	(3.0)

The potential gains or losses arising from these movements in exchange rates would partly result in foreign exchange movements in the Income Statement and partly through movements directly through reserves.

The Group's sensitivity to foreign currency decreased during the year, mainly due to the movements in working capital at the US and European subsidiaries.

Interest rate risk

The Group finances its operations through a mixture of retained profits, bank and private placement borrowings and leasing lines of credit. The UK borrowings are denominated in sterling, Euro and US dollar, and at the shorter end are subject to floating rates of interest. The Group has entered into a floating to fixed interest rate swap for the Euro borrowings at a weighted average rate of 3.84%.

The Group has outstanding fixed interest loan notes in the US, repayable in full in November 2016 (\$80 million), November 2017 (£12.5 million and \$125 million) and in November 2019 (\$200 million). This arrangement provides a natural hedge against the Group's investment structure in its US businesses.

As the Group has predominantly fixed interest rate loans, a change in interest rates would not have an immediate significant impact on the Income Statement.

Liquidity risk

The table below details the maturity profiles of the Group's derivative financial instruments and loans (excluding finance leases, preference shares and capitalised facility fees) as at 31 October:

	Derivative payables £m	Derivative receivables £m	Loans and overdrafts £m	2011 Total £m	Derivative payables £m	Derivative receivables £m	Loans and overdrafts £m	2010 Total £m
Falling due within:								
One year	48.5	(49.9)	90.1	88.7	84.2	(86.0)	65.6	63.8
One to two years	18.7	(19.5)	1.3	0.5	44.9	(45.8)	32.3	31.4
Two to five years	-	-	0.7	0.7	-	-	1.1	1.1
After five years	-	-	263.4	263.4	-	-	264.9	264.9
	67.2	(69.4)	355.5	353.3	129.1	(131.8)	363.9	361.2

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

Financial assets	2011 Total £m	2010 Total £m
Sterling	81.3	38.6
US dollar	69.7	101.2
Australian dollar	6.2	7.1
Euro	98.3	69.8
Other currencies	5.0	4.5
	260.5	221.2
Overdraft offset in the UK	(2.6)	(21.8)
Financial assets	257.9	199.4
Cash at bank and in hand	91.9	58.4
Trade receivables	164.1	139.1
Financial instruments	1.9	1.9
	257.9	199.4

Cash balances held in the UK enjoy a right of interest offset against overdraft balances. Overseas cash balances have a weighted average interest rate of 0.1% (2010: 0.5%) and are at a floating rate.

The foreign currency balances mostly sit within overseas business units and so do not result in significant exposure to transactional risks for the Group. Included within cash is £0.4 million of restricted cash (2010: £31.2 million) (see Note 21). During 2011, a standby letter of credit was put in place, substituting the need for funds held in escrow in relation to the Chemring Group Staff Pension Scheme.

Notes to the Group Financial Statements

25. Financial instruments and risk management continued

Financial liabilities	Floating rate £m	Fixed rate £m	2011 Total £m	Floating rate £m	Fixed rate £m	2010 Total £m
Sterling	(40.1)	(43.3)	(83.4)	(25.8)	(76.9)	(102.7)
US dollar	(3.7)	(287.8)	(291.5)	(1.3)	(287.4)	(288.7)
Euro	(5.2)	(87.2)	(92.4)	(0.3)	(98.1)	(98.4)
Other currencies	-	(2.3)	(2.3)	-	(7.9)	(7.9)
	(49.0)	(420.6)	(469.6)	(27.4)	(470.3)	(497.7)
Overdraft offset in the UK			2.6			21.8
Financial liabilities			(467.0)			(475.9)
Bank loans and overdrafts			(81.5)			(62.1)
UK medium term loans			(1.0)			(31.3)
Loan notes			(260.2)			(261.2)
Overseas medium term loans			(0.2)			(0.3)
Other loans			(5.2)			(5.3)
			(348.1)			(360.2)
Preference shares (see Note 28)			(0.1)			(0.1)
Obligations under finance leases			(6.4)			(5.6)
			(354.6)			(365.9)
Trade payables due within one year			(105.3)			(100.1)
Financial instruments due within one year			(1.5)			(1.6)
Trade payables due after more than one year			(1.2)			(1.0)
Financial instruments due after more than one year			(4.4)			(7.3)
			(467.0)			(475.9)

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

The weighted average interest rate of fixed rate financial liabilities at 31 October 2011 was 5.1% (2010: 5.6%) and the weighted average period of funding was five years (2010: six years).

Derivative financial instruments

The Group has one interest rate swap, from floating to fixed rate, that expires in April 2015 at a rate of 3.84%. The fair value of interest rate swaps recognised on the Balance Sheet at 31 October 2011 was a £4.2 million liability (2010: £5.7 million liability). The Group also has two forward exchange structures with a fair value of £1.7 million liability (2010: £3.2 million liability) and £1.9 million asset (2010: £1.9 million asset). The total of these financial instruments is a £4.0 million liability (2010: £7.0 million liability).

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

	2011 Total £m	2010 Total £m
Interest rate swaps	(4.2)	(5.7)
Forward exchange contracts	0.2	(1.3)
	(4.0)	(7.0)

Analysed as:

	2011 Total £m	2010 Total £m
Included in current assets	1.9	1.9
Included in current liabilities	(1.5)	(1.6)
Included in non-current liabilities	(4.4)	(7.3)
	(4.0)	(7.0)

The following table details the gain/(loss) on fair value movements on derivatives recognised in the Income Statement:

	2011 Total £m	2010 Total £m
Change in fair value of currency structures	2.4	(3.0)
Amortisation	-	(1.0)
	2.4	(4.0)

Fair value hierarchy

IFRS 7 *Financial Instruments: Disclosures* requires companies that carry financial instruments at fair value in the Balance Sheet to disclose their level of visibility, determining into which category those financial instruments fall under the fair value hierarchy.

The fair value measurement hierarchy is as follows:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 - Inputs for the asset or liability that are not based on observable market data (i.e. as unobservable inputs).

The following table presents the Group's assets and liabilities that are measured at fair value:

	Level 1 £m	Level 2 £m	2011 Total £m	Level 1 £m	Level 2 £m	2010 Total £m
Assets						
Forward exchange contracts	-	1.9	1.9	-	1.9	1.9
Total assets	-	1.9	1.9	-	1.9	1.9

	Level 1 £m	Level 2 £m	2011 Total £m	Level 1 £m	Level 2 £m	2010 Total £m
Liabilities						
Borrowings	(80.8)	(273.8)	(354.6)	(79.9)	(286.0)	(365.9)
Interest rate swaps	-	(4.2)	(4.2)	-	(5.7)	(5.7)
Forward exchange contracts	-	(1.7)	(1.7)	-	(3.2)	(3.2)
Total liabilities	(80.8)	(279.7)	(360.5)	(79.9)	(294.9)	(374.8)

There were no assets or liabilities that were classed under Level 3 on the fair value hierarchy.

Credit risk

The Group's principal financial assets are bank balances and cash, and trade and other receivables, which represent the Group's maximum exposure to credit risk in relation to financial assets. Whilst the Group does not have any significant credit risk exposure to any single counterparty, the credit risk on liquid funds and derivative financial instruments is monitored on an ongoing basis using credit ratings assigned by international credit rating agencies, the credit default swap market and market capitalisation.

The Group's credit risk is primarily attributable to its trade receivables. The amounts presented in the Balance Sheet are net of allowances for doubtful receivables, based on prior experience and an assessment of the current economic environment. Trade receivables consist of a small number of customers spread across diverse geographical areas. Customers are mainly multi-national organisations or government agencies with whom the Group has long term business relationships. The Group principally does business with government defence departments, such as the US Department of Defense and the UK Ministry of Defence, as well as US and UK defence prime contractors (such as Lockheed Martin, BAE Systems and General Dynamics).

Notes to the Group Financial Statements

25. Financial instruments and risk management continued

The counterparties are monitored on an ongoing basis for credit risk and as at the Balance Sheet date the risk was deemed to be low. Ongoing credit evaluation is performed on the financial condition of accounts receivable and, when appropriate, action is taken to minimise the credit risk to the Group.

Group accounting policy requires letters of credit to be put in place for the majority of contracts with overseas customers. Any departures from this policy require approval by the Group finance function.

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

Capital management

The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Board monitors both the demographic spread of shareholders, as well as the return on capital. From time to time the Group purchases its own shares on the market; the timing of these purchases depends on the market prices. Primarily, the shares are intended to be used for satisfying awards under the Group's share-based incentive schemes. Buy and sell decisions are made on a specific transaction basis by the Board. Following the share placing in April 2011 and the subsequent decision not to pursue further acquisition opportunities in the immediate future for which the funds had been partly intended, the Board has concluded that the Group should consider returning surplus capital to shareholders whilst maintaining the strength of the Balance Sheet, if deemed appropriate over the course of the next year.

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

26. Provisions

	Environmental provisions £m	Warranty provisions £m	Restructuring provisions £m	Total £m
At 1 November 2010	2.2	0.9	1.9	5.0
Unwinding of discount - charged to interest	0.3	-	-	0.3
Provided for in the year	0.7	0.6	-	1.3
Effect of foreign exchange movements	(0.2)	(0.2)	-	(0.4)
Paid in the year	(0.3)	(0.3)	(0.5)	(1.1)
Released in the year	-	-	(0.2)	(0.2)
At 31 October 2011	2.7	1.0	1.2	4.9
Analysed as:				
			2011 £m	2010 £m
Included in current liabilities			2.5	1.9
Included in non-current liabilities			2.4	3.1
			4.9	5.0

At the year end, a third party assessment was carried out of the provision held in respect of the environmental liabilities associated with the Chemring Energetic Devices site in Illinois, USA. The majority of the provision is expected to be utilised within the next year, with the balance due in future years.

The warranty provisions at 31 October 2011 are held by Simmel Difesa S.p.A. and represent management's best estimate of the Group's liability under six year warranties, based on past experience for defective products.

The restructuring provisions at 31 October 2011 relate to Chemring Countermeasures Limited and Chemring EOD Limited. The provisions represent management's best estimates of the costs to be incurred on the restructuring programmes during 2012.

27. Deferred tax

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

	Accelerated tax depreciation £m	Retirement benefit obligations £m	Tax losses £m	Acquired intangibles £m	Other £m	Total £m
At 1 November 2009	10.9	(7.9)	(2.1)	8.4	(4.4)	4.9
Charge/(credit) to income	2.9	0.1	0.1	(5.9)	5.7	2.9
Charge/(credit) to equity	-	1.4	-	0.9	(0.1)	2.2
Amounts arising on acquisition of subsidiary undertakings	(0.2)	-	(0.5)	28.6	(2.8)	25.1
At 1 November 2010 as restated (see Note 33)	13.6	(6.4)	(2.5)	32.0	(1.6)	35.1
Charge/(credit) to income	5.3	0.4	(6.1)	(8.2)	11.5	2.9
Credit to equity	-	(0.4)	-	(0.3)	-	(0.7)
At 31 October 2011	18.9	(6.4)	(8.6)	23.5	9.9	37.3

The Finance Act 2011, which provides for a reduction in the main rate of corporation tax from 26% to 25%, effective from 1 April 2012, was substantively enacted on 5 July 2011. The impact of the rate reduction has been reflected in the calculation of the UK deferred tax liability provided at 31 October 2011. Therefore, a credit of £2.1 million has been included within the deferred tax charge for the year.

The Government has also indicated that it intends to enact a future reduction in the main tax rate of 1% down to 24% on 1 April 2013. The future 1% main tax rate reduction is expected to have a similar impact on our financial statements as outlined above, subject to the impact of other developments in our tax position which may reduce the beneficial effect of this in our tax rate. As this reduction in the UK corporate tax rate has not been substantially enacted at the Balance Sheet date, this is considered a non-adjusting event in accordance with IAS 10 *Events After the Reporting Period* and no adjustments have been made. The impact of this and any further reduction will be taken into account at subsequent reporting dates, once the change has been substantively enacted.

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

	2011 £m	2010 £m
Deferred tax liabilities	59.0	52.4
Deferred tax assets (2010 figure restated - see Note 33)	(21.7)	(17.3)
	37.3	35.1

At the Balance Sheet date the Group had unrecognised tax losses of £53.0 million (2010: £72.6 million) potentially available for offset against future profits in certain circumstances, with the majority arising from recent acquisitions. No deferred tax asset has been recognised in respect of this amount because of the unpredictability of short term future qualifying profit streams.

28. Share capital

	2011 £m	2010 £m
Issued and fully paid		
195,476,434 (2010: 177,943,255) ordinary shares of 1p each*	2.0	1.8

At the Company's Annual General Meeting on 24 March 2011 a resolution was passed to split the Company's ordinary shares of 5p each (the "Existing Ordinary Shares") in issue or held in treasury into ordinary shares of 1p each (the "Ordinary Shares"), resulting in shareholders holding five Ordinary Shares for each Existing Ordinary Share they held prior to the share split. This share split took effect on 28 March 2011.

On 20 April 2011, the Company placed 17,405,183 new ordinary shares at an issue price of 645p per share, giving rise to £0.2 million of ordinary share capital and £110.2 million to the share premium reserve after costs (see Note 13). 127,996 ordinary shares (2010: 14,095*) were issued under the Group's savings-related share schemes during the year.

The Company's share capital also includes 62,500 7% cumulative preference shares of £1 each, which are all issued and fully paid-up, and are classified for accounting purposes within non-current liabilities. The cumulative preference shares carry an entitlement to a dividend at the rate of 7p per share per annum, payable in equal instalments on 30 April and 31 October each year. Holders of the preference shares have the right on winding-up to receive, in priority to any other classes of shares, the sum of £1 per share together with any arrears of dividends.

* Restated figures for prior year to reflect the subdivision of each 5p ordinary share into five 1p ordinary shares on 28 March 2011

Notes to the Group Financial Statements

29. Reserves

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

Included within retained earnings are £1.2 million of retained profits (2010: £1.1 million) relating to the associated undertaking and £0.1 million (2010: £0.1 million) of the Company's own shares held by the Group's ESOP trustee.

30. Own shares

	2011 £m	2010 £m
Balance at 1 November 2010	7.2	5.2
Acquired in the year	1.5	3.9
Issued in the year to satisfy employee share awards	(2.1)	(1.9)
Balance at 31 October 2011	6.6	7.2

The own shares reserve represents the cost of shares in Chemring Group PLC purchased in the market and held by the Group to satisfy awards under the Group's share-based incentive schemes (see Note 32). During the year 300,000 (2010: 634,400*) ordinary shares were acquired, and 456,855 (2010: 500,055*) ordinary shares were distributed following the vesting of awards under the Chemring Group Performance Share Plan. The total number of ordinary shares held in treasury at 31 October 2011 was 1,343,145 (2010: 1,500,000*) with an average cost of £4.89 (2010: £4.83*) per share. This represents 0.7% of the total issued and fully-paid ordinary share capital.

Since the year end, the Company has acquired an additional 1,000,000 ordinary shares, bringing the number of shares held in treasury at 23 January 2012 to 2,343,145, with an average cost of £4.50 per share.

* Restated figures for prior year to reflect the subdivision of each 5p ordinary share into five 1p ordinary shares on 28 March 2011

31. Obligations under non-cancellable operating leases

	2011 £m	2010 £m
Minimum lease payments under operating leases recognised in the Income Statement in the year	2.5	1.9

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

	2011 £m	2010 £m
Within one year	4.0	2.7
Two to five years	10.8	7.7
	14.8	10.4

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

The increase in operating lease commitments since 2010 is primarily due to the acquisition of Chemring Detection Systems, Inc..

32. Share-based payments

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

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

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

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

	Number of conditional shares awarded*	
	2011	2010
Outstanding at the beginning of the year	1,741,095	1,793,150
Awarded during the year	711,212	554,040
Vested during the year	(456,855)	(500,055)
Lapsed during the year	(202,475)	(106,040)
Outstanding at the end of the year	1,792,977	1,741,095
Subject to vesting at the end of the year	-	-

The following awards were outstanding at 31 October 2011:

Date of award	Number of ordinary shares under award*	Vesting price per share £	Date when awards will ordinarily vest
21 Jan 2009	614,920	Nil	21 Jan 2012
24 Jun 2009	30,530	Nil	24 Jun 2012
20 Jan 2010	447,365	Nil	20 Jan 2013
18 Mar 2010	25,575	Nil	18 Mar 2013
19 Jan 2011	657,095	Nil	19 Jan 2014
24 Oct 2011	17,492	Nil	24 Oct 2014

* Restated figures for prior year to reflect the subdivision of each 5p ordinary share into five 1p ordinary shares on 28 March 2011

The Group has applied a discount to the share-based payment, to reflect the anticipated achievement of the stipulated targets for each PSP award, based on the predicted figures within the Group's five year plan as well as the expected number of leavers over the life of the PSP awards.

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

- dividend growth at 2p per annum (2010: growth at 1p per annum);
- weighted average cost of capital 9.4% (2010: 7.5%).

The weighted average fair value of awards made during the year was 607p (2010: 584p).

The closing share price on the date of vesting of awards in the year was 666.6p (2010: 612p). The compensation expense recognised in respect of share options is based on their fair value at the grant date calculated using the Black-Scholes option pricing model.

The Group recognised a net charge of £0.2 million (2010: £2.3 million) in respect of share-based payment transactions during the year.

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

Options were granted during the year on 29 July 2011.

	Number of share options	2011 Weighted average exercise price Pence	Number of share options*	2010 Weighted average exercise price Pence
Outstanding at the beginning of the year	449,100	385	390,180	361
Granted during the year	182,629	508	89,605	478
Exercised during the year	(85,885)	373	(2,160)	360
Lapsed during the year	(40,680)	400	(28,525)	356
Outstanding at the end of the year	505,164	430	449,100	385
Subject to exercise at the end of the year	116,805	374	-	-

The following awards were outstanding at 31 October 2011:

Date of grant	Number of ordinary shares under option*	Exercise price per share* £	Dates between which options may be exercised
1 Aug 2008	11,395	3.736	1 Oct 2011 – 1 Apr 2012
1 Aug 2008	105,410	3.736	1 Oct 2013 – 1 Apr 2014
31 Jul 2009	80,905	3.444	1 Oct 2012 – 1 Apr 2013
31 Jul 2009	49,855	3.444	1 Oct 2014 – 1 Apr 2015
30 Jul 2010	40,485	4.784	1 Oct 2013 – 1 Apr 2014
30 Jul 2010	34,485	4.784	1 Oct 2015 – 1 Apr 2016
29 Jul 2011	120,104	5.080	1 Oct 2014 – 1 Apr 2015
29 Jul 2011	62,525	5.080	1 Oct 2016 – 1 Apr 2017

* Restated figures for prior year to reflect the subdivision of each 5p ordinary share into five 1p ordinary shares on 28 March 2011

The weighted average fair value of options granted in the year was 42p (2010: 99p).

The weighted average fair value of options exercised in the year was 85p (2010: 74p).

The weighted average share price on exercise of the options during the year was 610p (2010: 616p).

The fair values of the share options in the UK Sharesave Plan are based on the difference between the exercise price and the share price on the grant date of the option.

Notes to the Group Financial Statements

32. Share-based payments continued

The Chemring Group 2008 US Stock Purchase Plan (the “US Stock Purchase Plan”)

Options were granted during the year on 29 July 2011. This plan provides US employees with the opportunity to share in the future success of the Group and mirrors the UK Sharesave Plan subject to certain legal and tax differences due to the differing jurisdictions.

	Number of share options	2011 Weighted average exercise price Pence	Number of share options*	2010 Weighted average exercise price Pence
Outstanding at the beginning of the year	114,355	423	84,230	353
Granted during the year	40,635	481	56,135	499
Exercised during the year	(42,111)	348	(11,935)	370
Lapsed during the year	(20,089)	385	(14,075)	348
Outstanding at the end of the year	92,790	491	114,355	423
Subject to exercise at the end of the year	-	-	9,625	370

The following options were outstanding at 31 October 2011:

Date of grant	Number of ordinary shares under option*	Exercise price per share* £	Dates between which options may be exercised
30 Jul 2010	52,155	4.988	30 Jul 2012 – 29 Oct 2012
29 Jul 2011	40,635	4.810	29 Jul 2013 – 28 Oct 2013

* Restated figures for prior year to reflect the subdivision of each 5p ordinary share into five 1p ordinary shares on 28 March 2011

The weighted average fair value of options granted in the year was 69p (2010: 79p).

The weighted average fair value of options exercised in the year was 80p (2010: 40p).

The weighted average share price on exercise of the options during the year was 610p (2010: 616p).

The fair values of the share options in the US Stock Purchase Plan are based on the difference between the exercise price and the share price on the date of grant of the option.

33. Acquisitions

The following acquisition was completed during the year ended 31 October 2011:

Name of business acquired	Activity	Date of acquisition	Proportion of shares acquired %	Acquisition consideration £m
Chemring Detection Systems, Inc. – business and assets	Counter-IED	1 July 2011	N/A	56.1
Cash paid for acquisitions in the year				56.1
Net overdraft assumed with acquisitions				1.9
Cash outflow from investing activities				58.0
Acquisition related costs included within cash generated from operations				2.5
Net cash outflow relating to Chemring Detection Systems, Inc.				60.5
Acquisition related costs for acquisitions made in previous years				4.1
Net cash outflow relating to acquisitions				64.6

The net assets acquired are shown below:

	Book value £m	Provisional fair value adjustments £m	Provisional fair value £m
Intangible assets	4.8	30.3	35.1
Property, plant and equipment	4.2	(0.7)	3.5
Overdraft assumed	(1.9)	-	(1.9)
Working capital	8.0	(2.1)	5.9
Net assets acquired	15.1	27.5	42.6
Goodwill			13.5
Total			56.1
Total cash consideration			56.1

The acquisition was originally estimated to cost approximately £55 million, based on the exchange rate prevailing at the date of announcement of the acquisition in April 2011. The final cost of £56.1 million was due to the US dollar strengthening between the date on which the deal was announced and the completion date.

The acquisition during the year was completed in order to enhance the Group’s existing Counter-IED detection capabilities and the prospect of substantial opportunities for growth within Chemring Detection Systems’ chemical and biological detection programmes. Further information can be found in the Review by the Chief Executive.

The acquisition price was based on a cash-free/debt-free basis, however, at completion an overdraft was assumed. In compensation, trade receivables of the same amount were transferred with the business.

For the above acquisition the initial measurement period was incomplete as at the Balance Sheet date and so the fair values stated are all provisional. If there are changes to the provisional value next year the 2011 Balance Sheet will be restated. In the current year there were measurement adjustments to the acquired balance sheets of Roke Manor Research Limited, Mecar and Chemring Fuze Technology S.r.l..

	Roke Manor Research Limited £m	Mecar £m	Chemring Fuze Technology S.r.l. £m	Total £m
Intangible non-current assets	(0.1)	-	-	(0.1)
Property, plant and equipment	-	8.8	-	8.8
Deferred tax	-	0.7	-	0.7
Working capital	(0.7)	(3.2)	(0.1)	(4.0)
(Decrease)/increase to net assets	(0.8)	6.3	(0.1)	5.4
Goodwill as at 31 October 2010	27.5	7.4	2.8	37.7
Increase/(decrease) to goodwill	0.8	(6.3)	0.1	(5.4)
Goodwill as at 31 October 2011	28.3	1.1	2.9	32.3

There was a decrease in the fair value of acquired inventory at Roke Manor Research Limited of £1.0 million, and a decrease in the fair value of acquired current tax liabilities of £0.3 million, resulting in a net reduction to the fair value of working capital of £0.7 million. There was also a decrease in development costs of £0.1 million, resulting in a revised goodwill figure of £28.3 million.

At Mecar the fair value of other receivables decreased by £0.7 million and accruals increased by £2.5 million, resulting in a £3.2 million reduction in the fair value of working capital. There was an increase in the deferred tax asset of £0.7 million and a revaluation of property, plant and equipment that increased the fair value by £8.8 million. This revaluation of the property, plant and equipment was undertaken by an independent valuer. The net effect reduced goodwill by £6.3 million down to £1.1 million.

An additional £0.1 million of accruals were identified in relation to Chemring Fuze Technology S.r.l., resulting in revised goodwill of £2.9 million.

Notes to the Group Financial Statements

33. Acquisitions continued

The Balance Sheet as at 31 October 2010 has been restated to reflect the above changes.

	Original 2010 balance £m	Fair value adjustment £m	Restated 2010 balance £m
Goodwill	236.4	(5.4)	231.0
Development costs	13.4	(0.1)	13.3
Land and buildings	87.5	8.8	96.3
Deferred tax asset	16.6	0.7	17.3
Work in progress	68.4	(1.0)	67.4
Other debtors	14.8	(0.7)	14.1
Current tax liabilities	(8.0)	0.3	(7.7)
Accruals and deferred income	(21.7)	(2.6)	(24.3)

Adjustments from book value to provisional fair value arise principally from the application of Group accounting policies on working capital and the recognition of intangible assets under IFRS 3 *Business Combinations and Fair Value Adjustments to Inventories, Receivables, Property, Plant and Equipment*. Intangible assets relate principally to customer relationships and technology.

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

The acquisition during the year contributed £14.6 million of revenue and £0.9 million to the Group’s profit before interest and tax for the period between the date of acquisition and the Balance Sheet date.

If the acquisition had been completed on the first day of the financial year, Group revenue for the year would have been approximately £775.6 million, underlying profits before tax for the year would have been approximately £130.3 million, and statutory profits before tax for the year would have been approximately £92.8 million. This information is not necessarily indicative of the results of operations that would have occurred had the operations been acquired at the start of the year, nor of the future results of the combined operations.

Acquisition related costs

A total of £5.7 million (2010: £6.7 million) of costs relating to the acquisition above, as well as acquisitions completed in previous years, have been recognised in the Income Statement as non-underlying items.

	2011 £m	2010 £m
Hi-Shear Technology Corporation	-	2.0
Mecar S.A.	0.2	3.4
Roke Manor Research Limited	0.2	0.9
Chemring Detection Systems, Inc.	2.5	-
Aborted acquisition	0.9	-
Joint ventures and other acquisition related costs	1.9	0.4
Total acquisition related costs	5.7	6.7

This figure differs from the cash flow figure arising from acquisition related costs of £6.6 million due to £0.9 million of final payments associated with the acquisition of Non-Intrusive Inspection Technology, Inc., as required under the original purchase agreement.

34. Pensions

Within the UK, the Group operates a defined benefit scheme (the “Chemring Group Staff Pension Scheme”). In Germany, Chemring Defence Germany GmbH operates a defined benefit scheme (the “Chemring Defence Germany Scheme”) and in Norway, Chemring Nobel AS operates a defined benefit scheme (the “Chemring Nobel Scheme”). The other UK and overseas arrangements are all defined contribution schemes with a combined cost of £6.6 million (2010: £5.3 million).

The Chemring Group Staff Pension Scheme is a funded scheme and the assets of the scheme are held in a separate trustee administered fund. A full actuarial valuation for the Chemring Group Staff Pension Scheme as at 6 April 2009 has been prepared and updated to 31 October 2011 by a qualified actuary, using the projected unit credit method. The main assumptions for the scheme are detailed below.

Under the funding plan agreed with the trustees following the 2009 actuarial valuation, the Company agreed to eliminate the deficit calculated at that time over a period of 9.75 years. The Company and the trustees monitor funding levels annually, and a new funding plan is agreed with the trustees every three years, based on actuarial valuations. The next triennial valuation is due to be completed as at 6 April 2012. The Group considers that the current contribution rates agreed with the trustees are sufficient to eliminate the calculated deficit over the agreed period.

The Group has provided letters of credit and bank guarantees to the Chemring Group Staff Pension Scheme totalling £27.2 million (2010: £7.2 million). The letters of credit and guarantees may be drawn upon in certain events of default by the Company. The letters of credit totalling £20 million were provided in order to facilitate the release of £15 million of restricted cash pledged by the Company to the scheme, and the additional £5 million was in line with the agreed funding plan.

The Group is currently consulting with active members of the Chemring Group Staff Pension Scheme on the proposed closure of the scheme to future accrual.

The Chemring Defence Germany Scheme is an unfunded scheme. The actuarial liability has been calculated at 31 October 2011 by a qualified actuary using the projected unit credit method. The main assumptions used were a discount rate of 5.3%, inflation rate of 1.8% and rate of increase in deferred pensions of nil%. The net deficit of the Chemring Defence Germany Scheme was £1.3 million at 31 October 2011 (2010: £1.3 million).

The Chemring Nobel Scheme is an unfunded scheme. The actuarial liability has been calculated at 31 October 2011 by a qualified actuary using the projected unit credit method. The main assumptions used were a discount rate of 3.3%, inflation rate of 2.5% and rate of increase in deferred pensions of 0.7%. The net deficit of the Chemring Nobel Scheme was £0.2 million at 31 October 2011 (2010: £0.8 million).

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

	2011 £m	2010 £m	2009 £m
Present value of funded and unfunded obligations	(65.2)	(61.9)	(63.0)
Fair value of scheme assets	40.0	38.9	34.9
Net liability recognised in the Balance Sheet	(25.2)	(23.0)	(28.1)

An analysis of the net liabilities recognised is as follows:

	2011 £m	2010 £m	Change £m
Chemring Group Staff Pension Scheme	(23.7)	(20.9)	(2.8)
Chemring Defence Germany Pension Scheme	(1.3)	(1.3)	-
Chemring Nobel AS Pension Scheme	(0.2)	(0.8)	0.6
Net liability recognised in the Balance Sheet	(25.2)	(23.0)	(2.2)

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

	2011 £m	2010 £m
Amounts included within operating profit:		
Current service (cost)/credit	(1.2)	0.6
Amounts included as other finance costs:		
Expected return on scheme assets	2.5	2.3
Discount on scheme liabilities	(3.2)	(3.5)
	(0.7)	(1.2)
Net charge	(1.9)	(0.6)

Amounts recognised in the Statement of Comprehensive Income are as follows:

	2011 £m	2010 £m
Actual return less expected return on pension scheme assets ⁽ⁱ⁾	(1.3)	1.4
Changes in assumptions underlying the present value of the scheme liabilities ⁽ⁱⁱ⁾	(0.5)	2.6
Actuarial (loss)/gain recognised in the Statement of Comprehensive Income	(1.8)	4.0

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

Notes to the Group Financial Statements

34. Pensions continued

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

	2011 £m	2010 £m
Opening defined benefit obligations	(61.9)	(63.0)
Service credit	(1.2)	0.6
Interest cost	(3.2)	(3.5)
Contributions from scheme members	(0.6)	(0.6)
Actuarial (losses)/gains	(0.5)	2.6
Benefits paid	2.2	2.0
Closing defined benefit obligations	(65.2)	(61.9)

Movements in the fair value of the schemes' assets were as follows:

	2011 £m	2010 £m
Opening fair value of schemes' assets	38.9	34.9
Expected return on scheme assets	2.5	2.3
Actuarial (losses)/gains	(1.3)	1.4
Contributions from scheme members	0.6	0.6
Contributions from sponsoring companies	1.5	1.7
Benefits paid	(2.2)	(2.0)
	40.0	38.9

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

		2011		2010		2009
	Long term rate of return expected		Long term rate of return expected		Long term rate of return expected	
		£m		£m		£m
Equities	6.8%	27.7	7.65%	27.7	8.4%	24.7
Bonds	3.4%	12.3	4.2%	11.2	4.9%	10.2
Total fair value of assets		40.0		38.9		34.9

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

History of experience gains and losses:

	2011 £m	2010 £m	2009 £m	2008 £m	2007 £m
Present value of funded and unfunded obligations	(65.2)	(61.9)	(63.0)	(42.0)	(48.3)
Fair value of scheme assets	40.0	38.9	34.9	28.4	35.0
Deficit in the schemes	(25.2)	(23.0)	(28.1)	(13.6)	(13.3)
Experience gains on scheme liabilities	-	3.8	-	-	-
Percentage of scheme liabilities	-	6.1%	-	-	-
Experience (losses)/gains on scheme assets	(1.3)	1.4	4.2	(9.9)	0.3
Percentage of scheme assets	(3.3)%	3.6%	12.0%	(34.9)%	0.9%

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

	2011 £m	2010 £m
Opening deficit in schemes	(23.0)	(28.1)
Current service (cost)/credit	(1.2)	0.6
Contributions	1.5	1.7
Other finance costs	(0.7)	(1.2)
Actuarial (loss)/gain	(1.8)	4.0
Closing deficit in the schemes	(25.2)	(23.0)

The principal assumptions used in the actuarial valuation of the Chemring Group Staff Pension Scheme were as follows:

	2011	2010
Discount rate	5.0%	5.35%
Rate of increase in salaries	4.05%	4.45%
Rate of increase in deferred pensions	3.0%	3.4%
Rate of increase in pensions in payment (where applicable)	3.0%	3.4%
Inflation assumption - RPI	3.05%	3.45%
- CPI	2.35%	2.75%
Expected return on scheme assets	5.72%	6.6%

In determining the pension liabilities the Group uses mortality assumptions which are based on published mortality tables. For the Chemring Group Staff Pension Scheme, the actuarial table currently used is SAPS Year of Birth Tables with a medium cohort and 1% underpin.

Life expectancy at 65:

	2011	2010
Future pensioners - male	88.2	88.5
- female	91.0	91.9
Current pensioners - male	86.3	86.6
- female	89.1	89.8

The assumption considered to be the most significant is the discount rate adopted. If the discount rate in the scheme were to change by 0.1% then it is predicted that the deficit in the scheme would change by approximately £1.2 million. A change in the rate of inflation by 0.1% is predicted to change the deficit by approximately £0.8 million and a one year change to the longevity assumption would change the deficit by approximately £1.6 million.

The Group anticipates contributions to the defined benefit schemes for the year ending 31 October 2012 will be £2.2 million (2011: £2.0 million).

35. Contingent liabilities

The Group enters into contracts which sometimes have offset commitments. These requirements are valued at the time of the contract being awarded. The cost of the offsets are reviewed throughout the contract life and provided for to the extent of the potential liability.

At 31 October 2011, the Group had contingent liabilities in respect of bank and contractual performance guarantees and other matters arising in the ordinary course of business. Where it is expected that a material liability will arise in respect of these matters, appropriate provision is made within the Group financial statements. As the conditions of these guarantees are currently being met, no obligating event is foreseeable and therefore no provision has been made at the year end.

The Group is, from time to time, party to legal proceedings and claims which arise in the ordinary course of business. The directors do not anticipate that the outcome of these proceedings, actions and claims, either individually or in aggregate, will have a material adverse effect upon the Group's financial position.

During the year the Group wound up its captive insurance company, CHG Insurance Limited. CHG Insurance Limited ceased to provide insurance cover for the Group on 31 October 2010, and the Group has instead carried a self-insured deductible of £2.5 million on its material damage and business interruption insurance cover since that date.

Notes to the Group Financial Statements

36. Related party transactions

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

Trading transactions

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

Remuneration of key management personnel

The remuneration of the directors, who are the key management personnel of the Group, is set out below in aggregate for each of the categories specified in IAS 24 *Related Party Disclosures*. Further information on the remuneration of individual directors is provided in the audited part of the Directors' Remuneration Report on pages 39 to 47.

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

The remuneration of the executive directors is determined by the Remuneration Committee having regard to the performance of the individuals and market trends. The remuneration of the non-executive directors is determined by the Board having regard to the practice of other companies and the particular demands of the Group.

	2011 £m	2010 £m
Remuneration of the executive and non-executive directors	1.5	1.6
Share-based payments	-	0.5
Total	1.5	2.1

Independent Auditors' Report on the Parent Company Financial Statements

We have audited the parent company financial statements of Chemring Group PLC for the year ended 31 October 2011 which comprise the Parent Company Balance Sheet, the Parent Company Statement of Total Recognised Gains and Losses, the Reconciliation of Movements in Shareholders' Funds and the related Notes 1 to 12. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the parent company financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the parent company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications in our report.

Opinion on financial statements

In our opinion the parent company financial statements:

- give a true and fair view of the state of the parent company's affairs as at 31 October 2011;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the parent company financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Other matters

We have reported separately on the Group financial statements of Chemring Group PLC for the year ended 31 October 2011.

Nigel Mercer ACA (Senior Statutory Auditor)

for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditors
London, United Kingdom
24 January 2012

Parent Company Balance Sheet (under UK GAAP)

as at 31 October 2011

	Note	£m	2011 £m	£m	2010 £m
Fixed assets					
Tangible assets	2		0.9		0.8
Investments	3		571.2		515.6
			572.1		516.4
Current assets					
Debtors	5	15.4		5.9	
- due within one year	5	272.0		246.9	
- due after more than one year	5				
Creditors due within one year	6	(133.1)		(129.4)	
			154.3		123.4
Net current assets					
			726.4		639.8
Total assets less current liabilities					
Creditors due after more than one year	7		(381.4)		(417.1)
			345.0		222.7
Capital and reserves					
Called-up share capital	8		2.0		1.8
Reserves					
Share premium account	9	230.6		120.4	
Special capital reserve	9	12.9		12.9	
Hedge reserve	9	-		(1.5)	
Profit and loss account	9	106.1		96.3	
			349.6	228.1	
Own shares	10	(6.6)		(7.2)	
			343.0		220.9
Shareholders' funds					
			345.0		222.7

These financial statements were approved and authorised for issue by the Board of Directors on 24 January 2012.
Signed on behalf of the Board of Chemring Group PLC (registered number 86662)

D J Price P A Rayner

Parent Company Statement of Total Recognised Gains and Losses

for the year ended 31 October 2011

	Note	2011 £m	2010 £m
Profit for the financial year	9	36.7	106.1
(Losses)/gains on cash flow hedges		(0.1)	0.6
Tax charge on items taken directly to reserves		-	(0.1)
Additional charge due to treasury shares		(0.5)	(0.6)
Total recognised gains and losses for the year		36.1	106.0

Reconciliation of Movements in Shareholders' Funds

for the year ended 31 October 2011

	Note	2011 £m	2010 £m
Profit for the financial year		36.7	106.1
Dividends		(22.7)	(18.7)
Profit for the year		14.0	87.4
Other recognised losses		(0.6)	(0.1)
Ordinary shares issued	8	0.2	-
Share premium arising	9	110.2	0.1
Share-based payments (net of deferred tax)		(2.1)	0.1
Own shares	10	0.6	(2.0)
Net addition to shareholders' funds		122.3	85.5
Opening shareholders' funds		222.7	137.2
Closing shareholders' funds		345.0	222.7

Profit attributable to shareholders
In accordance with the concession granted under the Companies Act 2006, section 408, the profit and loss account of Chemring Group PLC has not been presented separately in these financial statements. There is no material difference between the results disclosed and the results on an unmodified historical cost basis.

Cash flow statement
In accordance with the exemption under FRS 1 the Company's cash flow statement has not been presented separately in these financial statements.

Notes to the Parent Company Financial Statements

for the year ended 31 October 2011

1. Chemring Group PLC accounting policies

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards. The particular accounting policies adopted have been applied consistently throughout the current and previous year and are described below.

Accounting convention

The financial statements are prepared under the historical cost convention, as modified by the revaluation of property, in accordance with the Companies Act 2006 and applicable accounting standards (UK GAAP).

Related Parties

The Company is exempt under FRS 8 *Related Party Disclosures* from disclosing transactions with other members of the Group.

Revenue recognition

Interest income is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to its net carrying amount.

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

Tangible fixed assets

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

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

Investment in Group undertakings

Investments are stated at cost less any provision for impairment in value.

Operating leases

Operating lease rental charges are taken to the profit and loss account on a straight-line basis over the life of the lease.

Provisions

A provision is recognised when the Company has a present legal or constructive obligation as a result of a past event and it is probable that settlement will be required of an amount that can be reliably estimated. Long term liabilities and provisions are discounted when the impact is material.

Current tax

Current tax, including UK corporation tax and foreign tax, is provided for at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted, or substantially enacted, by the Balance Sheet date.

Deferred tax

Deferred tax is provided in full at the anticipated tax rates on differences arising from the inclusion of items of income and expenditure in tax computations in periods different from those in which they are included in the financial statements. Deferred tax is not provided on timing differences arising from the revaluation of fixed assets where there is no commitment to sell the asset. Deferred tax assets and liabilities are not discounted.

Special capital reserve

The special capital reserve was created as part of a capital

reduction scheme involving the cancellation of the share premium account which was approved by the Court in 1986, in accordance with the requirements of the Companies Act 1985.

Foreign currencies

The functional currency of the Company is sterling. Transactions in foreign currencies are translated into sterling at the rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the Balance Sheet date are translated at the rates ruling at that date. These translation differences are dealt with in the profit and loss account.

For a forward foreign exchange contract to be treated as a hedge the instrument must be related to actual foreign currency assets or liabilities or to a probable commitment. It must involve the same currency or similar currencies as the hedged item and must also reduce the risk of foreign currency exchange movements on the Company's operations. Gains and losses arising on these contracts are deferred and recognised in the profit and loss account, or as adjustments to the carrying amount of fixed assets, only when the hedged transaction has itself been reflected in the Company's financial statements.

For an interest rate swap to be treated as a hedge the instrument must be related to actual assets or liabilities or a probable commitment and must change the nature of the interest rate by converting a fixed rate to a variable rate or vice versa. Interest differentials under these swaps are recognised by adjusting new interest payable over the periods of the contracts.

If an instrument ceases to be accounted for as a hedge, for example because the underlying hedged position is eliminated, the instrument is marked to market and any resulting profit or loss recognised at that time.

Bank borrowings

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

Pensions

The Company operates a defined benefit pension scheme. The defined benefit scheme is a multi-employer scheme including employees of other Group companies. It is not considered possible to allocate scheme assets and liabilities between the various companies and accordingly schemes are accounted for as though they were defined contribution schemes. The amount charged to the profit and loss account is the contribution payable in the year. Differences between amounts payable and actually paid are shown as accruals or prepayments in the Balance Sheet.

The Company also operates a defined contribution pension scheme. The amount charged to the profit and loss account in respect of pension costs and other post-retirement benefits is the contributions payable in the year. Differences between contributions payable in the year and contributions actually paid are shown as either accruals or prepayments in the Balance Sheet.

Share-based compensation

For grants made under the Company's share-based incentive schemes, amounts which reflect the fair value of options awarded at the time of grant are charged to the profit and loss account. The valuation of the awards utilises a methodology based on the Black-Scholes model. Further details can be found within Note 3 of the Group financial statements.

2. Tangible assets

	Land and buildings £m	Plant and equipment £m	Total £m
Cost			
At 1 November 2010	0.4	1.3	1.7
Additions	0.1	0.3	0.4
Disposals	-	(0.1)	(0.1)
At 31 October 2011	0.5	1.5	2.0
Depreciation			
At 1 November 2010	0.1	0.8	0.9
Charge for the year	-	0.3	0.3
Disposals	-	(0.1)	(0.1)
At 31 October 2011	0.1	1.0	1.1
Net book value			
At 31 October 2011	0.4	0.5	0.9
At 31 October 2010	0.3	0.5	0.8

The Company had no capital commitments as at 31 October 2011 (2010: nil).

Land and buildings represent leasehold improvements.

3. Investments

	Shares in subsidiary undertakings £m	Loans to subsidiary undertakings £m	Total £m
Cost			
At 1 November 2010	528.5	6.3	534.8
Capital contribution to subsidiary undertakings	56.1	-	56.1
Disposal	(0.5)	-	(0.5)
At 31 October 2011	584.1	6.3	590.4
Provision for impairment			
At 1 November 2010 and 31 October 2011	19.2	-	19.2
Net book value			
At 31 October 2011	564.9	6.3	571.2
At 31 October 2010	509.3	6.3	515.6

During the year the Company wound up its captive insurance company, CHG Insurance Limited. The business distributed its assets to its parent, Chemring Group PLC. The distribution led to the investment being received and no gain or loss being incurred. CHG Insurance Limited ceased to provide insurance cover for the Group on 31 October 2010, and the Group has instead carried a self-insured deductible of £2.5 million on its material damage and business interruption insurance cover since that date.

Notes to the Parent Company Financial Statements

for the year ended 31 October 2011

4. Investments in Group undertakings

The trading subsidiary undertakings held at 31 October 2011 were:

Trading subsidiary undertaking	Country of incorporation (or registration) and operation	% of issued ordinary share capital controlled by Chemring Group PLC	Activity
Chemring Countermeasures Ltd	England	100	Countermeasures
Chemring Defence UK Ltd	England	100	Counter-IED/Pyrotechnics
Chemring Marine Ltd	England	100	Pyrotechnics
*Chemring EOD Ltd	England	100	Counter-IED
Chemring Prime Contracts Ltd	England	100	Munitions
Roke Manor Research Ltd	England	100	Counter-IED/Countermeasures
Chemring Energetics UK Ltd	Scotland	100	Counter-IED/Pyrotechnics/Munitions
*Chemring Defence Germany GmbH	Germany	100	Counter-IED/Pyrotechnics
*Alloy Surfaces Company, Inc.	USA	100	Countermeasures
*Kilgore Flares Company LLC	USA	100	Countermeasures
*Technical Ordnance, Inc.	USA	100	Pyrotechnics/Munitions
*Chemring Energetic Devices, Inc.	USA	100	Pyrotechnics/Munitions
*Chemring Ordnance, Inc.	USA	100	Pyrotechnics/Munitions
*Chemring Military Products, Inc.	USA	100	Munitions
*Non-Intrusive Inspection Technology, Inc.	USA	100	Counter-IED
*Hi-Shear Technology Corporation	USA	100	Pyrotechnics
*Chemring Detection Systems, Inc.	USA	100	Counter-IED
*Chemring Australia Pty Ltd	Australia	100	Counter-IED/Countermeasures/ Pyrotechnics/Munitions
*Chemring Defence Spain S.L.	Spain	100	Pyrotechnics
*Simmel Difesa S.p.A.	Italy	100	Counter-IED/Pyrotechnics/Munitions
*Chemring Nobel AS	Norway	100	Munitions
Mecar S.A.	Belgium	100	Munitions
Associated undertaking			
CIRRA S.A.	France	49	Countermeasures
* Investments held by a subsidiary company			

The directors consider that the carrying value of the investments does not exceed their fair value.

5. Debtors

Amounts due within one year:	2011 £m	2010 £m
Group relief receivable	-	0.6
Deferred tax asset (see Note 11)	0.5	1.2
Other debtors	13.2	3.1
Prepayments and accrued income	1.7	1.0
	15.4	5.9
Amounts due after more than one year: Amounts owed by subsidiary undertakings	272.0	246.9

A financial instrument asset of £1.9 million (2010: £1.9 million) is recognised within other debtors in respect of the fair value of interest rate swaps (see Note 25 of the Group financial statements). The directors consider that the carrying value of the debtors approximates to their fair value.

6. Creditors due within one year

	2011 £m	2010 £m
Bank overdrafts	9.6	58.2
Bank loans	80.8	53.4
Trade creditors	1.2	1.6
Amounts owed to subsidiary undertakings	30.9	5.1
Other creditors	2.8	1.8
Other tax and Social Security	0.3	0.7
Accruals and deferred income	7.5	8.6
	133.1	129.4

A financial instrument liability of £1.2 million (2010: £1.6 million) is recognised in other creditors in respect of the fair value of derivative financial instruments (see Note 25 of the Group financial statements for further details).

In January 2011, the Group refinanced its bank facilities with a syndicate of five banks, extending the term of the facilities from April 2012 to April 2015. This revolving credit facility provides access to committed lending and bonding line support. Further information on the borrowing facilities can be found in Note 22 of the Group financial statements.

7. Creditors due after more than one year

	2011 £m	2010 £m
Derivative financial instruments (see Note 25 of the Group financial statements)	4.4	7.3
Medium term loan	-	26.6
Loan notes	260.3	261.2
Preference shares (62,500 shares of £1 each)	0.1	0.1
Amounts owed to subsidiary undertakings	116.6	121.9
	381.4	417.1

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

	2011 £m	2010 £m
Borrowings falling due within:		
One year	90.4	111.6
One to two years	-	26.6
After five years	260.3	261.2
	350.7	399.4

The interest incurred on the above borrowings is detailed within Note 22 of the Group financial statements. The overdraft and bank loans are denominated in sterling and Euro.

8. Called-up share capital

	2011 £m	2010 £m
Issued, allotted and fully paid		
195,476,434 (2010: 177,943,255*) ordinary shares of 1p each	2.0	1.8

On 20 April 2011 the Company placed 17,405,183 new ordinary shares, representing an increase of £0.2 million in the ordinary share capital and £110.2 million in the share premium reserve after costs (see Note 13 of the Group financial statements).

127,996 ordinary shares (2010: 14,095*) were issued under the Group's savings-related share schemes during the year.

The preference shares are presented as a liability (see Note 7) and accordingly are excluded from called-up share capital in the Balance Sheet.

Share-based incentive schemes

Full details of the schemes are disclosed in Note 32 of the Group financial statements.

* Restated figures for prior year to reflect the subdivision of each 5p ordinary share into five 1p ordinary shares on 28 March 2011

Notes to the Parent Company Financial Statements

for the year ended 31 October 2011

9. Reserves

	Share premium account £m	Special capital reserve £m	Hedging reserve £m	Profit and loss account £m	Total £m
At 1 November 2010	120.4	12.9	(1.5)	96.3	228.1
Ordinary shares issued	110.2	-	-	-	110.2
Profit for the year	-	-	-	36.7	36.7
Dividends paid	-	-	-	(22.7)	(22.7)
Other recognised losses	-	-	-	(0.6)	(0.6)
Cost of share-based payments	-	-	-	(2.1)	(2.1)
Transfers between reserves	-	-	1.5	(1.5)	-
At 31 October 2011	230.6	12.9	-	106.1	349.6

The share premium account and special capital reserve are not distributable. Of the £106.1 million in the profit and loss account, £42.6 million is distributable, with the remaining £63.5 million arising from the disposal of the investment in Simmel Difesa S.p.A. not being distributable.

The Company generated a profit for the financial year of £36.7 million (2010: £106.1 million). Dividends from subsidiary undertakings of £29.5 million (2010: £45.4 million) were received in the year.

The proposed final dividend in respect of the year ended 31 October 2011 of 10.8p per share will, if approved, absorb approximately £20.9 million of shareholders' funds. The dividend is subject to approval by shareholders at the Annual General Meeting and accordingly has not been included as a liability in these financial statements.

10. Own shares

	2011 £m	2010 £m
Balance at 1 November 2010	7.2	5.2
Acquired in the year	1.5	3.9
Issued in the year to satisfy employee share awards	(2.1)	(1.9)
Balance at 31 October 2011	6.6	7.2

The own shares reserve represents the cost of shares in Chemring Group PLC purchased in the market and held by the Group to satisfy awards under the Group's share-based incentive schemes (see Note 32 of the Group financial statements). During the year 300,000 (2010: 634,400*) ordinary shares were acquired, and 456,855 (2010: 500,055*) ordinary shares were distributed following the vesting of awards under the Chemring Group Performance Share Plan. The total number of ordinary shares held in treasury at 31 October 2011 was 1,343,145 (2010: 1,500,000*) with an average rate of £4.81 (2010: £4.83*) per share. This represents 0.7% of the total issued and fully-paid ordinary share capital.

Since the year end, the Company has acquired an additional 1,000,000 ordinary shares, bringing the number of shares held in treasury at 23 January 2012 to 2,343,145, with an average cost of £4.50 per share.

* Restated figures for prior year to reflect the subdivision of each 5p ordinary share into five 1p ordinary shares on 28 March 2011

11. Deferred tax

	2011 £m	2010 £m
Movements in deferred tax assets are as follows:		
At 1 November 2010	(1.2)	(1.4)
Charge to profit and loss account	0.7	0.2
At 31 October 2011	(0.5)	(1.2)
The amount provided represents:		
Other timing differences	(0.5)	(1.2)

12. Staff costs

	2011 Number	2010 Number
The average monthly number of employees (including executive directors) was:		
Total	38	34
	2011 £m	2010 £m
The costs incurred in respect of these employees were:		
Wages and salaries	3.4	3.3
Social security costs	0.4	0.4
Other pension costs	0.3	0.2
	4.1	3.9

Disclosures in respect of directors' emoluments can be found in the Directors' Remuneration Report on pages 39 to 47 of the Group financial statements.

Glossary and website

Glossary of terms

APOBS	Anti-Personnel Obstacle Breaching System	JCAST	Joint Combined Aircraft Systems Tester
EBITDA	Earnings before interest, tax, depreciation and amortisation	JSF	Joint Strike Fighter
EOD	Explosive ordnance disposal	JSLSCAD	Joint Service Lightweight Stand-off Chemical Agent Detector
EW	Electronic warfare	LAV	Light armoured vehicle
GPR	Ground penetrating radar	LOVA	Low vulnerability ammunition
HMDS	Husky Mounted Detection System	MANPADS	Man-portable air-defence system
I3M	ISTAR Information Integration and Management	MJU	Multi-Jettison Unit
IED	Improvised explosive device	NATO	North Atlantic Treaty Organization
IM	Insensitive munitions	OCO	Overseas Contingent Operations
IR	Infra-red	OEM	Original equipment manufacturer
ISTAR	Intelligence, Surveillance, Target Acquisition and Reconnaissance	OSHA	Occupational Safety and Health Administration (US)
JBPDS	Joint Biological Point Detection System	UAV	Unmanned aerial vehicle

Find out more online

For more information about Chemring Group PLC, please visit www.chemring.co.uk where you can access the latest shareholder information:

- Current share price
- Key financial information
- Financial calendar
- Shareholder services and notices
- Corporate governance
- RSS news feeds
- Results and presentations
- Analysts' forecasts
- Regulatory news

Chemring Group PLC's Annual Report and Accounts 2011 can also be viewed online at www.chemring.co.uk/investors.

You can also view and download the Notice for our Annual General Meeting.



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