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AN ANALYSIS OF THE ARMAMENTS CORPORATION OF SOUTH AFRICA'S (ARMSCOR) ANNUAL REPORT FOR THE FINANCIAL YEAR 2017/18

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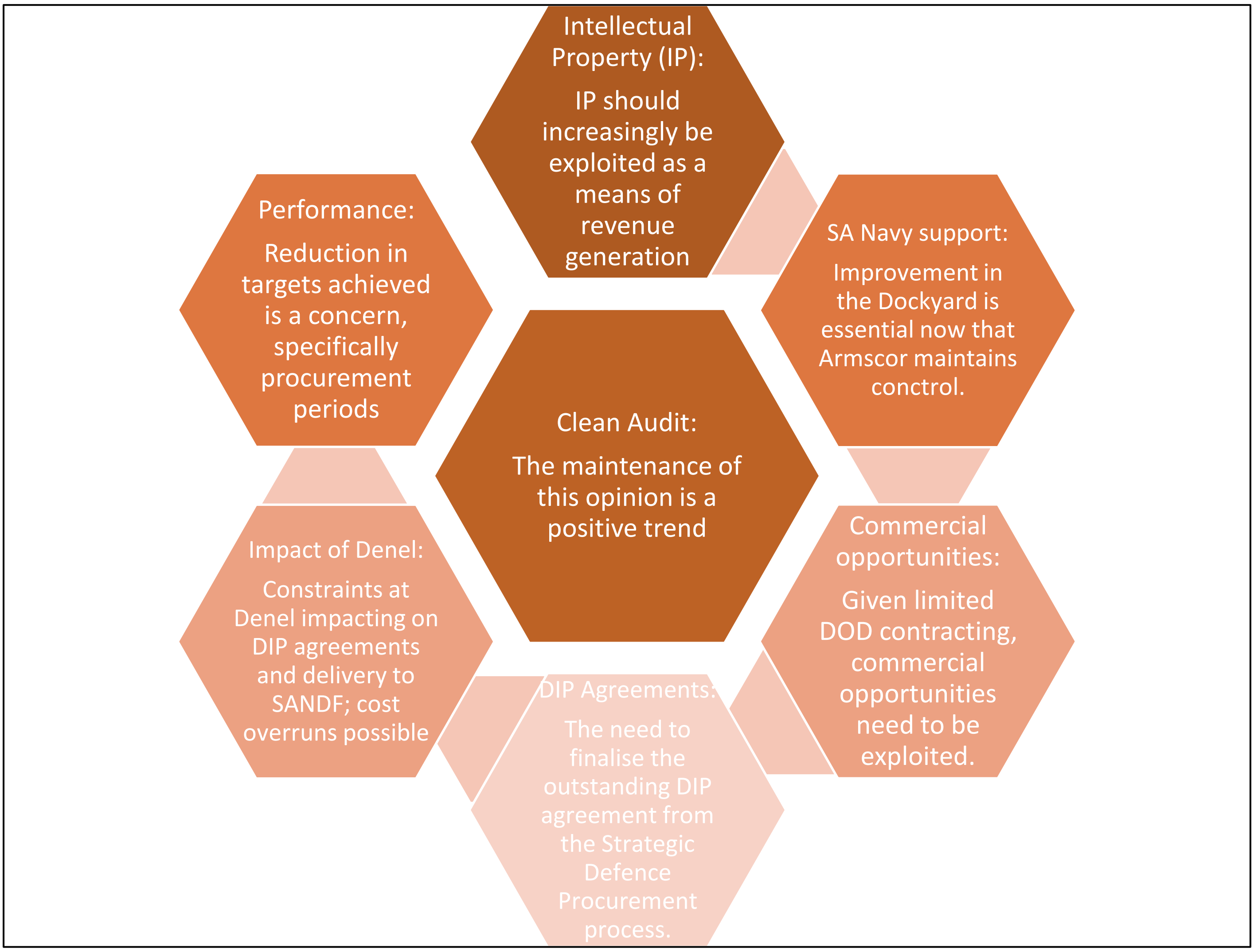
KEY FOCUS AREAS FOR THE PCDMV RELATED TO ARMSCOR

Armscor has succeeded in maintaining its clean audit without findings from the AG for the third year running. This is representative of its high levels of corporate and financial discipline. Profits also increased and the Armscor Group managed to show an overall profit of R1.7 million compared to a loss of R126.9 million in the previous financial year. However, while profits increased, Armscor remains largely dependent on its state allocation. Given the financial constraints of the DOD which results in less contracting for Armscor, it is therefore essential that Armscor continue to exploit commercial opportunities where possible. In this regard, the work of Alkantpan, the Hazmat Facility, Gerotek as well as the exploitation of Intellectual Property are essential. Finally, improvement at the Dockyard should be addressed as a matter of urgency as it impacts both on the SA Navy's capabilities and internal developments of Armscor. Finally, it is increasingly clear that constraints at Denel are impacting on Armscor's effectiveness and means should be developed to limit this impact.

Figure 1: Possible Armscor focus areas for the PCDMV



1. INTRODUCTION

The Armaments Corporation of South Africa Ltd (Armscor) was established in terms of the Armaments Production and Development Act (No. 57 of 1968) to satisfy the requirements of the South African National Defence Force (SANDF) in respect of Defence Matériel.

In 2017/18, Armscor continued to provide this support to the Department of Defence (DOD) as its primary client. Given the reduced spending capability of the DOD, Armscor and the broader defence industry continues to be under increased financial pressure. This underlies Armscor's current Turnaround Strategy which entered Phase 2 (Implementation) during the 2017/18 financial year. Armscor again obtained an unqualified audit from the Auditor-General of South African (AGSA) for the year under review.

This document analyses Armscor's major operations, including Acquisitions, Defence Industrial Participation (DIP), Research and Development, and the Armscor Dockyard. It also provides an overview of the current human resources situation and an overview of concerning Key Performance Indicators (KPI). It concludes with an analysis of financial statements.

A Review of the legislative framework for performance assessment:

The Constitution vests the National Assembly with the power of oversight over their respective executives, in addition to their legislative and other powers. Furthermore, the Money Bills Amendment Procedure and Related Matters Act, 2009 (Act 9 of 2009) stipulates the procedure to be followed by Parliament prior to the introduction of the national budget. Section 5(1) states that the National Assembly, through its committees, must annually assess the performance of each national department, with reference to the following:

- The medium term estimates of expenditure of each national department, its strategic priorities and measurable objectives (APP), as tabled in the National Assembly with the national budget (ENE);
- prevailing strategic plans;
- the expenditure report relating to such department published by the National Treasury in terms of section 32 of the Public Finance Management Act (quarterly expenditure);
- the financial statements and annual report of such department (Annual Report);
- the reports of the Committee on Public Accounts relating to a department; and
- any other information requested by or presented to a House or Parliament.

The outcome of the performance assessment process followed by Committees is to annually submit a **budgetary review and recommendation reports (BRRR)** for tabling in the National Assembly, as per Section 5(2) of the Money Bills Amendment Procedure and Related Matters Act. The BRRR -

- Must assess the department's service delivery performance given available resources;
- Must provide an assessment on the effectiveness and efficiency of the departments use and forward allocation of available resources; and
- May include recommendations on the forward use of resources.

The *PCDMV* should keep the above-mentioned outcomes of the BRRR in mind during its deliberations with Armscor on its Annual Report in order to deliver a substantial BRRR.

2. ACQUISITIONS

Acquisitions for the SANDF and other government departments reflect Armscor's core function. Recent years have seen an internal review of Armscor's acquisition strategy (in 2013/14 and 2016) to ensure alignment with international best practice. The updated and new documents promulgated during the review period are amongst others, the updated Acquisition and Project review practices, updated procedure for User Requirement Reviews, new Standard for Technical Baseline Items, and a new Handbook on Technical Reviews and Audits.[1] During the 2017/18 financial year, Armscor achieved the following in terms of contract management:

- R4.526 billion in terms of contracts relating to maintenance and support (in line with similar sized contract management for 2016/17).
- The value of capital acquisition contracts managed increased from R6.842 billion in 2016/17 to R7.744 billion in 2017/18.[2]

Armscor managed acquisition in terms of a number systems, of which the following should be noted:

Maritime systems. *A Hydrographic vessel* is being purchased for the SA Navy. The Annual Report notes that Armscor contracted the preferred bidder in November 2017. Construction was set to start "later in 2018".[3] Durban-based Southern African Shipyards (SAS) is the main contractor for Project Hotel to supply the SA Navy with a new hydrographic vessel and ancillary equipment.

Furthermore, an acquisition process for three new *Inshore Patrol Vessels* (IPVs) is in progress. The Annual Report notes that by December 2017 the contract was awarded for the construction of the three IPVs. News reports indicates that the contract was awarded to Cape-Town Based Damen Shipyards.[4] A similar tender for three Offshore Patrol Vessels have been put on hold.

Airborne systems. The 2015/16 Annual Report noted that the A-Darter Air-to-Air missile has been completed and an order placed for large-scale production. The first batch of missiles was expected to be delivered by the 3rd Quarter of 2016. However, the 2016/17 Annual Report notes a number of delays with the finalisation of the A-Darter missile system and the delivery of the first batch is now only expected in the 4th Quarter of 2017. The 2017/18 Annual Report then notes further delays of 26 month.[5] The A-Darter missile is funded jointly by the South African Air Force and the Brazilian Air Force.

Landward acquisitions. The most significant acquisition in the landward defence environment is Project Hoefyster which relates to the purchasing of new Infantry Fighting Vehicles for the SA Army to replace the ageing Ratel fleet which has been in service since 1976. An order for 244 new vehicles was placed with various variants to be delivered to the

[1] Armscor. (2018). p. 50
[2] Armscor. (2018). p. 16
[3] Armscor. (2018). p. 52
[4] Damen. (2018).
[5] Armscor. (2018). p. 53

SANDF. The majority of the new fleet will be constructed in South Africa and a locally designed and manufactured turret is used. While the first batch of 21 vehicles have been delivered from Finland, **local manufacturing by Denel has seen significant delays**. The 2017/18 Armscor Annual Report notes that "Denel Land Systems has slipped on the completion of the development phase" and that "the Industrialisation Phase, and at the end of the reporting period the entire programme had already been delayed by at least 32 months."

Furthermore, Phase 1 of a new Ground Based Air Defence System (GBADS) for the SA Army was delivered to the Air Defence Artillery Formation. This focused on the radar-guided system the 35mm guns of the Air Defence Artillery Formation. A second phase of the GBADS is currently under way and on track.

Questions

- In 2014 and 2016 Armscor carried out a review of its internal acquisition processes. What practical improvements have been made by Armscor to enhance Acquisition Management?
- The awarding of the contract for the SA Navy's new hydrographic vessel to a South African company should be commended as it enhances domestic capabilities and skills.
- What is the status of Project Hotel? Has the actual manufacturing of the vessel started?
- What is the delivery date for the SA Navy's new hydrographic vessel?
- What is the delivery date for the SA Navy's Inshore Patrol Vessels?
- How will it be ensured that there are no cost overruns for both Projects Biro and Hotel?
- What is the current position of the DOD on the acquisition of new Offshore Patrols Vessels for the SA Navy? Will this tender be introduced again in the near future?
- When can full integration of the A-Darter missiles with the Hawk Aircraft be expected?
- Are the current challenges experienced at Denel impacting on the final delivery and integration of the A-Darter with SA Air Force platforms?
- What are the potential for exports of the A-Darter system to ensure return on investment?
- A 32 month delay by Denel in the delivery of new Infantry Fighting Vehicles to the SANDF is of major concern. What is the new scheduled date for first delivery to the SANDF?
- Given the major delays in Project Hoefyster, how will it be ensured that cost overruns are not incurred?
- What was the initial cost set aside for the 244 vehicles and what are the latest figures?
- Are any penalties built into contracting for the delays caused by Denel regarding the delivery of the vehicles?
- How does the delays on Project Hoefyster impact on small local businesses subcontracted to the project? And how will this impact on potential exports of Denel's turret systems?
- Phase 1 of the new Ground Based Air Defence System focused on the 35mm cannons of the SANDF's Air Defence Artillery Capability. Are more advanced systems, such as long-range Surface-to-Air Missiles, currently in place in the SANDF?
- What are the practical advances to be made under Phase 2 of the Ground Based Air Defence System?

3. DEFENCE INDUSTRIAL PARTICIPATION

Defence Industrial Participation (DIP) relates to the obligation of a foreign supplier to reciprocate defence related business in South Africa as a result of a Defence acquisition. The DIP Policy was revised in October 2015. In 2017/18, Armscor continued to manage 14 such agreements, which is higher than the 12 managed in 2016/17. The value of DIP credits being managed remained similar to the previous financial year and comes to a total of R22.571 million. Of this, only R7.276 million relates to the 14 current ongoing DIP agreements in the defence domain.

One DIP agreement related to the 1999 Strategic Defence Procurement remains under the management of Armscor. This refers to an agreement with MBDA (a European based missile developer and manufacturer). The outstanding obligation in this regard equates to R933 million. The 2015/16 Annual Report indicated that the DIP agreement will be extended to 2019 to allow for the identification of new projects to offset the DIP. The 2017/18 Annual Report[6] notes the same extension, thus raising a question whether any progress was made in this regard.

Questions

- The fact that there is still an outstanding DIP agreement from the 1999 Strategic Defence Procurement process is of major concern. DIP projects are essential to skills transfers to South Africans and reinvesting in the country. The Committee should ask for a comprehensive explanation of the MBDA DIP agreement and reasons for the fact that obligations are likely not to be met.
- Are there any penalties in place should MBDA fail to meet its DIP obligations?
- Was there any progress made in 2017/18 to identify offsets for the MBDA DIP credits?
- What are the major changes introduced through the revised DIP Policy?
- What are the two new DIPs that were managed in 2017/18?

4. DEFENCE MATERIEL DISPOSAL[7]

Armscor also manages the disposal of defence equipment such as vehicles, vessels, ammunition and other equipment for the DOD. During 2017/18, Armscor concluded orders to the value of R72.3 million which is significantly higher than the R18.56 million worth of contracts placed in 2016/17. The African market was the main source of revenue. The Annual Report further notes the completion of disposal turnaround strategies in 2017/18, that resulted in an increase in revenue derived from collaboration with the local defence industry.

Questions

- Armscor should be commended for increasing revenue generated from disposal from R18.56 million in 2016/17 to R72.3 million in 2017/18.
- Are the funds generated from the sale of defence equipment returned to the DOD or are they returned to the fiscus?
- Is there further room for growth in revenue in this sector, specifically in Africa?

[6] Armscor. (2018). p. 55.
[7] Armscor. (2018). p. 89

5. RESEARCH AND DEVELOPMENT[8]

The Annual Report indicates that Armscor managed to earn 27 per cent of the total portfolio of R493.7 million from commercial contracts while the rest is attributed to contracts from the DOD in 2017/18. This is a decline compared to 2016/17 when Armscor earned 34 per cent of the total portfolio of R541.3 million from commercial contracts. The 2017/18 Annual Report further notes that Armscor is exploring the possibility of business partnering under the Turnaround Strategy to ensure the sustainability and effective management of Research and Development. The bulk of such services took place at Research and Development Facilities such as the *Gerotek and Alkantpan* test facilities as well as *Hazmat protective systems.*

Alkantpan is a munitions test range in the Northern Cape Province and attracts a number of international clients. Several international clients from, *inter alia*, Singapore and Germany conducted tests at the facility in 2017/18. The 2017/18 Annual Report does not indicate the exact income from sales at Alkantpan. In 2016/17, R86.2 million was generated by Alkantpan. The Alkantpan facility has also signed an agreement with the Square Kilometre Array (SKA) to ensure the viability of both facilities in the same geographic area.

Hazmat produces respiratory equipment for military and commercial purposes. The subsidiary managed to achieve a positive net income through the implementation of a conscious cost saving effort. This is considered an achievement considering the current economic climate. Hazmat is a self-sufficient entity that can serve the needs of all its major clients. The income generated from Hazmat's activities is not reflected in the Annual Report. In 2016/17, R14.6 million in sales was derived from commercial initiatives.

Other defence science technology institutes that receive the bulk of their funding from the DOD include:

- *Armour Development*: Conducting of defensive and reactive armour development. Funded by the Research and Development Board. In 2017/18, all tests were completed and a new three-year quotation submitted for the development of armour Protection Technology.
- *Protechnik laboratories*: Focus on chemical and biological defence. Previously the Armscor Annual Reports indicated the laboratory's achievement against its research/development services to the DOD and private sector. This breakdown was not provided in the 2017/18 Annual Report.
- *Ergonomics technologies*: Focus on integrating ergonomics into the SANDF. The 2016/17 Annual Report notes, among others that the institution assist with the selection of SA Air Force flight crews. Members should inquire further details regarding the selection of air crew. Previous media reports indicate that the SA Air Force is in the process of altering the safety and ejection seats of various aircraft, including the Pilatus PC7, the Hawk Mk120 and the JAS39 Gripen. "The projects has its origins in concerns raised regarding the "unfair exclusion of smaller built females" to pilot the three aircraft types."[9]

[8] Armscor. (2018) p. 57-65
[9] Helfrich, K. (2017).

- *Institute for Maritime Technology*: Provision of techno-military expertise to support naval decision-making. In 2016/17, sales increased to R94.2 million and required funding from the DOD also decreased from 93 per cent to 86.7 per cent. This information was not provided in the 2017/18 Annual Report. One of the major projects that the Institute is working on is the Ultrasonic Broken Rail Detector, which has significant commercial potential. It is indicated that a commercial product is to be available by the end of 2018/19.
- *Defence division support institute*: Provision of decision support to the DOD.
- *Flamengro*: Computer aided engineering centre of excellence.

Finally, Armscor has indicated to the PCDMV in the past the importance of exploiting Intellectual Property (IP) as a means of generating revenue. This excludes sovereign IP that can only be exploited after due consideration. Two IP exploitation requests were approved by the Armscor's Board of Directors in the 2017/18 financial year. The said requests are yet to be approved by the DOD.

Questions

- Armscor earned 27 per cent of the total portfolio of R493.7 million from commercial contracts. This is less than the 34 per cent achieved in 2017/18. What are the reason for the decline in generating business from commercial contracts?
- Armscor is exploring the possibility of business partnering under the Turnaround Strategy. What does this partnering entail and how will this assist Armscor (and the DOD)? Which subdivisions of Armscor are likely to partner with other institutions? Are private equity partners being considered?
- In 2016/17, Alkantpan generated R86.2 million in sales. What was the amount generated in 2017/18?
- Armscor's Hazmat facility achieved self-sustaining status in 2017/18 and should be commended for this achievement. Members may inquire as to the financial income of the institution in 2017/18 (compared to income of R14.6 million in 2016/17).
- What was the income of Gerotek in 2017/18? Is the institution self-sufficient? How does its 2017/18 income compare to that of previous years?
- What was Protechnik Laboratory's achievement against its research/development services to the DOD and private sector?
- Members should consider requesting Armscor to provide measurable targets for all of its subsidiaries. This will allow Parliament to track achievement more accurately in future.
- Is Ergonomics Technologies involved in the SA Air Force aircrew selection? If so, were they consulted on the decision to revamp ejection seats on various aircraft?
- Given the comparatively few aircraft in the SA Air Force, why was it decided to revamp ejection seats on various aircraft? What is the total cost of the project? How many "smaller built" pilots were excluded from potential training that resulted in the decision to revamp ejection seats?
- The development of the Ultrasonic Broken Rail Detector has attracted significant attention from the commercial market, including the Indian Railways. Have any orders for this been placed? Is the Intellectual Property of this projects well managed? Has this capability been tested by Transnet?

- Two Intellectual Property (IP) exploitation requests were approved by the Armscor's Board of Directors in the 2017/18 financial year. The requests are yet to be approved by the DOD. What are the reasons for the delays by the DOD? Is there significant potential for revenue generation from the exploitation of these two requests? *Members should consider the merits of the case and may further consider intervening to resolve unnecessary delays to ensure that IP can be exploited and due revenue generated.*

6. THE ARMSCOR DOCKYARD[10]

The Armscor Dockyard serves as the primary maintenance supplier to the SA Navy. As was noted in a number of previous years, the Dockyard is facing significant concerns. As such, a decision was previously taken to change the management of the dockyard. Subsequently, the Minister of Defence called for a "harmonious approach"[11] to management comprising Armscor, Denel and the SA Navy. However, the 2017/18 Annual Report notes that the "transfer of the Dockyard from Armscor to Denel was governed by the transfer agreement. These agreements contain suspensive conditions, which Denel had to fulfil by the 28 February 2018. The Minister of Defence and Military Veterans took account of the fact that Denel had not met the suspensive conditions for the transfer of the Dockyard to it, despite previous extensions. Thus, the Honourable Minister correctly concluded that the Dockyard Transfer Agreement had lapsed."[12] The CEO of Armscor further notes in the Annual Report that "the Dockyard will continue to explore a variety of collaborative measures with the private sector to reduce the Dockyard deficit and enhance the ongoing sustainability of the Dockyard.

In 2017/18, repair and maintenance were done on a number of SA Navy vessels. Armscor submitted Financial Authority requests for materials/spares and casual labour (fixed-term contractors) to the SA Navy for 2017/18. R18.497 million was approved and a total of R17.542 was paid equating to a 94.48 per cent spent.

Questions

- Given that Armscor is again in full control of the Dockyard, what steps will it take to ensure improvement in the management of the entity?
- The CEO mentioned that "the Dockyard will continue to explore a variety of collaborative measures with the private sector to reduce the Dockyard deficit." What steps have been taken in this regard?
- What measures will be implemented to ensure that the introduction of private sector partners will not reduce the Dockyards ability to prioritise SA Navy services?
- Given the strategic importance of the Dockyard, will external (foreign) private and/or state partners be considered or only domestic (South African) partners?
- Why was only 94.48 per cent of funds approved for work by the Dockyard actually spent?

[10] Armscor. (2018) p. 17; 66-68.
[11] Armscor. (2016) p. 23.
[12] Armscor. (2018) p. 17

7. HUMAN RESOURCES MANAGEMENT AND TRANSFORMATION[13]

The 2017/18 Annual Report indicates that Armscor, including the Armscor Dockyard, has a staff complement of 1 463, which is lower than the 2016/17 figure of 1 502. In terms of representation, a target was set to increase black employees from 66 to 68 per cent and performance of 77.32 per cent was already achieved in 2016/17. This increased further to 78.61 per cent in 2017/18. Female employees now comprise 35.27 per cent of Armscor.

Armscor should also be lauded for identifying capability retention and succession planning as key focus areas. As such, in 2017/18, at least 46 key position were identified as well as 74 potential successors. This translates to a 83.69 per cent compliance with the development plan as contracted with successors.[14]

Armscor continues to provide skills development through a number of programmes, the following of which are noteworthy:

- International Training Programmes. Three employees completed their studies at the Naval Post Graduate School in the USA in engineering. Four employees are registered for Masters in Science: Military Aerospace and Airworthiness. Two employees commenced with studies for the Advanced Masters in Unmanned Aircraft Systems Management programme.
- Talent Development Programme. In 2016/17, a total of 35 candidates were included in this graduate training programme. In 2017/18, 44 talent development candidates went through the programme.[15]
- Bursaries. 36 Bursaries were made available to undergraduate students at various universities.[16] Although the target of 33 bursaries was exceeded, it is a major reduction from the 116 bursaries afforded in 2016/17.
- Dockyard training. The Dockyard provided training to 92 apprentices. Of these, three have qualified as artisans, 40 are preparing for their trade tests and 48 are continuing with the theoretical foundation training.

Questions

- Armscor should be lauded for its improvement in achieving its transformation targets as well as its ability to do succession planning and skills retention.
- What was the major reason for the overall decrease in personnel numbers from 1 502 in 2016/17 to 1 463 in 2017/18?
- What are the reasons for the reduction in the number of bursaries from 116 in 2016/17 to 33 in 2017/18?
- Given financial constraints at the Dockyard, will Armscor be able to maintain the number of apprentices currently working at the Dockyard?

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[13] Armscor. (2018). p. 106-109
[14] Armscor. (2018) p. 43
[15] Armscor. (2018) p. 43
[16] Armscor. (2018) p. 42

8. PERFORMANCE OVERVIEW: UNDER ACHIEVEMENTS AND CHALLENGES[17]

Armscor performed relatively well when performance against set targets are measured. *A total of 53 Key Performance Indicators (goals) were set for 2017/18. Armscor managed to achieve 39 of these, which is a success rate of 73.58 per cent. This is a decrease in performance when compared to 2016/17.* 14 Targets were either not achieved, partially achieved or no opportunity to perform presented itself.

The KPIs not achieved were as follow:

Table 2: Selected Key Performance Indicators not achieved during 2017/18

Objective	KPI	Goal	Achievement	Comments
Procurement	90 days for standard procurement	90 days	101 days	This reflects a regression from the achievement of 93 days in 2016/17
Procurement	60 days for commercial off-the-shelf items	60 days	114	Significant regression from 60 days achieved in 2016/17
Defence Industrial Participation (DIP)	Value of DIP credits to be granted	R235.6 million	R157 million	Delays in project Hoefyster, the A-Darter system and other contracts
Generate additional income	Earn a fee based income from brokering deals	R34 million	R23.8 million	No comment
New business initiative	Sweating of DOD Assets	31 March 2018	No opportunity to perform	DOD strategy still to be developed
Transformation	Improving gender composition	37% Female employees	36.34% Female employees	No comment
Employee satisfaction	Employee satisfaction	1% improvement	0.74% decline	No comment
Infrastructure renewal	Completion of implementation of finance model	31 March 2018	Not achieved	Most of the development work on Finance module was mainly on the Acquisition Purchases

[17] Armscor. (2018) p. 34-49

Infrastructure renewal	Developing HR Modules	31 March 2018	Not achieved	The development of all nine submodules for HR & Payroll module had only progressed to just over 50%.
Infrastructure renewal	Investigate and implement e-procurement for identified Commercial and Military off the Shelf procurement	31 March 2018 Implementation of selected e-procurement process	New target date: March 2020	This solution has a dependency on the Supply-Chain Management module
Acquisition excellence	Engage with DOD to influence better alignment of capital projects	Finalisation of Through Life Capability Management acquisition policy	Project on Hold	DOD placed project on hold
Military Veterans Support	Submit application for set asides for Military Veterans with National Treasury.	31 March 2018	No longer required	Due to the change of legal requirements (as the Preferential Procurement Regulations gazetted in January 2017 provide for Military Veterans) this objective is not pursued anymore.

Questions

- The regression in the purchasing period for off-the-shelf items from 60 days to 114 days is of concern. What are the reasons for them exceeding the 60 day deadline?
- Are services deliver to international clients (such as those hosted at Alkantpan and Gerotek) impacted negatively by the slow procurement processes? For example, if a client request a quick acquisition of a product for their purposes at these facilities, can this be delivered on with the prescripts of the PFMA and existing procurement challenges?
- What can be done to improve procurement to under 90 days?
- *Members should note the impact of problems at Denel on the implementation of DIP credits in South Africa.*
- What are the reasons for not achieving the target for earning a fee based income from brokering deals?
- Is the strategy for sweating of DOD assets still being considered by the DOD? If so, is Armscor doing any preparatory work in this regard?
- The regression in terms of employee satisfaction is of concern. What are the main causes found for dissatisfaction among employees?
- What is the new target date for the implementation of the finance model?
- Why did the DOD put the Through Life Capability Management Acquisition Policy on hold?

9. FINANCIAL STATEMENTS AND REPORT OF THE AUDITOR-GENERAL[18]

The total comprehensive income of the Group increased from a loss of R126.9 million in 2016/17 to reflect a profit of R1.7 million in 2017/18. Revenue generated increased significantly from R1 399 million in 2016/17 to R1 668 million in 2017/18. However, this increase should be seen in context as it is largely due to an increased state allocation. The state allocation increased from R860 million in 2016/17 to R1 057 million in 2017/18. Nonetheless, Armscor did increase its sale of goods and services from R403 million in 2016/17 to R467 million in 2017/18. Other income also increased by R9.5 million.

Group reserves increased from R1 998 million to R2 000 million mainly as a result of the surplus during the year.

The following additional financial matters should be noted:

- Payment to employees as salaries and wages increased from R995.2 million in 2016/17 to R1 118 million in 2017/18. This translates to a 21.3 per cent increase in costs paid to employees.
- Compensation for executive directors increased from R6.295 million in 2016/17 to R7.124 million in 2017/18. This translates to a 13 per cent increase in income. (Executive income was R4.994 million in 2015/16)

Finally, as was the case in 2016/17, Armscor received a **clean audit with no qualifications** from the Auditor General of South Africa for 2017/18.

Questions

- Armscor should be congratulated for maintaining a clean audit for a third year running.
- The increase in the Groups surplus as well as the profitability of the Group are very positive developments.
- Are there any ways to make Armscor increasingly less reliant on its state subsidy?
- What are Armscor's major obstacles to further increasing profitability?
- Wages increased from R995.2 million in 2016/17 to R1 118 million in 2017/18. Yet, over the same period the number of employees decreased from 1 502 to 1 463. Armscor needs to explain the increase in staff costs against the reduction in personnel.
- What are the main drivers in the 13 per cent increase in executive remuneration?
- Previously, Armscor indicated to the PCDMV that it would be approaching the United Nations in an effort to boost South African involvement in the supply of equipment and services. Has any progress in this regard been made?

[18] Armscor (2018) p. 117

10. CONCLUSION

Armscor has succeeded in maintaining its clean audit without findings from the AG for the third year running. This is representative of its high levels of corporate and financial discipline. Profits also increased and the Armscor Group managed to show an overall profit of R1.7 million compared to a loss of R126.9 million in the previous financial year. However, while profits increased, Armscor remains largely dependent on its state allocation. Given the financial constraints of the DOD which results in less contracting for Armscor, it is therefore essential that Armscor continue to exploit commercial opportunities where possible. In this regard, the work of Alkantpan, the Hazmat Facility, Gerotek as well as the exploitation of Intellectual Property are essential. Improvement at the Dockyard should also be addressed as a matter of urgency as it impacts both on the SA Navy's capabilities and internal developments of Armscor.

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