

GEM DIAMONDS

Annual Report and Accounts 2016



A journey of perfection



The **Maluti Mountains**, in the Kingdom of Lesotho, is home to the world's highest situated diamond mine – Letšeng. At 3 100m above sea level, it is not only the altitude that makes the mine unique. Letšeng is renowned for some of the most distinctive diamonds ever recovered. In the past 10 years since Gem Diamonds took the mine over, four of the 20 largest white diamonds ever recorded were recovered at Letšeng. It is here in these rugged mountains that the remarkable 314 carat diamond, named the **Letšeng Destiny**, was unearthed in May 2015.

In line with Gem Diamonds' strategic goal to maximise the revenue received from these diamonds, a partnership arrangement was entered into, whereby the Group participates in further margin from the final polished sale of the diamond.

The result of the polished diamond was an exceptional **105.07 carat D flawless** pear-shaped diamond – unveiled in August 2016 and named the **Graff Vendôme**.

An additional 12 diamonds were created from the **Letšeng Destiny** with the largest being **17.10 carats**.

No one can predict when a large, exceptional find such as the Destiny will be made – although, given the **rich history of our Letšeng mine**, pinpointing the where may not be as challenging.

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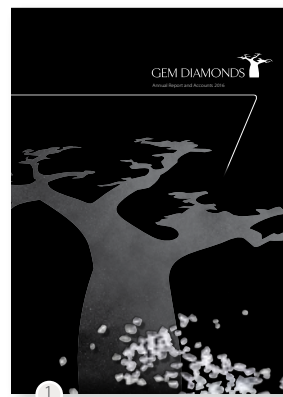
1. Annual Report and Accounts 2016

The Annual Report and Accounts have been prepared in accordance with:

- ▶ applicable English and British Virgin Islands law;
- ▶ regulations and best practice as advised by the Financial Reporting Council and the Department of Business, Innovation and Skills in the United Kingdom; and
- ▶ International Financial Reporting Standards.

2. Sustainable Development Report 2016

This document has been compiled in accordance with G4 Core Compliance and Global Reporting Initiative (GRI) and Gem Diamonds internal reporting guidelines, with consideration of the UN Global Compact. Refer to legal compliance in the document.



Gem Diamonds is a leading producer of high-value diamonds

NAVIGATION AID



This icon indicates additional information available on the Group's website www.gemdiamonds.com



This icon refers the reader to further information available in the Group's 2016 Sustainable Development Report which can be viewed on the Group's website.



Download this QR code on your smart device to gain quick access to our website.

The Strategic Report is set out on pages 2 to 59.

The Directors' Report is set out on pages 105 to 109.



About Gem Diamonds

Our presence

Diamond analysis and manufacturing

Baobab Technologies

Baobab Technologies

OWNERSHIP

100%

Gem Diamonds Limited

ESTABLISHED

April 2012

DESCRIPTION OF OPERATIONS

The Group's high-tech diamond analysis and manufacturing operation is tasked with:

- ▶ Investing in state-of-the-art diamond analysis technology
- ▶ Understanding the value of exceptional rough diamonds through mapping and analysis
- ▶ Manufacturing selected diamonds for final polished sale

Head Office

United Kingdom

Belgium

Sales and marketing

Gem Diamonds Marketing Services

Gem Diamonds Marketing Services

OWNERSHIP

100%

Gem Diamonds Limited

ESTABLISHED

October 2010

Gem Diamonds Marketing Botswana

Gem Diamonds Marketing Botswana

OWNERSHIP

100%

Gem Diamonds Limited

ESTABLISHED

August 2015

DESCRIPTION OF OPERATIONS

The Group's diamond sorting, sales and marketing operations in Belgium and Botswana focus on:

- ▶ Maximising the revenue achieved on diamond sales
- ▶ Developing the Gem Diamonds brand in the market
- ▶ Enhancing customer relationships



Gem Diamonds is a leading producer of high-value diamonds. The Group, which has its head office in the United Kingdom, owns the Letšeng mine in Lesotho and the Ghaghoo mine in Botswana. The Letšeng mine is renowned for its regular production of large, top colour, exceptional white diamonds, making it the highest average dollar per carat kimberlite diamond mine in the world. Since Gem Diamonds acquired the mine in 2006, Letšeng has produced four of the 20 largest white gem quality diamonds ever recovered.

Gem Diamonds has an organic growth strategy based on enhancing the operating efficiencies of the Letšeng mine and re-commencing production at Ghaghoo when the market for its production improves. Its primary focus is to achieve operational excellence and enhance value through continued cost reduction discipline and extracting maximum diamond value through technological initiatives. Additional value is generated through the Group's sales, marketing and manufacturing capabilities. Financial, technical and administrative services are supported by its South African subsidiary.

Mines

Letšeng Diamonds

TOTAL RESOURCE

5.0m carats

(as at 1 January 2015)

IN-SITU VALUE

US\$10.3 billion

(as at 1 January 2015)

Letšeng Diamond Mine

OWNERSHIP

70%

Gem Diamonds Limited

30%

Government of the Kingdom of Lesotho

ACQUIRED

July 2006

DESCRIPTION OF OPERATIONS

The Group's open pit mining operation in Lesotho focuses on:

- ▶ Mining and processing ore efficiently and safely from its two kimberlite pipes (Main and Satellite pipe)
- ▶ Optimising expansion projects to reduce diamond damage, diamond theft and to improve diamond liberation
- ▶ Implementing optimised life of mine (LoM) extensions

Gem Diamonds Botswana

TOTAL RESOURCE

20.5m carats

(as at 1 January 2014)

IN-SITU VALUE

US\$4.9 billion

(as at 1 January 2014)

Ghaghoo Diamond Mine

OWNERSHIP

100%

Gem Diamonds Limited

ACQUIRED

May 2007

DESCRIPTION OF OPERATIONS

Ghaghoo, the Group's development in Botswana was placed on care and maintenance in 2017 pending an improvement in market conditions for its diamond production.

Technical and administrative services

Gem Diamonds Technical Services

Famous Letšeng diamonds

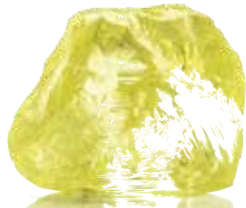
A strong track record

The Letšeng mine in Lesotho is renowned for its recovery of some of the world's most valuable diamonds, achieving the highest US\$ per carat of any kimberlite diamond mine in the world. Letšeng regularly produces diamonds of exceptional size and colour. In line with the Group's strategic goal to maximise the revenue achieved from remarkable diamonds, certain diamonds are sold into partnership arrangements whereby the Group participates in further margin from the final polished sale. The 314 carat Letšeng Destiny recovered and sold into partnership in the previous year, yielded exceptional polished diamonds further contributing to revenue in 2016.

299 carat yellow diamond

Recovered: 2014
Sold for: undisclosed*

This diamond was recovered in December 2014 and sold into a partnership arrangement in January 2015. Unmasking its true radiance, the gem was cut and polished by expert artisans with coloured diamond expertise, which resulted in a magnificent 132 carat fancy intense yellow cushion-shaped polished diamond, along with eight other yellow diamonds, the largest being a 21 carat fancy yellow pear shape. The 132 carat gem, aptly named The Golden Empress, was set into a breathtaking Graff signature necklace, adorned with 30 other cushion-cut yellow diamonds.



The 357 carat 'Letšeng Dynasty'

Recovered: 2015
Sold for: US\$19.3 million

The Letšeng Dynasty was recovered in July 2015 and sold for US\$19.3 million in September 2015, achieving the highest value ever for a single Letšeng diamond. The name given was to symbolise the succession of diamonds from the same family.



During 2016, Graff unveiled the Venus, a 118 carat heart-shaped, D flawless diamond, which was polished from the Letšeng Dynasty, making it the largest of its kind in the world. In total, 23 polished diamonds were extracted from this one rough diamond.

The 314 carat 'Letšeng Destiny'

Recovered: 2015
Sold for: undisclosed*

The Letšeng Destiny was recovered in May 2015 and sold into a partnership arrangement in June 2015. The name was given to signify a hidden power believed to control future events. During 2016, the Letšeng Destiny has yielded a main polished 105 carat pear-shaped D colour flawless diamond, the Graff Vendôme, making it the largest cut and polished diamond of its kind in Graff's history. Twelve smaller diamonds of D colour were also extracted from the rough diamond, totalling a polished weight of 164 carats.



The 493 carat 'Letšeng Legacy'

Recovered: 2007
Sold for: US\$10.4 million

The Letšeng Legacy is also ranked in the top 20 largest rough white diamonds recorded and its name highlighted the growing legacy that the Letšeng mine in Lesotho was creating as a producer of significant large white diamonds. This diamond was recovered in September 2007 and was sold for US\$10.4 million in November 2007. Twenty polished diamonds were extracted from this rough diamond.



* Sold into partnership arrangement

In 2016, Letšeng experienced a paucity of exceptional iconic diamonds but continued to recover large, high-quality diamonds. The largest diamond recovered in 2016 was a 160 carat diamond. The highest US\$ per carat achieved for a single diamond during the year was for an 11.8 carat pink diamond, which achieved US\$187 700 per carat, making it the third highest of its kind in the Group's history.

The 550 carat 'Letšeng Star'

Recovered: 2011
Sold for: undisclosed*

The 550 carat Letšeng Star was recovered in August 2011 and was so named to signify the growing number of 'stars' in Letšeng's constellation of large diamonds recovered. The Letšeng Star is also ranked in the top 20 largest white rough diamonds on record and the second largest white diamond to be recovered at Letšeng. This diamond yielded 12 pairs of pear shaped diamonds, as well as a main polished stone of 33 carats, also a pear shape, to form a unique collection of over 165 carats of D flawless and internally flawless polished gems stemming from this single rough diamond.



The 478 carat 'Leseli La Letšeng'

Recovered: 2008
Sold for: US\$18.4 million

The 'Leseli La Letšeng', which translates to 'Light of Letšeng', reflecting the diamond's remarkable colour and clarity, was recovered in September 2008 and is also ranked in the top 20 largest rough white diamonds recorded. This diamond was the third significant recovery from the Letšeng mine in as many years and was sold in November 2008 for US\$18.4 million (during the height of the global financial crisis).



The fame of this diamond extends further in that it revealed a 102 carat round shaped, D colour internally flawless diamond, making it the largest round-shaped polished diamond ever to be graded D colour internally flawless by the Gemological Institute of America (GIA). A further 10 exquisite polished diamonds were also revealed.

12 carat Blue diamond

Recovered: 2013
Sold for: US\$7.5 million

This rare 12.47 carat blue diamond was recovered at Letšeng in September 2013. It was sold a month later on tender in Antwerp for a record price of US\$603 047 per carat (US\$7.5 million), the highest US\$ per carat for any Letšeng rough diamond sold to date.



The 603 carat 'Lesotho Promise'

Recovered: 2006
Sold for: US\$12.4 million

The 603 carat Lesotho Promise was recovered in August 2006 and together with being ranked in the top 20 of the world's largest white diamonds on record, is also the largest diamond to emerge from the Letšeng mine to date. The Lesotho Promise was sold for US\$12.4 million in October 2006 and was subsequently polished into 26 D flawless and internally flawless diamonds, the largest of which was a 76 carat pear shaped diamond.

All 26 polished diamonds were fashioned into a single necklace by Graff.



* Sold into partnership arrangement

2016 in review a challenging year

Financial

US\$ million	FY 2016	FY 2015	% change
Revenue	189.8	249.5	24 ↓
Corporate expenses	11.0	11.7	6 ↓
Underlying EBITDA	62.8	103.5	39 ↓
Profit for the year (before exceptional items)	32.4	67.4	52 ↓
(Loss)/profit from exceptional items	(176.5)	10.2	1 830 ↓
(Loss)/profit for the year (after exceptional items)	(144.1)	77.6	247 ↓
Basic earnings per share (EPS) (before exceptional items) (cents)	12.8	30.2	58 ↓
Basic EPS (after exceptional items) (cents)	(114.9)	37.6	406 ↓
Cash and short-term deposits	30.8	85.7	64 ↓
Bank loans owing	27.8	30.4	9 ↓

Refer to Note 3, Operating profit, for definition of non-GAAP measures.

Health, safety, social and environment (HSSE)



Our mines achieved a **fatality free** year with the lowest ever recorded all injury frequency rate (AIFR)



Five lost time injuries (LTIs) resulting in 0.18 lost time injury frequency rate (LTIFR)



Letšeng retains **ISO 14001 and ISO 18001** certification



Zero major or significant environmental and stakeholder incidents

Letšeng



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Plant 2 Phase 1 upgrade post investment review indicates **achievement** of expected **increase** in plant capacity

Five diamonds larger than 100 carats recovered

11.78 carat pink diamond sold for **US\$187 700 per carat**, making it the **third highest price per carat diamond sold** by Letšeng

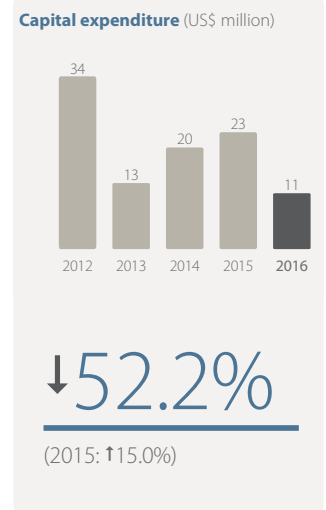
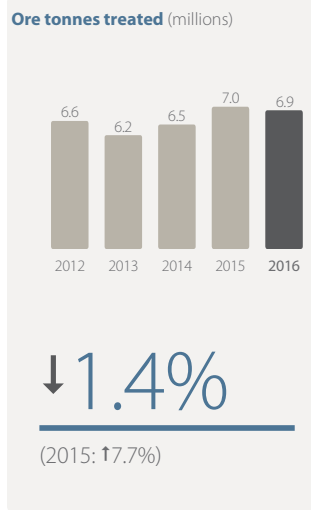
Largest diamond recovered during the year was **160.21 carats**

Average price achieved of US\$1 695 per carat due to paucity of large high-value diamonds recovered

Achieved **562 consecutive LTI-free days**

Opened the **Letšeng Diamond Discovery Centre** in Lesotho to promote knowledge about the diamond mining industry in the country

Operational



Ghaghoo



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Group



Operation **downsized**

Achieved **449 consecutive LTI-free days**

Average price achieved of **US\$152 per carat**

Post period end placed on **care and maintenance**

Increased Company facility from US\$20.0 million to US\$35.0 million

Lowest AIFR in Company history

Chairman's statement



Roger Davis Chairman

Dear shareholder,

On behalf of the Board, it is my pleasure to present Gem Diamonds' 2016 Annual Report. I believe this report offers a fair and balanced account of the business, its performance over the last year and its prospects going forward. As an organisation, Gem Diamonds remains committed to transparent and relevant reporting to you, its shareholders.

2016 IN REVIEW

Gem Diamonds' strategy is built on three pillars; namely value creation, growth and sustainability. This broad-based approach was developed to allow the Group the flexibility to respond to an ever-changing operating context and has enabled it to adapt to short-term opportunities and challenges while moving towards its long-term goal of delivering sustainable shareholder returns.

The 2016 financial year was challenging for the Group's two operations. Operationally, the Letšeng mine performed well, with all production metrics achieved. In addition, the demand for, and prices of, its large, high-quality, white diamonds remained relatively firm throughout the year. However, the decline in the number of diamonds larger than 100 carats recovered during the year, adversely impacted the Group's revenue, projects and cash flow.

Despite the paucity in the number of large diamonds recovered during 2016, Letšeng continued to recover exceptional, high-quality diamonds demonstrated through the recovery of two rare and valuable pink diamonds of 11.78 and 12.31 carats, which were sold for US\$2.2 million and US\$1.4 million, respectively. A large 160 carat diamond was also recovered in 2016 and sold into a partnership agreement at a top price, reinforcing the quality of the Letšeng asset.

Development of the Ghaghoo mine continued following the decision to downsize the operation and reduce its associated cost structure. Regrettably, the market for smaller commercial goods (such as those mined at Ghaghoo) remained under pressure and prices for these goods have declined from US\$210 to US\$142 per carat. Largely due to the depressed market and low realised prices, the Board made the difficult decision to place the operation on care and maintenance in February 2017 resulting in an impairment of US\$170.8 million. Ghaghoo remains a key asset for the Group and its expansion opportunities, when diamond prices recover, will strengthen the Group's position. The orebody and all of its characteristics are well understood with just under

137 000 carats recovered and sold to date. 20.5 million carats are contained within the resource.

Against this backdrop, the Group delivered a satisfactory performance. The Group generated underlying EBITDA* of US\$63 million with an attributable profit of US\$18 million before a non-cash impairment charge of US\$176 million. The Group ended the year with a cash balance of US\$31 million and undrawn facilities of US\$53 million as at 31 December 2016.

SUPPORTING INDUSTRY ADVOCACY

The Group understands the importance of protecting and enhancing the premium brand of diamonds. Gem Diamonds was one of the founding members of the Diamond Producers Association (DPA). The Group's association with the DPA has allowed Gem Diamonds to play an active role in maintaining and enhancing consumer demand for and confidence in diamonds.

PARTNERING FOR GROWTH

Gem Diamonds is committed to partnering with its stakeholders to create mutual benefit and shared growth. The Group strives to create positive impact through social initiatives that will outlast the life of its mines. Therefore, the Group's focus is on implementing sustainable projects that address the needs of project-affected communities (PACs). This is done through constant engagement with stakeholders at all levels of the business and using their feedback to guide corporate social investment strategies.

On 6 May 2016, the Letšeng Diamond Discovery Centre was officially opened by His Majesty, King Letsie III in Maseru. The centre tells the story of Lesotho's diamond industry in an interactive manner, focusing on the history of diamond mining at Letšeng. The centre was built to promote knowledge and serve as a foundation for Basotho learners who wish to learn more about the diamond mining industry and possibly pursue careers in the field. To date almost 1 600 visitors have passed through the centre, the vast majority of whom are school children.

STRIVING FOR ZERO HARM

Gem Diamonds endeavours to incorporate sustainability best practice into every level of the business, keeping up-to-date with new developments. Pursuing its goal of zero harm in all areas is a continued priority. During 2016, the Group experienced a fatality-free year and continues to invest in safety training and capability building in its effort to embed a strong safety culture throughout the organisation. Pleasingly, the all injury frequency rate achieved during the year is the lowest in the history of the Group.

* Refer to Note 3, Operating profit, for the definition of non-GAAP measures.

Chairman's statement continued

PURSuing EXCELLENCE IN CORPORATE GOVERNANCE

The Board is committed to the highest standards of corporate oversight and believes that strong governance is critical to the Group's sustainability.

The Board is tasked with providing leadership and guidance to the Group within a framework of controls. It also ensures that the necessary financial and human resources are in place for the Group to meet its objectives and increase shareholder value.

In 2016, the Board once again conducted a detailed Board evaluation. The assessment reviewed the effectiveness of the Board as a collective and the contribution of the individual Directors. Furthermore, the Board evaluation exercise also looked at the composition of the Board and its committees' conduct and decision-making; its approach to and implementation of risk management, management information and reporting; training, development and succession planning; and communication. The outcome of the assessment was used to inform the Board's planning for the year and reinforced our commitment to applying best practices, and setting, monitoring and evaluating the high standards of governance we wish to maintain.

During the year, Alan Ashworth retired as Chief Operating Officer. On behalf of the Board, I would like to thank Alan for his tireless commitment to Gem Diamonds during his eight-year tenure. We welcomed Johnny Vellozo as the new Chief Operating Officer in 2016. Johnny brings a wealth of experience to the Group and his contribution has already been felt.

DIVIDEND

In line with the Group's strategy of returning cash to its shareholders, the Company paid a dividend of 5 US cents per share (US\$6.9 million) and a special dividend of 3.5 US cents per share (US\$4.9 million) in June 2016 in respect of the 2015 financial year.

Following a careful review of the 2016 results, the Board has decided to focus on cash preservation and is prudently recommending, despite the Group's dividend policy, that no dividend is paid in respect of the 2016 financial year. The Group will continue to focus on capital management discipline and cost control at the operations to return to a position to recommend dividend payments to shareholders in the future.

OUTLOOK

The medium to long-term outlook for diamond demand is expected to remain favourable.

The strategic focus of the Group will remain on creating value by focusing on mining and selling diamonds efficiently and responsibly. Through disciplined execution of its core strategy, the Group is well positioned to maximise shareholder returns and remains confident in its ability to continue delivering returns to shareholders.

APPRECIATION AND FAREWELL

I will be stepping down at this year's Annual General Meeting (AGM), following 10 years as Chairman of Gem Diamonds. It has been an honour to serve this dynamic business for almost a decade. I wish my successor well and know that they join a proud organisation with strong leadership and values. I would like to acknowledge the hard work and commitment of the entire Gem Diamonds team. To my fellow Board members – thank you for your insight and leadership throughout the year. To the host governments, thank you for your continued support. Finally, thank you to the Group's shareholders. Gem Diamonds remains committed to delivering value to you in the year ahead.

Roger Davis
Non-executive Chairman

14 March 2017

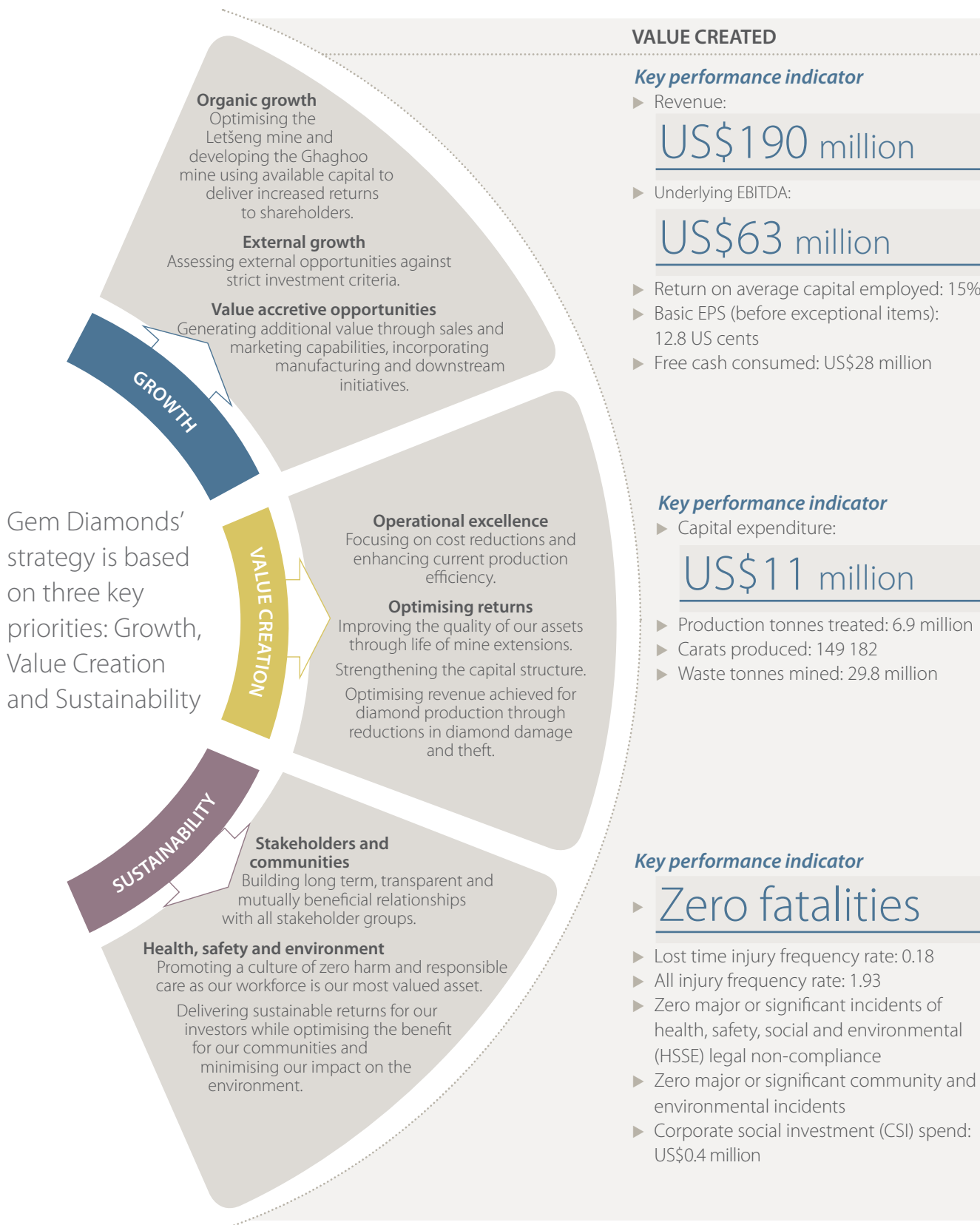


Letšeng Diamond Discovery Centre, opened on 6 May 2016 in Maseru, Lesotho

Our strategy

How we create value

We remain focused on primarily extracting diamonds through mining. To complement this, we continue our attention further along the diamond value chain through our sales, marketing and manufacturing activities. Our strategy is based on three key priorities – growth, value creation and sustainability. Our overarching objective is to deliver sustainable returns for our investors while optimising the benefit for our communities and minimising our impact on the environment. We are confident that our strategy is the right long-term path for Gem Diamonds.



Our investment case

What we offer

Gem Diamonds, through its unique Letšeng mine, produces the highest US\$ per carat diamonds in the world, which are sought after by high-end diamond jewellers. This competitive advantage has enabled the Company in becoming a regular dividend paying company with a strong balance sheet, making it an attractive investment proposition.

WHAT WE DO

Identifying resource

1

Identifying, evaluating and developing diamond deposits that are potentially valuable

Planning and developing reserves

2

Identifying the valuable, economical and technically feasible part of the resource to be mined

Mining

3

Mining in both open-pit and underground mines as efficiently as possible and minimising the impact on our employees, environment and PACs

Processing

4

Increasing recoveries and improve finished product quality through initiatives of reducing diamond damage and theft and increasing liberation of diamonds

Sales, marketing and manufacturing

5

Analysing and mapping our exceptional diamonds to understand and achieve highest rough value through multiple selling channels. Manufacturing of select high-value rough diamonds, capturing additional value through polished sales

WHAT WE OFFER

OUR ASSETS

Letšeng, our core asset, produces the highest value US\$ per carat diamonds in the world. We implement innovative solutions to further enhance this value.

The 20.5 million carats contained within the Ghaghoo resource offer an opportunity to further enhance the Gem Diamonds investment proposition.

SHAREHOLDER RETURN

We are committed to sustaining shareholder value through the implementation of appropriate dividend policies and we aim to pay dividends annually.

STRONG BALANCE SHEET MANAGEMENT

We focus on maximising revenue from our core assets through enhancing operational efficiencies and investing in low capital, short payback projects.

Cash generation and capital discipline have positioned us well for sustainable growth into the long term.

CORPORATE SOCIAL RESPONSIBILITY

Maintaining safe operations and minimising social and environmental impact, safeguards our social licence to operate and further promotes our corporate brand.

ROBUST CORPORATE GOVERNANCE

We are committed to the pursuit of best practice in governance principles. We hold to the fact that effective corporate governance is essential to securing the Group's long-term success and viability.

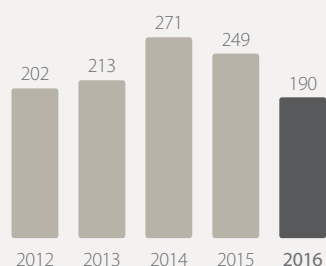
Focused risk management is a core element of our business. Our Board has overall accountability for ensuring that risks are effectively managed, reviewed and continually assessed across the Group.

Key performance indicators

Key performance indicators (KPIs) are used to assess the performance of the Group against its strategy. These indicators are monitored continually to effectively evaluate the performance of the Group over the short, medium and long term.

GROWTH

Revenue (US\$ million)



Definition

Revenue represents the value of goods sold during the year (both rough and polished) and measures the level of operating activity and growth of the business. Revenue for the year is as reported in the consolidated income statement and excludes revenue achieved by Ghaghoo on the basis that the mine had not reached full commercial production for accounting purposes by the end of the year.

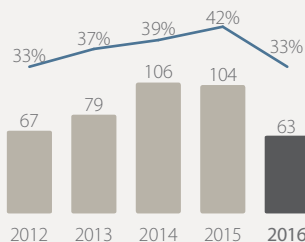
Commentary

The Group remains committed to maximising the value achieved on rough and polished diamond sales. Group revenue decreased by 24% compared to 2015 largely due to the paucity of exceptional large diamonds recovered at Letšeng which significantly impacted the overall US\$ per carat realised and overall revenue.

Ghaghoo concluded three sales during the year, generating US\$7.2 million (2015: US\$14.4 million) which is not included in Group revenue.

Total sales for the year including Ghaghoo was US\$197.2 million.

Underlying EBITDA (US\$ million)/ Underlying EBITDA margin (%)



Definition

Underlying EBITDA means earnings before interest, tax, depreciation and amortisation. It excludes share-based payments, other income, foreign exchange differences and exceptional items.

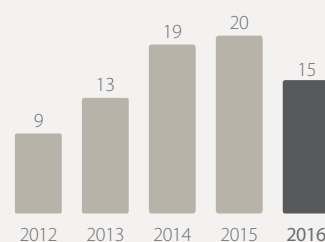
Underlying EBITDA margin is calculated as underlying EBITDA as a percentage of revenue. Both these indicators provide a measure of the operating profitability of the business. Refer to Note 3, Operating profit, in the financial statements for the calculation of underlying EBITDA.

Commentary

Underlying EBITDA of US\$62.8 million is 39% lower than 2015 reflecting the impact of lower Group revenue, partly mitigated by the positive impact on the translation of the local costs into US dollars driven by the overall weakening of the local currencies against the US dollar. This resulted in an underlying EBITDA margin of 33%.

Underlying EBITDA does not include any results from Ghaghoo due to the mine not having reached full commercial production.

Return on average capital employed (ROACE) (%)



Definition

ROACE is a pre-tax measure of the efficiency with which the Group generates operating profits from its capital. ROACE is calculated as underlying EBITDA (as per Note 3, Operating profit, in the financial statements) less depreciation and amortisation divided by average capital employed (being total equity and non-current liabilities per the consolidated statement of financial position).

Commentary

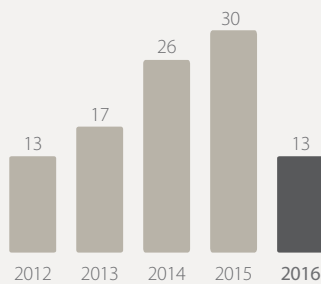
Pre-tax ROACE achieved 15%, mainly driven by lower Group revenue. Prior years' ROACE is as reported at that point in time and includes all operations in existence in those relevant years. ROACE is calculated after taking into account the impairment of assets of US\$172.9 million, mainly relating to Ghaghoo being placed on care and maintenance.



KPIs that are used as a measure in the incentive arrangements for the remuneration of executives are identified with this symbol: 

VALUE CREATION

Basic earnings per share (EPS) (US cents)



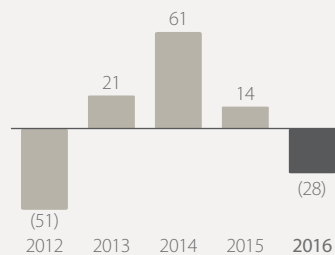
Definition

Basic EPS represents profit attributable to equity shareholders and is stated before exceptional items and after non-controlling interest. This is a measure of profitability of the Group taking into account changes in the equity structure. EPS is calculated as reported in the consolidated income statement and in accordance with Note 8, Earnings per share, in the financial statements.

Commentary

Basic EPS of 12.80 US cents per share is indicative of the lower earnings achieved. Basic EPS including exceptional items was a loss per share of 114.90 US cents, driven by the non-cash Ghaghoo asset impairment charge. There was no significant change in the capital structure of the Group.

Free cash generated (US\$ million)



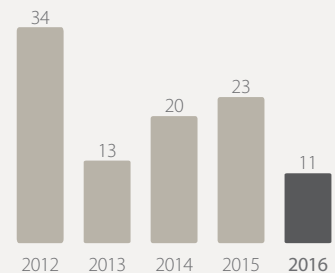
Definition

Free cash generated represents net cash flows before financing activities and investing activities in expansion projects. This measures the cash-generating capability of the Group to fund future growth. Free cash generated is reflected in the statement of cash flows and is determined by cash flows from operating activities of US\$70.7 million less sustaining capital of US\$10.8 million, cash invested in Ghaghoo development and commissioning costs of US\$18.0 million and waste cash costs incurred at Letšeng of US\$70.4 million.

Commentary

While the Company remains committed to generating and returning cash to shareholders with capital and cash management discipline remaining a priority, the lower revenue achieved during the year at Letšeng and Ghaghoo negatively impacted the Group's cash balance. The Group utilised existing cash resources and cash flows from operations to fund existing capital commitments and operating costs. The Group ended the year with US\$3.8 million cash net of drawn down facilities of US\$27.0 million after paying a dividend of US\$11.8 million during the year in relation to the 2015 results.

Capital expenditure (US\$ million)



Definition

Capital expenditure represents the amount invested in the Group's organic growth plans. Capital expenditure is reflected in the statement of cash flows as purchases of property, plant and equipment and includes expansion and sustaining capital.

Commentary

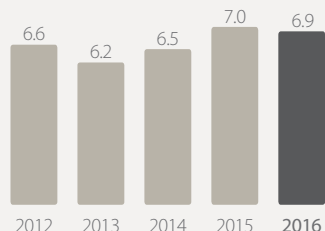
The Group invested US\$10.8 million into sustaining capital expenditure which mainly comprised of US\$7.6 million at Letšeng and US\$2.6 million at Ghaghoo. At Letšeng, capital allocation was focused on stay in business capital with early stage investment in projects that will deliver future benefits.



Key performance indicators continued

VALUE CREATION

Ore tonnes treated (millions)



Definition

The production profile sets out the tonnes treated at Letšeng and Ghaghoo.



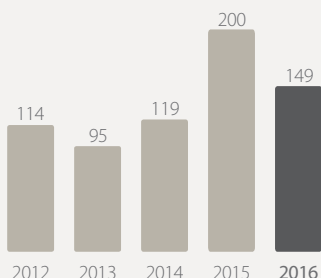
Commentary

The current year production represents 6.7 million tonnes treated at Letšeng and 0.2 million tonnes treated at Ghaghoo.

Ore tonnes treated at Letšeng were similar to those treated in 2015. The additional expected tonnes of 250 000 were not realised due to power outages caused by a severe snow storm experienced in July and August which resulted in all treatment plants running at reduced capacity for a period of 17 days.

Ghaghoo operated at a reduced production rate during the year, following the decision to downsize the operation.

Carats recovered (thousands)



Definition

The carats recovered profile sets out the carats recovered by Letšeng and Ghaghoo.



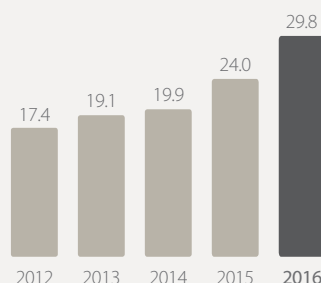
Commentary

Letšeng and Ghaghoo recovered 108 206 (2015: 108 579) and 40 976 (2015: 91 499) carats, respectively.

Letšeng's production was similar to 2015, with 108 206 carats recovered at a grade of 1.63 carats per hundred tonnes (cpht), in line with the expected reserve grade, at a reserve mine call factor of 101%. Production was hindered due to the extreme weather conditions experienced.

Carats recovered at Ghaghoo were 55% lower than 2015 due to lower volumes of ore tonnes treated. As mining moved towards the centre of the ore body additional basalt diluted kimberlite was mined and this resulted in a lower recovered grade than anticipated.

Waste tonnes mined (millions)



Definition

The waste tonnes mined profile sets out the waste tonnes mined by Letšeng.

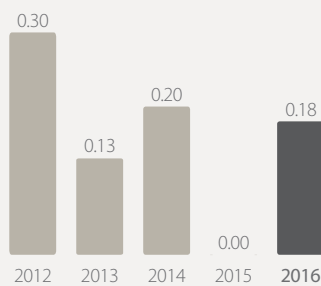


Commentary

The planned increase in mining production progressed during the year, with a 24% increase in waste mining in support of increasing the contribution of the higher-value Satellite pipe ore. Waste mined was also negatively impacted by the inclement weather conditions, as access to the pits was unattainable.

SUSTAINABILITY

Lost time injury frequency rate (LTIFR)



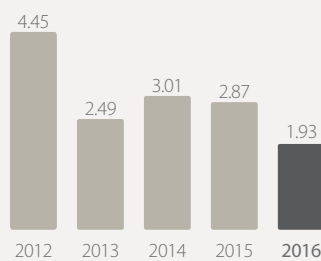
Definition

The LTIFR provides a measure of the safety performance of the Group, including partners and contractors. The LTIFR is measured on the reported LTI statistics for all of Gem Diamonds' companies and sub-contractors, expressed as a frequency rate per 200 000 man hours. Prior year rates include all operations in existence at that period.

Commentary

The Group recorded five LTIs during 2016, two at Letšeng and three at Ghaghoo. As a result, the LTIFR for the year was 0.18, above the internal target of zero harm.

All injury frequency rate (AIFR)



Definition

The AIFR is another measure of the safety performance of the Group. The AIFR is calculated based on all reported injuries including minor injuries, medical treatment cases, restricted work injuries and LTIs of all Gem Diamonds' companies and sub-contractors, and is expressed as a frequency rate per 200 000 man hours. Prior year rates include all operations in existence at that period.

Commentary

The AIFR decreased to 1.93 in 2016 and is the lowest rate achieved in the history of the Group. This reflects the decrease in total injuries across the Group as a result of proactive safety management.



Zero fatalities



Zero major or significant community incidents



Zero major or significant environmental incidents



Invested US\$0.4 million in corporate social projects during 2016 and continued to build positive relationships with stakeholders and project-affected communities

Principal risks and uncertainties

How we approach risk

The Group is exposed to a number of risks and uncertainties that could have a material impact on its performance and long-term growth. The effective identification, management and mitigation of these risks and uncertainties is a core focus of the Group as they are key to achieving the Company’s strategic objectives.

Central to Gem Diamonds’ approach to risk management is having the right Board and Senior Management team in place, with such members combining extensive experience in diamond mining, corporate governance, assurance management and knowledge of the local operating conditions in Lesotho and Botswana.

The Board is accountable for risk management, assisted primarily by the Audit and HSSE Committees, who together identify and assess change in risk exposure, along with the potential financial and non-financial impacts and likelihood of occurrence.

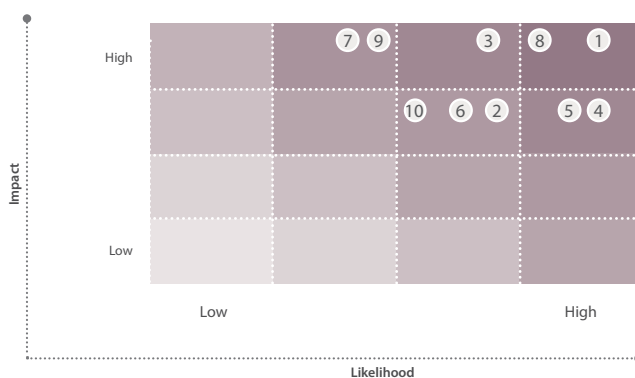
The Company is continually strengthening its risk management processes to provide informed assurance to the Board to assess current objectives. The Group internal audit function carries out the risk-based audit plan approved by the Audit Committee, to evaluate the effectiveness and contribute to the improvement of risk management controls and governance processes.

Following the extreme weather conditions experienced at Letšeng during the year, the mitigation measures relating to business continuity were reviewed and further strengthened where necessary.

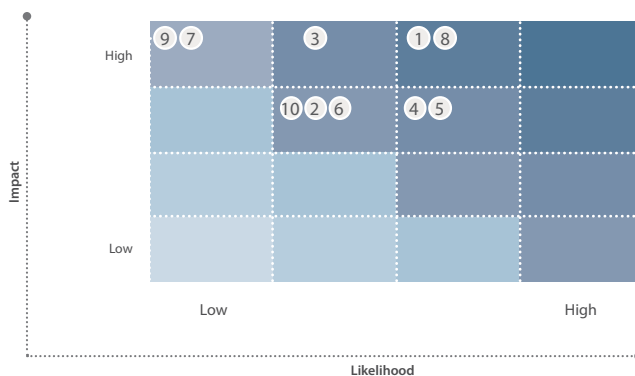
Given the long-term nature of the Group’s mining operations, risks are unlikely to alter significantly on a yearly basis; however, inevitably the level of risk and the Group’s risk appetite could change. The Board and its Committees have identified the following key risks which have been set out in no order of priority. This is not an exhaustive list, but rather a list of the most material risks facing the Group. The impact of these risks, individually or collectively, could potentially affect the ability of the Group to operate profitably and generate positive cash flows in the medium to long term. The risks are actively monitored and managed as detailed on the following pages.

The KPIs, which are grouped into the growth, value creation and sustainability of the Group’s strategy on pages 12 to 13 are linked to each risk.

INHERENT RISK (PRE MITIGATING CONTROLS)



RESIDUAL RISK (POST MITIGATING CONTROLS)



Movement in residual risk

1	Rough diamond demand and prices	↑
2	Mineral resource risk	↑
3	A major production interruption	↔
4	Diamond theft	↔
5	Diamond damage	↔
6	Expansion and growth	↑
7	HSSE-related risks	↔
8	Country and political risks	↔
9	Attracting and retaining appropriate skills	↓
10	Currency volatility	↑

↔ Unchanged ↑ Increased ↓ Decreased

Description and impact

Mitigation

2016 actions and outcomes

KPIs affected



MARKET RISKS

1. ROUGH DIAMOND DEMAND AND PRICES

- ▶ Numerous factors beyond the control of the Group may affect the price and demand for diamonds.
- ▶ These factors include international economic and political trends; projected supply from existing mines; supply and timing of production from new mines; and consumer trends.
- ▶ The volatility in the market can significantly impact the ability to generate cash flows and to fund operations and growth plans.

- ▶ Market conditions are continually monitored to identify trends that pose a threat or create opportunity for the Group.
- ▶ The Group has flexibility in its sales processes and the ability to reassess its capital projects and operational strategies considering existing market conditions to preserve cash balances.
- ▶ Strict treasury management procedures are in place to monitor cash and capital project expenditure.
- ▶ Revolving credit facilities are available during periods when cash constraints are experienced.

- ▶ Global macro-economic volatility and uncertainty and the cautious sentiment in the diamond market continued to strain the rough and polished diamond market during 2016.
- ▶ Letšeng's high-value diamonds continued to be in high demand and achieved firm prices.
- ▶ The price for Ghaghoo's more commercial production decreased by approximately 30% from that achieved at the beginning of 2015, and is anticipated to remain constrained due to projected increase in supply for these types of goods from new mines coming into production in 2017. The continued decline in Ghaghoo's prices prompted a review by management of the financial viability of the operation, and post year end, the decision was taken to place the operation on care and maintenance until such time that commencing full commercial production would make economic sense.

Growth Value creation

Principal risks and uncertainties continued

How we approach risk

Description and impact

Mitigation

2016 actions and outcomes

KPIs affected

OPERATIONAL RISKS

2. MINERAL RESOURCE RISK

- ▶ The Group's mineral resources influence the operational mine plans. Uncertainty or underperformance of mineral resources could affect the Group's ability to operate profitably.
- ▶ Limited knowledge of the resource could lead to an inability to forecast or plan accurately or optimally, and lead to financial risk.
- ▶ With Letšeng being the world's lowest grade operating kimberlite mine, the risk of resource underperformance is elevated.

- ▶ Various bulk sampling programmes, combined with geological mapping and modelling methods significantly improve the Group's understanding of and confidence in the mineral resources and assist in optimising the mining thereof.

- ▶ At Letšeng, ahead-of-face drilling and discrete production sampling programmes initiated in previous years continued in 2016 to better define the orebody. In addition, micro-diamond sample analysis which aims to predict grades at depth was also conducted. The outcomes of these programmes will be used to update resource models. A drilling programme was approved in 2016 and will commence during Q1 2017.
- ▶ During 2016, fewer exceptional large, high-value diamonds were recovered at Letšeng. Following a detailed review of the resource and operational processes, it was considered that the absence of these type of recoveries is due to the normal statistical short-term variability of the resource and is expected to revert to normal recovery levels.
- ▶ Resource development at Ghaghoo was limited to mapping of the geology for the underground tunnels. Data obtained from mining activities was analysed to further understand the resource and develop the value in the reserve. While the asset is on care and maintenance, further analysis of data will be undertaken to improve the knowledge of the resource.

**Growth
Value creation**



Description and impact	Mitigation	2016 actions and outcomes	KPIs affected
OPERATIONAL RISKS (continued)			
<p>3. A MAJOR PRODUCTION INTERRUPTION</p> <ul style="list-style-type: none"> ▶ The Group may experience material mine and/or plant shutdowns or periods of decreased production due to numerous events. Any such event could negatively impact the Group's operations and its profitability and cash flows. 	<ul style="list-style-type: none"> ▶ The Group continually reviews the likelihood and consequence of various possible events and ensures that the appropriate management controls, processes, and business continuity plans are in place to immediately mitigate risk. 	<ul style="list-style-type: none"> ▶ During 2016, excessive snow fall and severe winds were experienced in Lesotho, limiting access to Letšeng and damaging the Lesotho Electricity Company's infrastructure, impacting power to the operation. Backup generators at the mine were used to mitigate the impact, allowing treatment plants to continue to operate, albeit at reduced rates. ▶ The two major production interruption risks at Ghaghoo of wet underground conditions and single access tunnel to the underground, continued to be managed through water management strategies and regular monitoring of the condition of the access tunnel respectively. 	<p>Growth Value creation Sustainability</p>
<p>4. DIAMOND THEFT</p> <ul style="list-style-type: none"> ▶ Theft is an inherent risk factor in the diamond industry. ▶ At Letšeng, because of the frequency of high-value diamonds and the associated low grade, theft can have a material impact on Group cash flow. 	<ul style="list-style-type: none"> ▶ Security measures are constantly reviewed and implemented to minimise this risk. ▶ State-of-the-art security infrastructure and technologies are invested in and supported through additional surveillance processes. 	<ul style="list-style-type: none"> ▶ The Coarse Recovery Plant at Letšeng, with additional security features, continued to be optimised during the year. ▶ Three independent audits of the security systems were conducted, the outcomes of which resulted in a series of findings that provided opportunity to further improve the security processes at Letšeng. 	<p>Growth</p>



Principal risks and uncertainties continued

How we approach risk

Description and impact	Mitigation	2016 actions and outcomes	KPIs affected
OPERATIONAL RISKS (continued)			
<p>5. DIAMOND DAMAGE</p> <ul style="list-style-type: none"> ▶ Letšeng's valuable Type II diamonds are highly susceptible to damage during the mining and recovery process. To reduce such damage creates a potential upside for the Group. 	<ul style="list-style-type: none"> ▶ Diamond damage is regularly monitored and analysed through studies and variance analyses. ▶ Opportunities to reduce damage through modifications to the mining and treatment process are identified for further investigation. 	<ul style="list-style-type: none"> ▶ During the year, five diamonds greater than 100 carats were recovered. ▶ Options are currently being assessed to further enhance recovery and reduce damage to the large-sized diamonds through a large-diamond specific recovery plant. 	<p>Growth Value creation</p>
<p>6. EXPANSION AND GROWTH</p> <ul style="list-style-type: none"> ▶ The Group's growth strategy is based on delivery of expansion projects, premised on various studies, cost trends and future market assumptions. In assessing the viability, cost and implementation of these projects, risks concerning cost overruns and/or delays may affect the implementation and execution thereof. 	<ul style="list-style-type: none"> ▶ Project governance structures have been applied to ensure that projects are monitored and risks managed at an appropriate level. ▶ Flexibility in the execution of projects allows the Group to react quickly to changes in market and operational conditions. 	<ul style="list-style-type: none"> ▶ At Letšeng a post-investment review was completed on the Plant 2 Phase 1 upgrade which proved that the project achieved its objective. ▶ In Q4 2016 projects aimed at maximising Letšeng's value commenced and included a revised life of mine plan, aimed at reducing waste tonnes mined and further enhancing cash flows, and the study of the benefits of developing a large-diamond specific recovery plant. ▶ Ghaghoo was downsized during 2016, necessitated by the challenging diamond market for the Ghaghoo production. Market and operational conditions worsened during the year necessitated the placing of Ghaghoo on care and maintenance post year end. The viability of this asset will be continually monitored to allow the Group to react to any positive market movements. 	<p>Growth Value creation</p>

Description and impact	Mitigation	2016 actions and outcomes	KPIs affected
OPERATIONAL RISKS (continued)			
<p>7. HSSE-RELATED RISKS</p> <ul style="list-style-type: none"> ▶ The risk that a major health, safety, social or environmental incident may occur is inherent in mining operations. ▶ These risks could impact the safety of employees, licence to operate, Company reputation and compliance with facility agreements. 	<ul style="list-style-type: none"> ▶ The Group has implemented appropriate HSSE policies which are subjected to a continuous improvement review. ▶ The Group actively participates and invests in corporate social initiatives for its PACs. 	<ul style="list-style-type: none"> ▶ The Group achieved a fatality-free year. ▶ Five LTIs were reported resulting in an LTIFR of 0.18 and AIFR of 1.93, being the lowest achieved to date in the history of the Group ▶ Ghaghoo maintained its four-star rating for the external HSSE audits. ▶ Letšeng retained its ISO14001 and ISO18001 certification. ▶ Corporate social investment into the Group's PACs continued during the year. 	<p>Sustainability</p>
<p>8. COUNTRY AND POLITICAL RISKS</p> <ul style="list-style-type: none"> ▶ The political environment of the various jurisdictions that the Group operates within may adversely impact its ability to operate effectively and profitably. Emerging market economies are generally subject to greater risks, including regulatory and political risk, and can be exposed to a rapidly changing environment. 	<ul style="list-style-type: none"> ▶ Changes to the political environment and regulatory developments are closely monitored. Where necessary, the Group engages in dialogue with relevant government representatives to build relationships and to remain well informed of all legal and regulatory developments impacting its operations. 	<ul style="list-style-type: none"> ▶ There were no strikes or lockouts during the year across the Group. ▶ In Lesotho, numerous initiatives in promoting in-country stakeholder relationships were undertaken during the year, including the successful establishment of the Lesotho Chamber of Mines which is chaired by a representative from Letšeng. ▶ There were no disruptions to operations following the retrenchment of employees after the downsizing of Ghaghoo. 	<p>Growth Sustainability</p>



Principal risks and uncertainties continued

How we approach risk

Description and impact	Mitigation	2016 actions and outcomes	KPIs affected
OPERATIONAL RISKS (continued)			
<p>9. ATTRACTING AND RETAINING APPROPRIATE SKILLS</p> <p>▶ The success of the Group's objectives and sustainable growth depends on its ability to attract and retain key suitably qualified and experienced personnel, especially in an environment and industry where skills shortages are prevalent and in jurisdictions where localisation policies exist.</p>	<p>▶ The Group regularly reviews human resources practices, which are designed to identify areas of skill shortages, and implements development programmes to mitigate such risks. In addition, these programmes are designed to attract, incentivise and retain individuals of the appropriate calibre through performance-based bonus schemes and long-term reward and retention schemes.</p>	<p>▶ Intensified efforts continued in the development of selected key employees through structured training and development programmes.</p> <p>▶ Extensive engagements with respective government departments are ongoing as part of the effort to implement efficient work permit processing and to develop plans for local employee upskilling.</p> <p>▶ Following engagement with the Government of Lesotho during the year a memorandum of understanding was signed post year end to expedite the issuing of work permits and facilitate the entry of expatriates.</p>	<p>Growth Value creation Sustainability</p>
FINANCIAL RISKS			
<p>10. CURRENCY VOLATILITY</p> <p>▶ The Group receives its revenue in US dollars, while its cost base is incurred in the local currency of the various countries within which the Group operates. The volatility of these currencies trading against the US dollar impacts the Group's profitability and cash.</p>	<p>▶ The impact of the exchange rates and fluctuations are closely monitored.</p> <p>▶ It is the Group's policy to hedge a portion of future diamond sales when weakness in the local currency reach levels where it would be appropriate. Such contracts are generally short term in nature.</p>	<p>▶ Local currencies in the jurisdictions in which the Group operates weakened against the US dollar during the first half of the year; however, the second half of the year saw significant strengthening of local currencies of Lesotho and Botswana against the US dollar. This has negatively impacted the Group's results which are translated into US dollars. Due to the volatility and uncertainty of the currency movements during the year, no hedges were entered into.</p>	<p>Growth Value creation</p>

Viability statement

In accordance with the revised UK Corporate Governance Code, the Directors have assessed the viability of the Group over a period significantly longer than 12 months from the approval of the financial statements. The Board concluded that the most relevant time period for consideration for this assessment is a three-year period from the approval of the financial statements, taking into account the Group's current position and the potential impact of the principal risks documented on pages 18 to 24 that could impact the viability of the Group. This period also coincides with the Group's business and strategic planning period, which is reviewed annually, led by the CEO and involving all relevant functions including operations, sales and marketing, financial, treasury and risk. The Board participates fully in the annual review process by means of structured board meetings and annual strategic sessions. A three-year period gives management and the Board sufficient and realistic visibility in the context of the industry environment of the Group.

At Letšeng, the Group's focus is on organic growth with particular emphasis on enhancing efficiencies and optimising expansion plans at the operation. At Ghaghoo, following the weak state of the diamond market for this category of diamonds, the decision has been taken to place the mine on care and maintenance with the objective of cash preservation and the option to bring the mine into commercial production should the diamond market improve for these goods.

For the purpose of assessing the Group's viability, the Directors focused their attention on the more critical principal risks categorised within the Market, Operational and Financial risks together with the likely effectiveness of the potential mitigations that management reasonably believes would be available to the Company over this period. Although the business and strategic plan reflects the Directors' best estimate of the future prospects of the Group, they have also tested the potential impact on the Group of a number of scenarios over and above those included in the plan, by quantifying their financial impact and overlaying this on the detailed financial forecasts in the plan.

The scenarios tested considered the Group's revenue, EBITDA, cash flows and other key financial ratios over the three-year period. Given that Letšeng experienced a paucity of larger high quality diamonds in 2016 impacting its revenue and cash flows, the scenarios tested included the impact of continued paucity of these diamonds over the three-year period. This paucity is considered to be due to the normal statistical short-term variability of the resource and would be expected to revert to normal recovery levels within this three-year period.

The scenarios tested included the compounding effect of:

- ▶ a decrease in forecast rough diamond prices from the expected reserve prices; and
- ▶ an appreciation of local currencies to the US dollar from expected market forecasts.

With the current net cash position of US\$3.8 million as at 31 December 2016 and available standby facilities of US\$53.3 million, the Group would be able to withstand the impact of these scenarios occurring over the three-year period, due to the cash-generating nature of the Group's core asset, Letšeng, and its flexibility in adjusting its operating plans within the normal course of business. Post year end, the US\$25.0 million Ghaghoo facility was settled out of available facilities at the Company level.

Based on their robust assessment of the principal risks, prospects and viability of the Group, the Board confirms that they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three-year period ending March 2020.

Market review

Despite another challenging year for the diamond industry, prices for the large, high-value rough production from Letšeng remained resilient during 2016.

THE GLOBAL ECONOMIC BACKDROP IN 2016

- ▶ Continuing macro-economic uncertainty
- ▶ Slow growth of the Chinese economy
- ▶ Demonetisation in India
- ▶ Positive economic trends in the USA
- ▶ Reported improvement in commodities markets

THE GLOBAL DIAMOND MARKET IN 2016

Global macro-economic volatility and uncertainty continued in 2016 and the sentiment in the diamond market remained cautious. The strengthening US dollar, slow growth in the Chinese economy, demonetisation in India, continued liquidity constraints and high levels of polished inventory (particularly in the manufacturing sector) continued to plague the diamond market during the year, placing downward pressure on both rough and polished diamond prices. Despite these challenges, the prices achieved for the large, high-value rough production from Letšeng remained firm.

Significant drivers of the diamond market during 2016 included:

▶ Stabilised demand and high inventory levels in China

Notwithstanding indications that the diamond market in China stabilised and showed signs of recovery during the year, reported inventory levels remained high. This continued to have a negative impact on the rough and polished diamond market.

▶ The continued US recovery

The economic recovery in the US continued in 2016. This positive trend is closely linked to spending on luxury goods, and had a positive impact on diamond sales in the US during the year. The US remains the largest consumer of polished diamonds, with an estimated 45% of world consumption. However, due to diamond sales being US dollar denominated, a stronger US dollar negatively impacted sales in non-US denominated countries.

▶ Liquidity and funding constraints

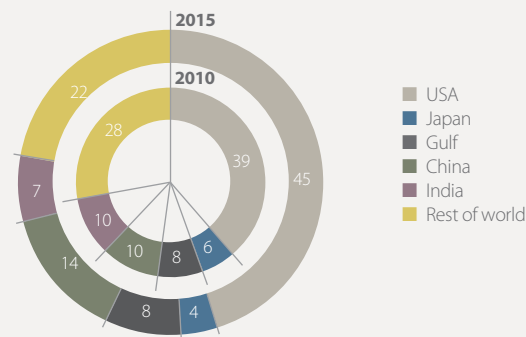
The demonetisation experienced in India in the latter part of 2016 and the withdrawal of Standard Chartered of its financing of the midstream of the diamond market in mid-2016, together with the closure of the Antwerp Diamond Bank at the end of 2014, and reported high levels of inventory, precipitated the continued liquidity and midstream working capital funding constraints experienced by the diamond market in 2016. Positively, several banks including ABN AMRO, the State Bank of India and more

recently banks in the United Arab Emirates continue to provide funding to the diamond industry and in particular, the midstream diamantaires.

▶ High levels of polished inventory

The reported slowdown in the demand for polished diamonds seen in 2016 was mainly a result of slow growth in China; lower than expected demand in the US (notwithstanding its reported economic recovery); and a delay in expected growth in diamond jewellery demand in India. This resulted in high levels of polished inventory in the midstream and retail sector of the diamond pipeline, negatively impacting the diamond market as the diamantaires traded their polished stock at lower margins.

Share of polished diamond demand by value (%)



Source: De Beers analysis based on proprietary retail and consumer research and on publicly available statistics.

Letšeng average price achieved
US\$1 695* per carat

Ghaghoo average price achieved
US\$152 per carat

Estimated global average
US\$109 per carat

* Includes carats extracted for polishing at rough valuation.

GEM DIAMONDS' MARKET POSITION

Although not immune to these macro-influences, the large, high-value diamond market remained resilient during the year. Prices achieved for Letšeng's large, high-value diamonds ensured that the mine retained its standing as the highest average dollar per carat kimberlite diamond producer in the world. The Letšeng mine places the Group at the top end of the diamond market in terms of the size and quality of its large diamond production, with its greater than 10.8 carat diamonds accounting for approximately 75% of its value in 2016.

The Group's Ghaghoo mine in Botswana produces diamonds of a more commercial size, quality and colour, which, although diversifying the production of the Group, was negatively impacted by the challenging diamond market experienced in 2016.

MEDIUM- TO LONG-TERM OUTLOOK

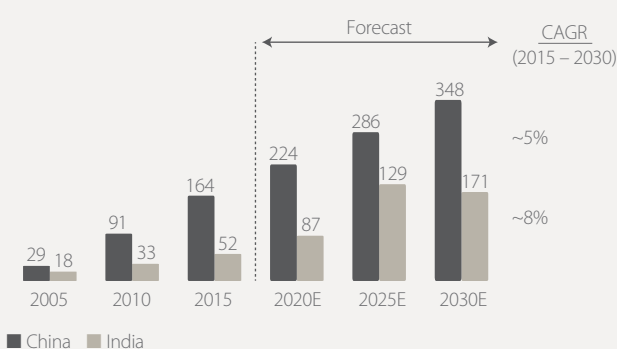
Demand for rough and polished diamonds is expected to outstrip supply in the medium to long term despite the current market conditions. The medium to long-term outlook for the diamond demand/supply fundamentals are expected to remain favourable given the expected rising consumer demand in developed and developing markets contrasted with declining supply forecast in the medium to long term.

Global demand trends

Diamond demand is expected to continue to grow in real value terms due to:

- ▶ The continued recovery in the US, the major diamond market.
- ▶ The growing international trends to use diamonds across a wider range of luxury goods, including jewellery, watches, accessories and digital devices.
- ▶ The growing middle and upper classes and the continued urbanisation in emerging economies – especially in India and China.
- ▶ The continued growth in the number of high-net-worth individuals worldwide.

Middle class in China and India (millions of households)



Note: The middle class in India includes households with an annual disposable real income of more than US\$10 000; the middle class in China (including Hong Kong) includes households with an annual disposable real income exceeding US\$15 000.

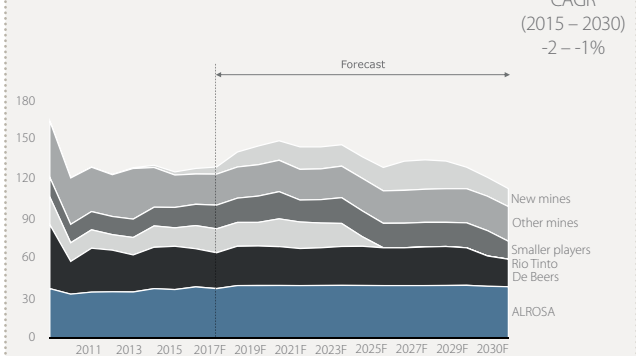
Sources: Euromonitor; Bain analysis

Global supply trends

The ageing and depletion of existing mines will steadily decrease the global diamond supply which will be marginally offset by limited additional supply from new mines in the short to medium term:

- ▶ Rough diamond production has declined considerably since peaking in 2005 and is yet to recover to the pre-global financial crisis levels of approximately 168 million carats per annum.
- ▶ Annual global diamond production is currently in the region of 128 million carats and with the introduction of several new mines, is expected to peak near 150 million carats in the next three to four years. Thereafter a steady decrease in supply from 2021 reduces annual production to around 110 million carats by 2030¹.
- ▶ The projected supply from new mines is expected to add an additional 26 million carats a year until 2026 and thereafter output from these mines is expected to decrease to around 16 million carats by 2030. The additional supply from these new mines is not expected to compensate for the expected growth in demand during the same period.

Rough diamond supply (million carats)



¹ Bain and Company: The Global Diamond Industry 2016.

LOOKING AHEAD

In the short term, the reported high levels of polished inventory and the downward pressure on both rough and polished prices in the diamond market remains a challenge. However, it is expected that the prices for Letšeng's large, high-value production will remain resilient in the short, medium and long term.

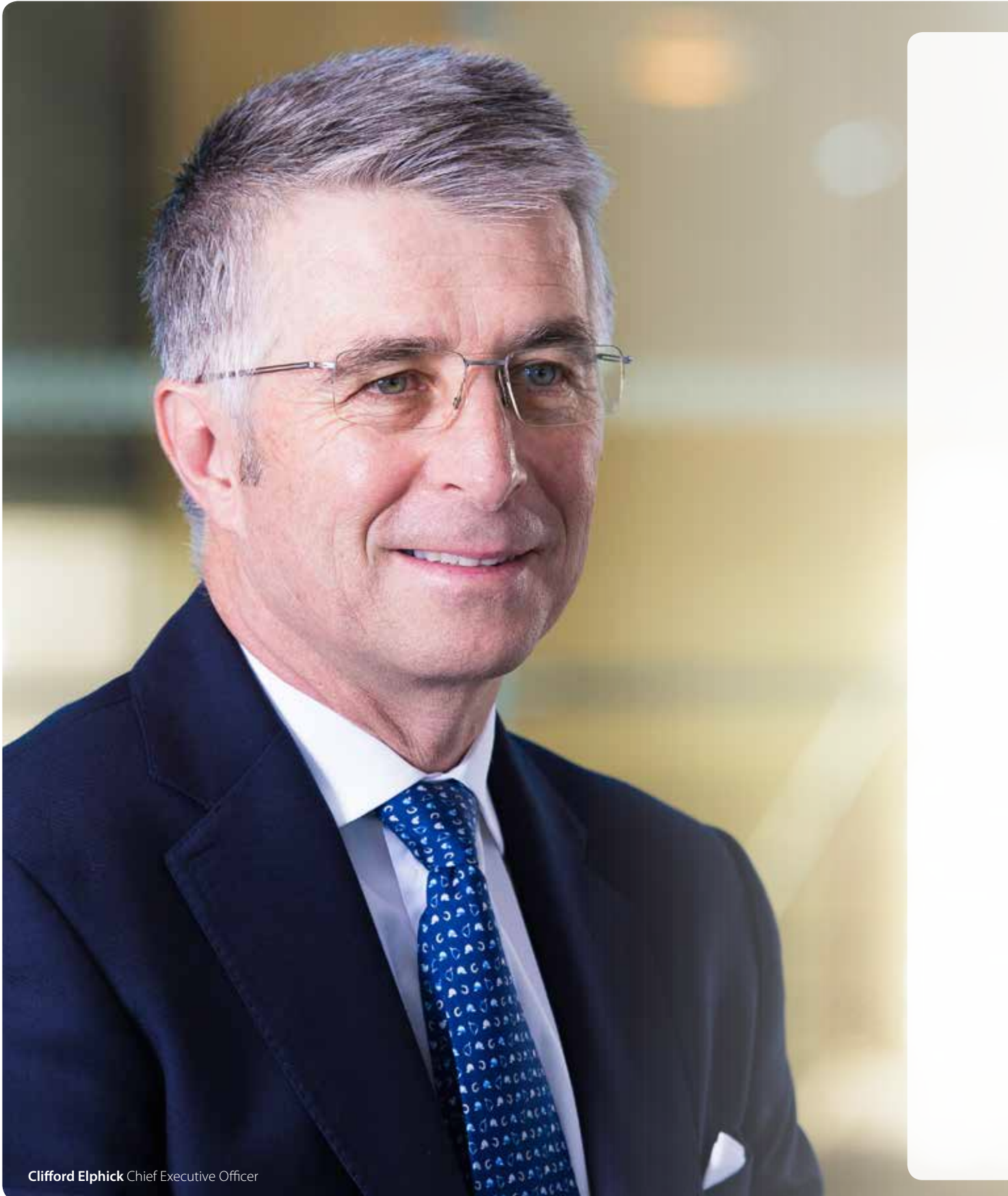




Management and operating review

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Q & A with the Chief Executive



Clifford Elphick Chief Executive Officer

Q: Reflecting on 2016, how would you characterise Gem Diamonds' financial year?

A: Simply put, the year was challenging for both Letšeng and Ghaghoo.

At Letšeng, despite a good operational performance and robust demand for its production, the decline in the number of large special diamonds recovered impacted on the average price achieved per carat for the year. On the other end of the diamond spectrum, the depressed market for smaller-sized diamonds continued to place pressure on the prices obtained from our Ghaghoo operation's sales.

The Group's financial results were adversely impacted by these lower effective prices, resulting in an EBITDA of US\$63 million for the year, 39% lower than in 2015.

Q: 2016 was clearly a challenging year. Focusing on Letšeng, what were the highlights for the year?

A: Operationally, Letšeng had a satisfactory year with all production metrics achieved within plan and guidance.

In 2015 the life of mine plan continued to evolve, the implementation of which was successful in its objective of contributing additional higher-value Satellite pipe ore to the processing plants.

During the period, a post-investment review on the Plant 2 Phase 1 upgrade, completed in 2015, showed that the plant capability had improved by 12%, in line with the project expectations. The impact of the severe weather experienced during the year offset this improved plant capability, however, we expect the full benefit of this uplift to be evident in 2017 and future years.

While, as I mentioned, the number of exceptional diamonds recovered was lower than in prior years, an 11.8 carat pink diamond and a 160.2 carat Type II white diamond were recovered. These two diamonds, respectively, represent the highest US\$ per carat price achieved as well as the largest diamond recovered for 2016.

The pink diamond was sold for US\$187 700 per carat – making it the third highest price per carat achieved for a single Letšeng diamond. The 160.2 carat Type II white diamond was sold into a partnership arrangement, where Gem Diamonds will participate in additional final polished margin.

Q: Conversely, what were the main challenges the Letšeng operation faced during 2016?

A: The robust operational performance of the mine is given further credence when you take into consideration the challenges presented by factors entirely outside of our control. In late July, extreme weather conditions were experienced across the Maluti Mountains in Lesotho where the mine is located, with excessive snowfall and severe winds limiting access to the mine and damaging the national grid power supply to the mine. Because of the setbacks that resulted from the severe weather, we revised our targets downwards. During this time, Letšeng provided accommodation and food to approximately 250 local people who were at risk, demonstrating the sense of community of the Letšeng team.

Unfortunately, while the mine was able to achieve its revised operational objectives, the lower than expected recovery frequency of exceptional, large diamonds nevertheless had a significant negative impact on our financial results. The lower revenue achieved for the year is a direct consequence of this.

Q & A with the Chief Executive continued

Q: Is there any concern that the low recovery rate of exceptional diamonds is indicative of more than simply a poor year?

A: No, I don't believe that's the case. Following a detailed review of the resource and operational processes by our geology team, we are confident that, as was the case in 2012 and 2013, the lower recovery rate is simply due to the normal statistical short-term variability of the resource. Letšeng is well known for its recovery of these exceptional diamonds and we expect this trend to continue.

Meanwhile, we are assessing options to further enhance recovery and reduce damage to these diamonds through a large-diamond specific recovery plant. As part of the Group's annual planning cycle, a review of the Letšeng mine plan was completed in Q1 2017. This mine plan further optimises the waste mining profile, which in turn will improve cash flow.

Q: The Ghaghoo operation is facing considerable headwinds. Please describe the performance and prospects for the operation?

A: I think it's important to understand that the challenges are predominantly due to market conditions. The market for small, commercial diamonds remains constrained. At the start of 2016, we announced the decision to downsize our Ghaghoo operation owing to the underperforming smaller-sized diamond market. The actions required to reduce tonnage at Ghaghoo were completed in 2016 and the operational improvements progressed well. Mill modifications yielded positive results with increased and improved diamond liberation. Furthermore, the focus on cost discipline resulted in reduced operating costs. There have also been encouraging recoveries of larger diamonds as mining moves into the undiluted portions of kimberlite ore – demonstrating the potential of the mine.

Despite the steps taken, ongoing development of the mine in the near term has been reviewed. Taking into consideration the continued weakness in the market for Ghaghoo's diamonds, which continued to decline from US\$210 to US\$142 per carat in prices achieved, and which we expect to be further exacerbated by the increase in supply from three new mines entering this particular category of diamond market in February 2017, the Group has decided to place the Ghaghoo mine on care and maintenance until conditions improve. This has led to us recognising a non-cash impairment charge of US\$170.8 million in this year's results.

A decision to place a mine on care and maintenance is a very difficult one based on the impact it has on the people that we employ at the mine. I would like to acknowledge and thank the entire team in Botswana for their tremendous effort and hard work to bring this mine into operation. The 20.5 million carats contained in the mine body will be mined when prices recover and the operation can be economically justified.

Q: Gem Diamonds is committed to maximising the profits received from its diamonds. How does the Group do this?

A: It starts with a focus on operational targets to achieve the maximum value from our production, balanced with ongoing cost discipline to maximise profits. Beyond a focus on operational efficiency, we are always looking for ways to create additional value. This means limiting diamond damage as well as continually investing in downstream activities, such as selecting certain high-value rough diamonds for cutting and polishing if they do not achieve reserve prices which have been set on competitive tender. This, of course, is done through our own facilities in Antwerp or by partnership arrangements. This has paid off and offered the Group added resilience in the face of the challenges experienced.

Q: How have challenges of 2016 impacted the Group's balance sheet strength?

A: We ended 2015 in a strong financial position underpinned by strong cash generation from Letšeng and prudent capital management over the past few years. While the cash resources were depleted in 2016 because of the challenges faced during the year, the Group still ended the year in a net cash position, demonstrating the strength of our balance sheet, which was bolstered by previously implemented revolving credit facilities.

Q: Safety is an ongoing priority. How does the Group ensure safety remains top of mind?

A: Behaviour-based safety forms the cornerstone of our health and safety strategy. We regularly engage with employees to better understand our operational processes, in that way, we become more efficient and improve the working environment. Another way we prioritise the safety and well-being of our employees is through our thorough induction procedure and the ongoing daily monitoring and reporting of safety statistics.

These systems continue to bear fruit and I'm pleased to report a fatality-free year, for the second consecutive year. Regrettably, five lost time injuries occurred. Continued emphasis on improving safety remains a focus in striving towards our goal of zero harm.

Q: The Group operations are set in unique locations. How does Gem Diamonds manage and minimise its environmental impacts?

A: We understand that our operations are located in sensitive ecosystems, rich in biodiversity. It is, therefore, imperative that we manage our environmental impacts with a high degree of operating discipline throughout the lifecycle of the mining operations. During 2016, our environmental teams continued to monitor the Group's ongoing compliance and pursued innovative ways of addressing environmental challenges. We are happy to report that for the eighth consecutive year, no major environmental incidents have occurred across the Group.

Q: What is Gem Diamonds' approach to social development?

A: We are committed to contributing positively to the economies in which we operate and to supporting the sustainable development of the communities we directly impact through our operations. We do so through the payment of taxes and royalties, as well as through the development and implementation of appropriate, sustainable corporate social investment projects.

At Letšeng, corporate social projects are implemented in three-year cycles based on needs identified in the community through an in-depth needs analysis. For instance, the Botha-Bothe vegetable project, which commenced in 2015, continued to make a positive and sustainable contribution to community upliftment during the year. Ghaghoo continued to contribute towards initiatives aimed at improving community access to medical services and the upgrading of educational infrastructure.

Q: Looking ahead, what are the prospects and focus for the Group in 2017?

A: We believe the long-term fundamentals for the diamond industry are strong. As a Group, our focus will be on replenishing cash and strengthening our balance sheet. The emphasis for 2017 and beyond remains on maximising our core asset – Letšeng. We are committed to reducing diamond damage and enhancing the mine plan to improve cash flow.

In trying times, it is the difficult decisions we take now that will stand us in good stead in the future. At Ghaghoo, we are focused on placing the asset on care and maintenance efficiently and as cost effectively as possible.

We remain confident about the future of Gem Diamonds and its strategic positioning to weather the current challenging commodity prices and to continue creating value for our shareholders and other stakeholders.

Q: Would you like to add anything in closing?

A: I would like to take this opportunity to thank our shareholders and stakeholders for their continued support. I also extend my sincere gratitude to the Board for their guidance and support throughout the year. A special thanks to our outgoing Chairman, Roger Davis – your commitment to driving Gem Diamonds forward has been instrumental in the Group's success over the years. We wish you well in your future endeavours. We are in the final stages of recruiting Roger's successor and look forward to updating the shareholders further, ahead of the 2017 AGM.

At the end of February 2017, the Letšeng Chief Executive Officer (CEO), Ms Mazvi Maharasoa, retired from the organisation after 10 years of diligent service. During her tenure, Mazvi has been instrumental in driving the successful growth strategy of the mine. Mazvi has also been an important role player in the establishment of the Lesotho Chamber of Mines. I would like to take this opportunity to thank Mazvi for her valued contribution to the Group's success.

Finally, thank you to all our employees – your hard work and faithful commitment to the success of Gem Diamonds continues to drive us forward.

Clifford Elphick
Chief Executive Officer

14 March 2017

Group financial performance



Michael Michael Chief Financial Officer

Balance sheet strength withstands tough operating and market conditions

The 2016 results were disappointing for the Group when compared to the results of previous years. Challenging market conditions impacting diamond prices, especially for the Ghaghoo type production, and operational headwinds at Letšeng with the lack of large, high-value diamond recoveries, had a significant impact on revenue, profit and cash. Although cash resources were reduced during the year, the Group still ended the year in a positive net cash position.

In response to the challenging operating environment and weak state of the market for the Ghaghoo type production in early 2016, the downsizing of the operation was actioned in Q1 2016. Although cost reductions were initiated and plant modifications implemented, these positive outcomes were not enough to support the operation, considering the continued depressed state of the market. With the last tender held in December 2016 achieving US\$142 per carat, down 11% from the first tender of the year, the Board made the decision to place the Ghaghoo operation on care and maintenance in February 2017 and an impairment charge of US\$170.8 million was recognised at year end.

Although the heavy snow storms and extreme weather experienced at Letšeng in July 2016 impacted the operation (losing 17 days of production), Letšeng achieved similar operational throughput to that of the previous year. However, the paucity of the larger high-value diamonds recovered in 2016, especially in the second half of the year, significantly impacted the overall US\$ per carat achieved. Letšeng achieved US\$1 695* per carat for 2016, with an average of US\$1 898* per carat achieved in H1 2016 and US\$1 480* per carat in H2 2016. The reduction in H2 2016 was driven further by the lower volume of the higher-value Satellite pipe material mined of 0.7 million tonnes compared to 1.0 million tonnes in H1 2016.

Gem Diamonds remains focused on cost discipline and its fundamental goal of extracting the maximum value from its resources for long-term shareholder value creation. In light of the current year's results and the reduced cash resources, the Board did not approve a dividend for the 2016 results. The Group will continue to focus on capital and cost discipline at the operations to remain in a position to recommend dividend payments to shareholders in the future.

REVENUE

The Group continued its objective of maximising the value achieved on rough and polished diamond sales. The Group's revenue is primarily derived from its two business activities, namely sales from its mining operations in Lesotho at Letšeng and Botswana at Ghaghoo, and additional margin generated from its rough diamond manufacturing operation in Belgium. The sales generated by Ghaghoo are not reflected in the Group's revenue figures for the current and prior years, but have been set off against operating and development costs capitalised to the carrying value of the development asset, as the mine did not reach full commercial production for accounting purposes by the end of the year.

Group revenue of US\$189.8 million in 2016 is 24% lower than that achieved in 2015. Letšeng achieved an average of US\$1 695* per carat from the sale of 108 945 carats, which was 26% lower than that achieved in 2015 of US\$2 299*. This lower US\$ per carat is largely the consequence of fewer high-quality +100 carat diamonds being recovered at Letšeng during the year.

Ghaghoo sold 47 266 carats during the year for US\$7.2 million, achieving an average of US\$152 per carat for the year compared to US\$162 per carat in 2015. This fall in prices emphasised the weak state of the diamond market for this category of diamonds.

The Group's manufacturing operation contributed additional revenue of US\$5.0 million, comprising US\$3.2 million polished margin and US\$1.8 million as a result of the effect on Group revenue of the movement in own manufactured closing inventory year on year.

* Includes carats extracted for polishing at rough valuation.

Group financial performance continued

SUMMARY FINANCIAL PERFORMANCE

US\$ million	Year ended 31 December 2016	Year ended 31 December 2015
Revenue	189.8	249.5
Royalty and selling costs	(17.2)	(21.9)
Cost of sales	(98.8)	(112.4)
Corporate expenses	(11.0)	(11.7)
Underlying EBITDA	62.8	103.5
Depreciation and amortisation	(10.4)	(10.4)
Other income	0.3	0.5
Share-based payments	(1.8)	(1.7)
Foreign exchange gain	1.7	7.0
Net finance (costs)/income	(0.2)	0.1
Profit before tax	52.4	99.0
Income tax	(20.0)	(31.6)
Profit after tax	32.4	67.4
Non-controlling interests	(14.7)	(25.6)
Attributable profit before exceptional items	17.7	41.8
(Loss)/profit from exceptional items	(176.5)	10.2
Attributable (loss)/profit after exceptional items	(158.8)	52.0
Basic EPS before exceptional items (US cents)	12.8	30.2

Royalties consist of an 8% levy paid to the Government of Lesotho and a 10% levy paid to the Botswana Department of Mines on the value of diamonds sold by Letšeng and Ghaghoo, respectively. The Botswana royalty costs were capitalised to the carrying value of the Ghaghoo development asset during the year. Diamond selling and marketing-related expenses are incurred by the Group sales and marketing operation in Belgium. During the year, royalties and selling costs decreased by 22% to US\$17.2 million, mainly driven by the reduction in revenue.

US\$ million	Year ended 31 December 2016	Year ended 31 December 2015
Group revenue summary		
Sales – rough	184.6	236.3
Sales – polished margin	3.2	3.8
Sales – other	0.2	0.6
Impact of movement in own manufactured inventory	1.8	8.8
Group revenue	189.8	249.5

OPERATIONAL EXPENSES

While revenue is generated in US dollars, the majority of operational expenses are incurred in the relevant local currency in the operational jurisdictions. The Lesotho loti (LSL) (pegged to the South African rand) and Botswana pula (BWP) were weaker against the US dollar during the first half of the year, thereafter strengthening in the second half of the year. The overall weaker currencies, positively impacted the Group's US dollar reported costs. Group cost of sales for the year was US\$98.8 million, compared to US\$112.4 million in the prior year, the majority of which was incurred at Letšeng.

Exchange rates	Year ended 31 December 2016	Year ended 31 December 2015	% change
LSL per US\$1.00			
Average exchange rate for the year	14.70	12.78	15
Year-end exchange rate	13.68	15.50	(12)
BWP per US\$1.00			
Average exchange rate for the year	10.89	10.14	7
Year-end exchange rate	10.68	11.25	(5)
US\$ per GBP1.00			
Average exchange rate for the year	1.35	1.53	(12)
Year-end exchange rate	1.24	1.47	(16)

LETŠENG MINING OPERATION

Operational excellence through proactive cost management and enhanced production efficiencies continues to be a key focus at Letšeng. Cost of sales for the year was US\$97.8 million, down 12% from US\$110.6 million in 2015, and includes waste stripping costs amortised of US\$34.7 million (2015: US\$47.2 million).

In line with the mine plan at Letšeng, 29.8 million tonnes of waste were mined, 24% higher than 2015. Ore tonnes treated were at similar levels to 2015, at 6.6 million tonnes, of which 1.7 million tonnes were sourced from the Satellite pipe, compared to 1.9 million tonnes in 2015. The Satellite to Main pipe ratio of 26:74 for the year was lower than the previous year of 29:71 and was partly influenced by the extreme weather conditions experienced in 2016. Carats recovered during the year of 108 206 remained at similar levels to that of the prior year of 108 579.

Letšeng costs	Year ended 31 December 2016	Year ended 31 December 2015
Unit costs US\$		
Direct cash cost (before waste) per tonne treated ¹	10.70	11.40
Operating cost per tonne treated ²	14.64	16.50
Waste cash cost per waste tonne mined	2.09	2.20
Unit costs (local currency)		
Direct cash cost (before waste) per tonne treated ¹	157.29	145.64
Operating cost per tonne treated ²	215.13	210.84
Waste cash cost per waste tonne mined	30.69	28.08
Other operating information (US\$ million)		
Waste cost capitalised	70.4	61.4
Waste stripping costs amortised	34.7	47.2

¹ Direct cash costs represent all operating cash costs, excluding royalty and selling costs.

² Operating costs include waste stripping cost amortised, inventory and ore stockpile adjustments, and excludes depreciation.

Total direct cash costs (before waste) at Letšeng, in local currency, were LSL1 045.4 million compared to LSL972.8 million in 2015. This resulted in a unit cost per tonne treated of LSL157.29 relative to the prior year of LSL145.64, representing an effective increase of 8%. The increase was driven by local inflation of 5%, the one-off costs associated with the unexpected weather incident in July and an increase in explosive costs due to revised drill patterns (as part of the initiative to address diamond damage). These costs also include those associated with Alluvial Ventures (the contractor operating a third plant at Letšeng) which are based on a percentage of revenue and had a 1.4% effect on the overall increase. In Q4 2016, a productivity improvement project with the aim of increasing mining efficiencies commenced. The initial costs thereof were incurred in 2016; the benefits of which will only be seen in 2017.

Operating costs per tonne treated of LSL215.13 were 2% higher than the prior year's cost of LSL210.84 per tonne treated. This slight increase is driven by lower waste amortisation costs during the year, due to the different waste to ore strip ratios for the particular ore processed. During the year, ore was sourced from four cuts (compared to two in 2015), two of which had not previously been mined. In addition, less ore tonnes were mined from the Satellite pipe, which carries a higher rate of amortisation charge. The amortisation charge attributable to the Satellite pipe ore accounted for 61% of the total waste stripping amortisation charge in 2016 (2015: 65%).

The increase in local currency waste cash costs per waste tonne mined of 9% was impacted by local country inflation, longer haul distances to mine the various waste cutbacks and the impact of the US dollar strength on the cost of the mining fleet. As part of the ramp-up of waste tonnes mined, additional larger fleet was brought into use in 2016 by the mining contractor.

GHAGHOO MINING OPERATION

Based on the market conditions at the end of 2015, a decision was made in Q1 2016 to downsize the Ghaghoo operation with the objective of reducing cash burn. Although most cost reduction initiatives were effected, the challenging underground mining conditions impacted the anticipated downsized volumes and grades achieved. This had a negative effect on the expected revenue and together with the further decrease in diamond prices, the overall net cash invested (net after sales) in the operation for the year was US\$14.4 million. This included one-off retrenchment costs and costs associated with the creation of the buffer zone to prevent sand ingress into the production levels following the sink hole that resulted from the caving in late 2015. Development costs of US\$3.6 million were invested in order to access both current and future ore producing tunnels and US\$2.6 million was invested in sustaining capital.

Based on the 32% reduction in prices achieved over the two-year period, the continued weak state of the diamond market for the Ghaghoo category of diamonds, the recent strengthening of the Botswana pula against the US dollar and with the Group's focus on profitable production, Ghaghoo was placed on care and maintenance in February 2017. As a result, an impairment of US\$170.8 million, representing the total non-current assets on the balance sheet, was recognised in the results and disclosed as an exceptional item. Following the restructuring and settlement of one-off costs, it is planned that the ongoing care and maintenance costs will be approximately US\$3.0 million per year.

Letšeng average price achieved
US\$1 695 per carat

(2015: US\$2 299 per carat)

Ghaghoo average price achieved
US\$152 per carat

(2015: US\$162 per carat)

Group financial performance continued

DIAMOND MANUFACTURING OPERATION

The Group generated additional margin on selected high-value diamonds through its manufacturing facilities and partnership arrangements. The diamond manufacturing operation in Belgium contributed US\$3.2 million to Group revenue (through additional polished margin) and US\$2.2 million to underlying EBITDA. Extracted diamond inventory on hand at the end of the year was US\$4.4 million compared to US\$6.2 million in the prior year, further increasing Group revenue by US\$1.8 million.

As part of initiating cost efficiencies across the Group, the manufacturing operation (Baobab) in Antwerp was downsized during the year. Although Baobab will continue to provide its advanced mapping and rough diamond analysis and manufacturing services to the Group and to third parties, in order to decrease fixed overheads, the back-end cutting and polishing functions were outsourced.

CORPORATE OFFICE

Corporate expenses relate to central costs incurred by the Group through its technical and administrative offices in South Africa and head office in the United Kingdom and are incurred in South African rand and British pounds. The impact of Brexit on the Group was limited to the depreciation of the British pound against the US dollar during the second half of the year, reducing the costs incurred in the United Kingdom which are US dollar reported. Corporate costs for the year were US\$11.0 million, showing continued decrease from previous years. During the latter part of 2015 the Diamond Producers Association was formed with Gem Diamonds as a founding member along with industry peers. Costs include the increased associated membership fees. The 2016 costs include once-off notice costs relating to the retirement of an Executive Director. Finding innovative ways of reducing diamond damage is a continued focus and US\$0.5 million was spent in the current year investigating alternative processing methods to improve diamond liberation.

The share-based payment charge for the year was US\$1.8 million. During the year, a new award was granted in terms of the long-term incentive plan (LTIP), whereby 1 400 000 nil cost options were granted to certain key employees and Executive Directors. The vesting of the options to key employees is subject to the satisfaction of certain market and non-market performance conditions over a three-year period. The share-based payment charge associated with this new award was US\$0.4 million for the year.

UNDERLYING EBITDA AND ATTRIBUTABLE PROFIT

Based on the operating results, the Group generated an underlying EBITDA of US\$62.8 million. The reduced EBITDA from US\$103.5 million in the prior year was driven by the lower revenue of US\$59.7 million due to the lower US\$ per carat achieved during the year. Before exceptional items, the profit attributable to shareholders was US\$17.7 million equating to 12.8 US cents per share based on a weighted average number of shares in issue of 138.3 million.

The Group's effective tax rate was 38.2% excluding exceptional items, above the UK statutory tax rate of 20.0%. This tax rate is driven by tax of 25% on profits generated by Letšeng, withholding tax of 10% on dividends from Letšeng and deferred tax assets not recognised on losses incurred in non-trading operations.

EXCEPTIONAL ITEMS

Impairment of assets totalling US\$172.9 million were recognised during the year, of which US\$170.8 million relates to impairment of the Ghaghoo operation following the decision to place the asset on care and maintenance. The balance of the impairment of US\$2.1 million relates to the closure of the Calibrated operation. This operation was set up to use laser diamond shaping and cutting technology and machinery as part of the integration of the Group's rough diamond analysis and manufacturing business. As part of the Group's focus on reducing costs and the limited ability to develop this beneficiation opportunity in Lesotho, the operation was closed. US\$3.5 million foreign currency translation reserve was recycled through the income statement relating to the Calibrated business as the operation was based in South Africa.

After including the effect of exceptional items of US\$176.5 million, the Group's attributable loss was US\$158.8 million.

FINANCIAL POSITION AND FUNDING OVERVIEW

The Group ended the year with US\$30.8 million cash on hand, of which US\$28.5 million was attributable to Gem Diamonds and US\$3.1 million was restricted (2015: US\$2.6 million). This restricted cash mainly relates to funds reserved for a portion of the future repayment of the US\$25.0 million secured bank loan facility at Ghaghoo.

The Group generated cash flow from operating activities of US\$70.7 million before the investment in waste mining of US\$70.4 million and capital expenditure of US\$7.6 million at Letšeng and US\$2.6 million at Ghaghoo. The capital expenditure at Letšeng mainly comprised US\$1.8 million for planned dam wall rehabilitation, US\$1.0 million for the first phase of the mining support services workshop and US\$0.5 million for the reinforcement of the primary crushing area (PCA) structure. At Ghaghoo, the capital expenditure mainly comprised US\$1.1 million for earthmoving equipment, US\$0.5 million for borehole extension and US\$0.3 million extension to the slimes dam facilities.

During the year, Letšeng declared dividends of US\$46.5 million, of which US\$29.3 million flowed to the Company and US\$17.2 million was paid outside of the Group for withholding taxes of US\$3.3 million and payment to the Government of Lesotho of US\$13.9 million for its minority portion.

The facilities held at the Company and Ghaghoo were restructured during the year, where the Company's US\$20.0 million available revolving credit facility was increased to US\$35.0 million and the Ghaghoo fully drawn down facility was restructured whereby the capital repayments were scheduled to re-commence in June 2019. The Group therefore had US\$53.3 million worth of undrawn and available facilities at the end of the year comprising US\$35.0 million at Gem Diamonds and US\$18.3 million at Letšeng.

Post-year end, the decision to place the Ghaghoo mine on care and maintenance impacted the US\$25.0 million term loan facility and the Group used the revolving credit facility at the Company level to repay the loan. In addition, the LSL140 million

(US\$10.2 million) was settled with the final LSL28.0 million (US\$2.0 million) repaid in February 2017.

Post-year end, negotiations continued to secure funding for the construction of the mining support services complex valued at LSL215.0 million (US\$15.7 million). This facility has a planned tenure of 5.5 years with a 13-month availability period for draw down.

DIVIDEND

At the AGM held on 7 June 2016, shareholders approved the payment of an ordinary dividend of 5 US cents per share totalling US\$6.9 million, and equating to 18% of the Group's 2015 net sustainable attributable earnings. In addition, a special dividend of 3.5 US cents amounting to US\$4.8 million was also approved. Based on the current market conditions, the lower than expected Letšeng revenue, and the impact that it has had on the Group's cash resources, the Board resolved not to propose the payment of a dividend in 2017 based on the 2016 results.

OUTLOOK

Focus in 2017 will be on cash generation. At Letšeng, the implementation of the revised life of mine plan is expected to improve cash flows through a further optimised waste mining profile. Furthermore, the variability of the resource is expected to revert to normal, improving the recovery levels of the larger, high-quality diamonds at Letšeng. The benefits to be derived from the mining performance improvement project at Letšeng and the placing of Ghaghoo on care and maintenance will allow for reduced operating costs. These initiatives will drive the objective of maximising shareholder returns with the intention of recommencing the payment of a dividend in the future.

Michael Michael
Chief Financial Officer

14 March 2017

2016 IN REVIEW

Severe weather impact contained

Revised production targets achieved

Recovered grade achieved 1% above reserve grade

34 rough diamonds achieved a value greater than US\$1.0 million each

Five diamonds larger than 100 carats recovered

Average price achieved of US\$1 695 per carat

Retained ISO 18001 and ISO 14001 certification

Letšeng



STRONG OPERATIONAL RESULTS OVERSHADOWED BY PAUCITY OF LARGE HIGH-VALUE DIAMONDS



OPERATIONAL PERFORMANCE

The planned increase in mining production progressed during the year, with a 24% increase in waste mining in support of increasing the contribution of the higher-value Satellite pipe ore. Letšeng treated 6.6 million tonnes of ore compared to 6.7 million tonnes of ore in the prior year. A post-implementation review of the Plant 2 Phase 1 upgrade (commissioned in 2015) was completed during the year, indicating a 12% increase in the plant capability. The additional expected tonnes were not realised due to power outages caused by a severe snow storm experienced in July and August which resulted in both Letšeng and Alluvial Ventures' treatment plants running at reduced capacity for a period of 17 days. Ore and waste mined were also negatively impacted by the inclement weather conditions, as access to the pits was unattainable. Ore sourced from strategic stockpiles on surface partially mitigated this impact. Of the total ore treated, 69% was sourced from the Main pipe, 27% from the Satellite pipe and 4% from the Main pipe stockpiles. Letšeng recovered 108 206 carats at a grade of 1.63cpht, in line with the expected reserve grade, at a reserve mine call factor (MCF) of 101%.

LARGE DIAMOND RECOVERIES

During 2016, the frequency of exceptional larger diamonds recovered was lower than expected. Letšeng recovered five +100 carat diamonds during the year, compared to 11 that were recovered in 2015. Following a detailed review of the resource and operational process, it was considered that this paucity of large exceptional diamonds was due to normal statical short-term variability of the resource, as was experienced during 2012. The performance of the resource is further detailed in the mineral resource management section on pages 46 to 49.

MAXIMISING LETŠENG'S VALUE

Over the past five years, Letšeng has grown to be one of the largest open pit diamond mines in the world. This growth has required comprehensive capital investment. During this time, the mine has continually improved its systems and processes to support the additional volumes mined.

In 2016, a fleet management system was installed to drive further productivity improvements. This world-class system will optimise the running of the fleet of haul trucks which has again increased by seven additional 100 tonne Caterpillar rigid dump trucks in the current year. The KPIs generated by this system will provide the baseline against which productivity improvements will be measured.

Operational performance	Year ended 31 December 2016	Year ended 31 December 2015	% change
Waste tonnes mined	29 776 058	24 010 847	24.0
Ore tonnes mined	6 694 753	6 508 806	2.9
Ore tonnes treated	6 646 098	6 679 581	(0.5)
Carats recovered	108 206	108 579	(0.3)
Recovered grade – cpht	1.63	1.63	0
Carats sold	108 945	102 778	6.0
Average price per carat (US\$)	1 695	2 299	(26.3)

During the annual replanning cycle, the sequence of waste mining was reviewed with an aim to stabilise the waste stripping profile. The outcome of this resulted in an updated mine plan, which was completed in Q1 2017, and will reduce the waste stripping profile over the next three years and increase the ore tonnes available for treatment to 7.0 million tonnes per annum (up from 6.0 million tonnes per annum) for the open pit life of mine. The valuable contribution from the higher US\$ per tonne Satellite pipe will increase from 1.6 million tonnes per annum to 1.8 million tonnes per annum for the next two years, and thereafter will increase to 2.0 million tonnes per annum until 2029.

The expansion of the open pits has necessitated the construction and relocation of an expanded mining support services complex. The first phase of this project was completed at a cost of less than US\$1.0 million. Detailed design of the next phase has been completed and the construction thereof, at a cost of LSL215.0 million (US\$15.7 million), will commence in 2017 once project funding has been secured.

As part of optimising diamond liberation and initiatives aimed at reducing diamond damage, the splitting of the front ends of Plant 1 and Plant 2 commenced and is due for completion in Q1 2017. The splitting of the front ends provides the opportunity to dedicate ore treatment through the most suitable plant based on geo-metallurgical characteristics. Previously implemented workstreams targeting diamond damage reduction have had positive results with some exceptional undamaged diamonds recovered during the year, in particular, a 160 carat Type II, a 104 carat Type II and an 11.8 carat pink diamond. Diamonds continue to be damaged, and therefore the reduction in diamond damage remains a key focus area. To further address this, a project has been initiated to investigate the implementation of a large diamond recovery capability.

Letšeng continued

To address major sources of downtime experienced during 2016, the primary crushing area (PCA) structure was reinforced in December 2016, thereby prolonging the PCA's life and deferring major capital expenditure by between eight and 10 years. Simultaneously critical maintenance work in Plant 2 was completed during which two vertical conveyors, two major chutes and a new feed preparation screen was installed.

As part of Letšeng's efficiency and cost reduction drive, a mining productivity improvement initiative commenced during Q4 2016 engaging a global mining efficiency and continuous improvement consultancy firm to support the mining team on site, with the fundamental objective of improving mining operational practices and increasing mining equipment utilisation and efficiency, with the benefit of reducing operational costs.

These initiatives will further enhance Letšeng's value proposition and are expected to improve the cash flows from the operation.

RESOURCE DEVELOPMENT

During the year, four micro-diamond samples were treated and preliminary interpretation of the results indicated that it may be possible to use this technique to determine macro-diamond grades. A core drilling programme is scheduled to start in the first half of 2017. The programme provides for the drilling of a combined 7 540 metres of core in both the Main and Satellite pipes. This drilling will provide an enhanced understanding of the kimberlite geology below current mining levels. As part of the programme it is planned to treat suitable samples of core for further micro-diamond analysis. Refer to the mineral resource management section on pages 46 to 49 for further details.

SKILLS

The attraction and retention of skills remains an ongoing challenge at Letšeng. Working in a remote area and remunerating in a globally weak currency remains a challenge when attracting skilled employees. Localisation objectives, difficulties experienced in obtaining work permits for skilled expatriates and increasing competition for skilled personnel from other mining companies in Lesotho contribute to the challenges experienced in retaining the appropriate skills at Letšeng.

During the year, several development programmes with South African universities and other accredited institutions, for the development of Lesotho citizen employees, were successfully introduced.

Through the newly established Lesotho Chamber of Mines, the sector has conducted extensive engagement with the Government of Lesotho to expedite the issuing of work permits and facilitating the entry of expatriates into this important sector of the economy which in turn will assist in the development of mining expertise. A memorandum of understanding has been signed between these two parties which will see tangible benefits to the industry.

HEALTH, SAFETY, SOCIAL AND ENVIRONMENT (HSSE)

Letšeng retained its ISO 18001 and ISO 14001 certification for the second consecutive year. Independent audits were conducted to rate the operation's occupational health, safety and environmental management systems against these ISO standards. Letšeng is committed to identifying and mitigating the risks to the health and safety of its employees, contractors and project-affected communities (PACs). Regrettably, the operation recorded two lost time injuries (LTIs) in 2016, ending a 562-day LTI-free period in May 2016.

As a reflection of the operation's commitment to safeguarding the natural environment in which it operates, Letšeng recorded no major or significant environmental incidents for the year. The operation considers the protection of its natural environment as critical to sustainable success. Numerous environmental projects were launched in 2016, including a Bioremediation Project that forms part of the overarching nitrate and water management plans.

No major or significant stakeholder incidents were recorded in 2016 and Letšeng continues to work closely with all its stakeholders. PACs, identified through a comprehensive social and environmental impact assessment, form an important part of the operation's success. Letšeng worked closely with its PACs during 2016 to address socio-economic challenges faced by these communities.

Approximately US\$0.3 million was invested during the year towards community projects. This investment was made in accordance with a needs analysis and corporate social investment strategy that is specific to Letšeng. Education and small and medium enterprise developments received the bulk of the social investment, with US\$0.2 million invested in these two categories. In addition to the Botha-Bothe vegetable project, which has been

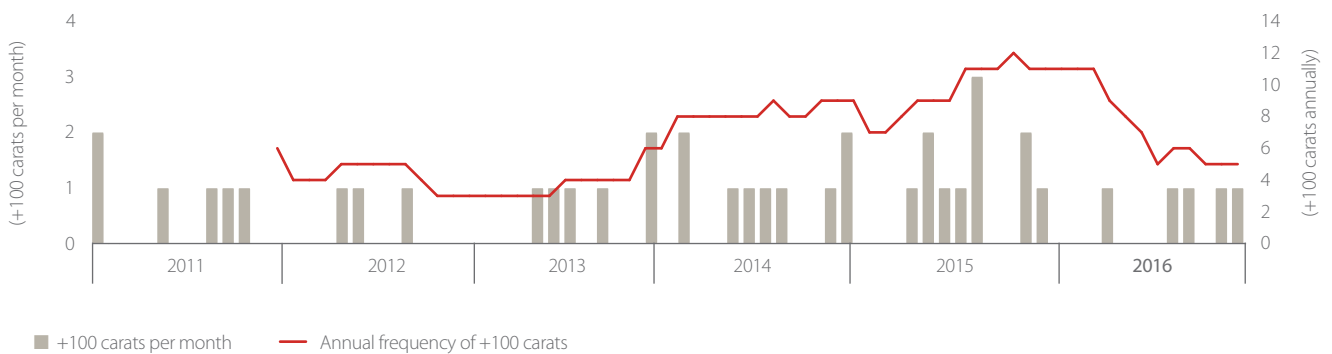
successfully running since 2015, the operation also invested in another enterprise development project, a dairy project. The dairy project is aimed at empowering local farmers by providing them with the means to generate income from dairy farming.

At the end of 2016, 97% of Letšeng’s workforce comprised Lesotho citizens.

Frequency of recovery of large diamonds

Number of diamonds	2008	2009	2010	2011	2012	2013	2014	2015	2016
>100 carats	7	6	7	6	3	6	9	11	5
60 – 100 carats	18	11	11	22	17	17	21	15	21
30 – 60 carats	96	79	66	66	77	60	74	65	70
20 – 30 carats	108	111	101	121	121	82	123	126	83
Total diamonds >20 carats	229	207	185	215	218	165	227	217	179

Letšeng +100 carat diamonds



2017 FOCUS

- ▶ Effective implementation of updated mine plan
- ▶ Deliver benefits from optimisation and expansion projects
- ▶ Construct expanded mining complex on time and within budget
- ▶ Complete core drilling to enhance the understanding of the kimberlite geology
- ▶ Progress feasibility studies of large-diamond recovery capabilities

2016 IN REVIEW

Operation downsized

49% of planned Level 1 VKSE ore extracted

Development to access Level 2 VKSE ore completed

VK-Main phase on Level 1 successfully sampled

Positive results from plant efficiency improvements

Average price achieved of US\$152 per carat

Four-star HSE NOSA rating

Ghaghoo

CONTINUED CHALLENGING MARKET CONDITIONS FOR GHAGHOO'S PRODUCTION HAS NECESSITATED PLACING THE OPERATION ON CARE AND MAINTENANCE IN 2017



OPERATIONAL PERFORMANCE

Ghaghoo operated at a reduced production rate during the year following the decision to downsize the operation due to the depressed state of the market that was experienced in 2015.

The buffer zone around the sand dilution from the sink hole that occurred in November 2015, was successfully created during Q1 2016, sterilising approximately 300 000 tonnes of ore.

A total of 1 440 metres of development was completed during the year. In total, 217 372 tonnes of ore were treated and 40 976 carats were recovered, achieving a recovered grade of 18.9cpht. The recovered grade was below the reserve grade of 27.8cpht due to the high percentage of coarse breccia dilution encountered in the ore extracted near the contact zone from Block 2. This was further exacerbated by diamond lock up in the DMS tailings and mill oversize material. The gratings and liners in the autogenous mill were reconfigured during the fourth quarter of the year and the mill operation was optimised to obtain better liberation and reduce diamond damage.

The VK-Main phase was successfully sampled and processed. The sample achieved a recovered grade of 18.2cpht, being 2% above the estimated reserve grade of 17.8cpht.

During the year, nine diamonds larger than 10.8 carats were recovered, of which the largest was a 40 carat diamond. Fancy coloured diamonds continued to be recovered, confirming the presence of these types of diamonds in the Ghaghoo resource.

Three sales were concluded during the year, achieving an average price of US\$152 per carat from the sale of 47 266 carats.

HSSE

During the year, Ghaghoo's health, safety and environmental (HSE) management system was audited by NOSA (previously audited by IRCA) and maintained its four-star rating for its fourth consecutive year. Ghaghoo focused on readying its HSE management systems for ISO 18001 and ISO 14001 pre-certification audits. The operation also underwent a 'Gem Way' internal audit during 2016, following which it was awarded a three-star rating.

Ghaghoo focused on building on the safety progress made in 2015, unfortunately the operation recorded three LTIs during 2016 ending a 449-day LTI-free period.

No major or significant environmental incidents were recorded during 2016. The operation underwent a suite of environmental audits during the year to monitor its compliance with legal and social licence requirements. Ghaghoo advanced its study into aquifer recharge and commenced with the construction of a pilot system that would provide the operation with data to better understand the feasibility of aquifer recharge as part of a water management strategy.

Operational performance	Year ended 31 December 2016	Year ended 31 December 2015	% change
Ore tonnes mined	231 099	320 630	(27.9)
Ore tonnes treated	217 372	326 922	(33.5)
Tunnelling metres developed	1 440	1 751	(17.8)
Carats recovered	40 976	91 499	(55.2)
Grade recovered (cpht)	18.9	28.0	(32.5)
Carats sold	47 266	89 107	(47.0)
Average price per carat (US\$)	152	162	(6.2)

No major or significant stakeholder incidents were recorded during 2016. Ghaghoo used the year to strengthen and formalise its corporate social investment strategy. A community needs analysis was completed at the start of 2016 and supported the social investment strategy implemented by Ghaghoo. Furthermore, approximately US\$50 000 was invested towards maintaining existing corporate social project commitments.

At the end of the year, 97% of Ghaghoo's workforce comprised Motswana citizens.

CARE AND MAINTENANCE

The fall in prices of Ghaghoo's production from US\$210 per carat in early 2015 to US\$142 per carat at its most recent sale in December 2016, emphasised the weak state of the diamond market for this category of diamonds. The operation has been placed on care and maintenance to preserve the value of the resource. The focus in 2017 will be to restructure the operation to reach a state of full care and maintenance during H1 2017. The care and maintenance philosophy is to maintain the asset as a going concern to enable effective and efficient recommencement of the operation when market conditions improve.

2017 FOCUS

▶ Execute the care and maintenance plan

▶ Assess future viable options

2016 IN REVIEW

Letšeng diamonds achieve top prices

Lack of larger high-quality diamonds impact overall US\$ per carat

Letšeng grade performance achieves MCF

VKMain at Ghaghoo bulk sampled

Mineral resource management



THE LETŠENG RESOURCE DELIVERS EXCEPTIONAL DIAMONDS ALTHOUGH FEWER OF THE LARGER HIGH-VALUE DIAMONDS WERE RECOVERED DURING THE CURRENT YEAR



RESOURCE PERFORMANCE

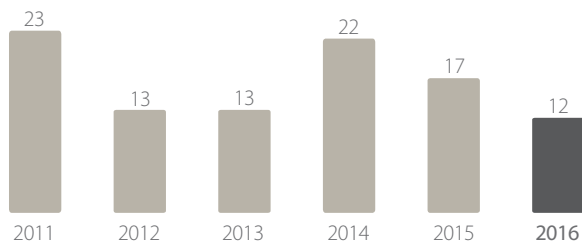
Letšeng

Letšeng is renowned for producing some of the world’s largest and highest-value diamonds. This is mainly as a result of the high proportion of exceptional quality, flawless white Type II diamonds. This ranks Letšeng as the highest average US\$ per carat kimberlite mine in the world.

Letšeng’s revenue is highly geared towards the number of large, high-value diamonds recovered. The years 2014 and 2015 were extraordinary in terms of large diamond (greater than 100 carats) recoveries and the percentage of total revenue derived from diamonds larger than 10.8 carats. In comparison, the 2016 production year has been characterised by fewer large and high-value diamonds. Letšeng’s realised US\$ per carat was below the 2016 expected reserve prices, and achieved US\$1 695 per carat compared to US\$2 092 per carat.

Of the 100 highest-value diamonds produced in the past six years, only 12 were produced in 2016, negatively impacting the revenue at Letšeng.

Top 100 US\$ per carat diamonds recovered



Although 2016 recorded fewer +100 carat diamonds than the prior year, the mine produced an 11.78 carat fancy pink diamond which achieved US\$187 700 per carat, the third highest price for a single diamond from Letšeng. In addition, four spectacular diamonds recovered during 2016 were ranked in the top 35 of the highest total revenue achieved for a single diamond from Letšeng since 2011. The aggregate value of these four diamonds was US\$22.0 million:

**Highest value diamonds of 2016
(ranked in top 35 since 2011)**

160.21 carat Type II D – ranked 8th

93.90 carat Type II D – ranked 16th

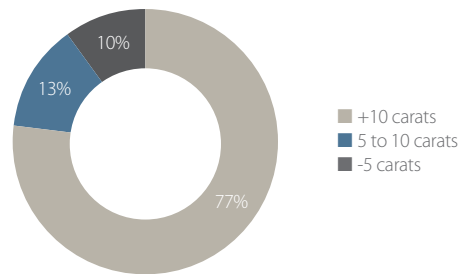
88.43 carat Type II D – ranked 28th

84.87 carat Type II D – ranked 31st

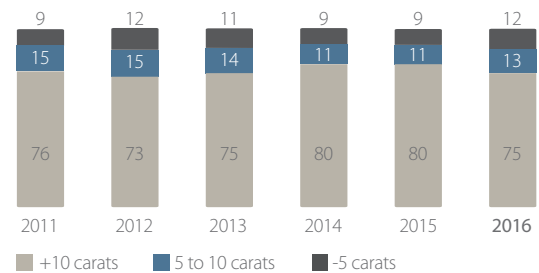
Despite recovering these exceptional diamonds, an increase in grade and the recovery of a higher quantity of smaller diamonds from an area within the southern portion of the Satellite pipe during the year, resulted in the average diamond price achieved for the year being below expectations.

Over the past six years, annual revenue from individual diamonds larger than 10.8 carats has been consistently 70% to 80% of total revenue and, therefore, the operational focus at Letšeng is dramatically different to other diamond producers where grade is usually the primary metric.

Average percentage revenue 2011 to 2016



Percentage revenue per size category (%)

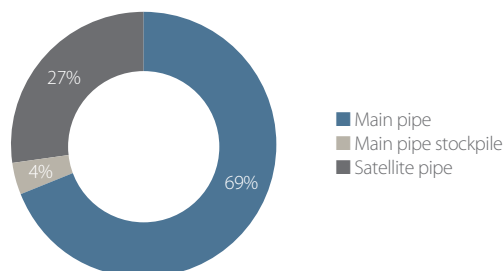


Mineral resource management continued

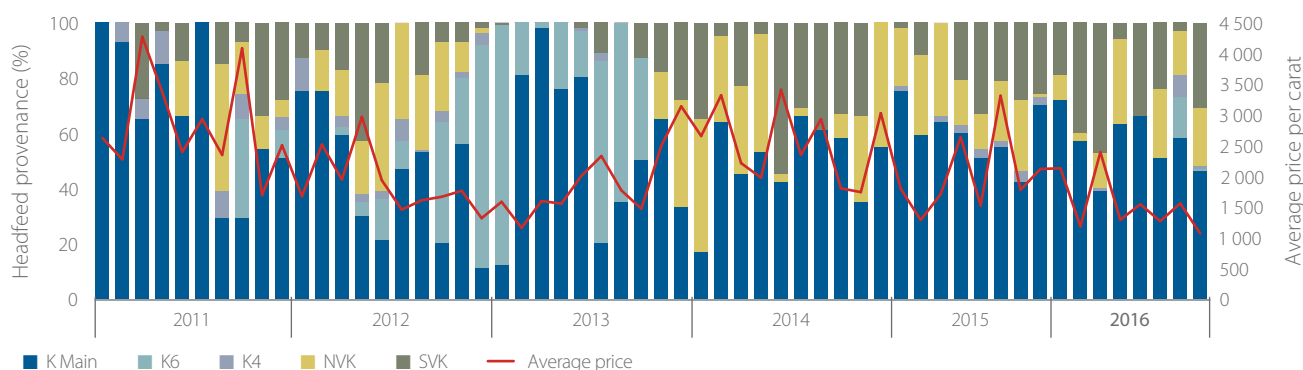
Grade performance

Letšeng's recovered grade of 1.63cpht was in line with the expected grade and achieved a reserve MCF of 101%. Of the total ore treated during 2016, 69% was sourced from the Main pipe, 27% from the Satellite pipe and 4% from the Main pipe stockpiles. Historically the Satellite pipe has produced a higher percentage of high-value Type II diamonds while Main pipe has produced some of the largest and most valuable stones.

2016 ore provenance



Letšeng headfeed provenance and average price per export 2011 to 2012



Discrete sampling results

During 2016, discrete sampling within Main pipe and Satellite pipe was focused on areas within the KMain, K4, NVK and SVK kimberlite domains. This sampling programme will continue into 2017 and together with the 2017 core drilling programme will augment the understanding of the resource. This work is enhancing the understanding of the geology and value of both pipes at depth.

Resource development

The Letšeng kimberlites are unique and have been a source of intrigue for geologists since their discovery. Not only are the diamond populations atypical, but the way the pipes were

formed and their emplacement history is rather unusual. Several features of the Letšeng pipes differentiate them from the Kimberly-type pyroclastic kimberlites and impact our understanding of the distribution of diamonds within the pipes.

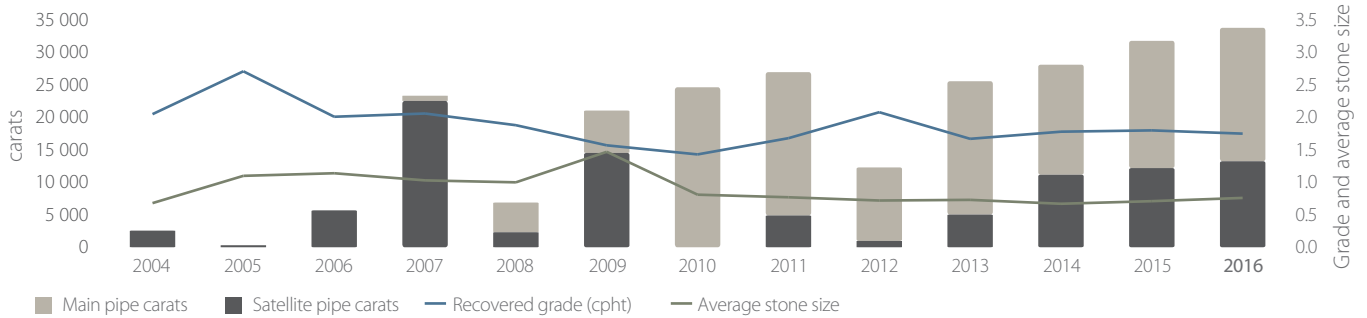
Since mid-2013, the geological team at Letšeng has been working with a team of leading kimberlite experts from Canada and South Africa to gain a deeper understanding of the relationships between the various kimberlite types within each pipe and to differentiate high-grade varieties from those with high value (containing large and abundant Type II diamonds). During the year, previous geological work was reassessed; historical drill core was relogged; more detailed studies were undertaken on

Discrete sampling results

Pipe	Domain	Wet tonnes*	Carats	Stones	Grade (cpht)*	Average Stone Size (carats)
Main	KMain	1 376 737	19 830	25 250	1.44	0.79
	K4	61 038	717	1 326	1.17	0.54
	Total	1 437 775	20 547	26 576	1.43	0.77
Satellite	NVK	177 621	4 372	5 580	2.46	0.78
	SVK	314 723	8 876	12 559	2.82	0.71
	Total	492 344	13 248	18 139	2.69	0.73

* Based on wet tonnes – no moisture factor applied.

Letšeng – Main pipe and Satellite pipe discrete sampling



indicator mineral abundances and petrography; and the rock types at depth were linked with those previously mapped in detail in the open pits to update the geological models.

Although Letšeng demonstrates broad scale consistency year on year in terms of price and average stone size for each of the kimberlite domains, the objective of the resource development programme is to gather data on local variability within each domain to improve large stone predictability and calibrate expectations of what each domain and subdomain can reasonably be expected to yield in terms of grade, average stone size, number of +100 carat stones and average price.

Capital was approved in late 2016 for another phase of core drilling in both the Main and Satellite pipes to increase the density of drillholes down to approximately 300m below the current pit floors and further refine the geological models. The programme is scheduled to start in the first half of 2017 and provides for the drilling of 7 540m of core.

Research was undertaken at University of Alberta on Type II macro-diamonds using Fourier Transform Infrared Spectroscopy and Secondary Ion Mass Spectrometry to assess a genetic relationship between microdiamonds and Type II macro-diamonds and to test the suitability of the technique as a predictor of grade and Type II diamond continuity. This research is being expanded in 2017 to study inclusions within the Type II macro-diamonds to identify a distinct mantle signature that could be used to target kimberlite phases with elevated Type II diamond potential based on associated indicator mineral chemistry.

The resource development programme has significantly advanced the understanding of the Letšeng kimberlites, the details of which are to be presented at the 11th International Kimberlite Conference in September 2017.

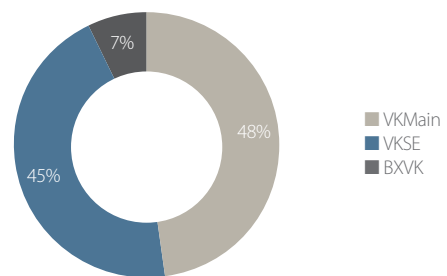
No additional resources and reserves were added during 2016. The priority for 2016 and into 2017 is firming up on the existing resource base and making appropriate operational and infrastructural adjustments to extract maximum value. Considering the current resource-related work streams in progress, no new resource and reserve statement is to be declared for 2016. After completion of the drilling programme and the associated geological studies on the core are integrated into the resource evaluation, an updated resource and reserve statement will be issued.

Ghaghoo

Since mining operations began, the focus was on confirming the historical estimates of the higher grade VKSE domain. Mining started in the south eastern portion of the pipe in the relatively undiluted VKSE ore. Mining then progressed towards the central zone containing abundant country rock dilution, referred to as the brecciated VK or BXVK in the resource statement. This material contains primary kimberlite that was diluted with brecciated country rock during the emplacement process.

2016 saw a convergence of several factors which served to stress the operation, most notably the decline in prices for the types of diamonds produced at Ghaghoo. Another contributing factor was the mining and processing challenges related to unavoidable highly diluted brecciated ore and the substantial proportion of lower grade ore from the VKMain.

2016 ore provenance



Of the 217 372 tonnes treated during 2016, 48% were from VKMain (17 cpht reserve), 45% from VKSE (27cpht reserve) and 7% from BXVK (9cpht reserve).

During 2016 the evaluation of the lower grade VKMain domain was initiated. This domain was originally excluded from the underground mining reserves due to its low grade. Underground development of the tunnel into the VKMain ore commenced in July 2016 and sample processing was completed in December 2016. The sample confirmed the reserve estimates with a recovered grade of 18.2cpht, which is 2% above the estimated 17.8cpht reserve. Additional resource delineation drilling was completed during the year in order to confirm geological contacts for level one and level two.

2016 IN REVIEW

11.78 carat pink diamond achieved US\$187 700 per carat

Letšeng achieved US\$1 695 per carat

Ghaghoo achieved US\$152 per carat

Polished sales contributed additional revenue of US\$3.1 million

Sales, marketing and manufacturing



PRICES FOR LETŠENG'S HIGH-VALUE DIAMONDS REMAIN FIRM



Gem Diamonds continues to invest in its sales, marketing and manufacturing operations to pursue ways of maximising revenue through a combination of marketing channels, including tenders, strategic partnerships, off-take arrangements and additional initiatives further along the diamond pipeline.

SALES AND MARKETING

The Group's rough diamond production is marketed and sold by Gem Diamonds Marketing Services (Belgium) and Gem Diamonds Marketing Botswana (Botswana). Letšeng's diamonds are viewed and sold through an open tender in Antwerp while Ghaghoo's diamonds are viewed in both Gaborone and Antwerp and, subject to prevailing market conditions, are sold either through an open tender or direct sale.

Following viewings by customers in either Antwerp or Gaborone, Gem Diamonds' electronic tender platform allows customers the flexibility to participate in each tender from anywhere in the world. The tender process is managed in a transparent manner. This, combined with professionalism and focused customer care and management, has led to a branded Gem Diamonds experience, contributing to securing customer loyalty, as well as supporting highest market-driven prices for the Group's rough diamond production.

Select rough diamonds from Letšeng which have been manufactured into polished diamonds by Baobab Technologies (Baobab) are sold by Gem Diamonds Marketing Services through direct selling channels to prominent high-end customers.

OPERATIONAL PERFORMANCE

During the year, the Group continued to build its premium customer base. Currently, the Group has 337 approved and registered customers, up from 105 in 2010. Eight large rough diamond tenders were held during the year, all of which were well attended, with an average of approximately 130 customers attending each tender. The Group continually engages with its customers to better understand their challenges and needs and, where possible, accommodates these in its marketing strategy. This is evident in the change in the number of tenders held in a year reducing from 10 to eight (implemented in 2015) and the tenders for the smaller production being reduced to one per quarter with higher volumes.

** Includes carats extracted for polishing at rough valuation.*

The multiple strategic and flexible marketing channels adopted in the sale of Letšeng's high-quality diamonds in 2016 contributed in achieving an average price of US\$1 695* per carat in a difficult and challenging diamond market. The lower Letšeng average US\$ per carat achieved in 2016 was largely a consequence of the paucity of large, high-quality diamonds, rather than any notable decrease in demand or weakening of the prices for these diamonds.

Prices achieved for Letšeng's large, high-value diamonds continued to impress with the following prices being achieved:

- ▶ an 11.78 carat pink diamond achieved US\$187 700 per carat, making it the third highest US\$ per carat achieved for a single Letšeng rough diamond since Gem Diamonds Marketing Services was established in 2010;
- ▶ a 12.31 carat pink diamond achieved US\$109 677 per carat; and
- ▶ the top two white diamonds of 93.90 and 56.48 carats achieved US\$56 561 per carat and US\$53 451 per carat respectively.

The sale of polished diamonds previously placed into strategic partnerships contributed additional revenue of US\$2.6 million to the Group.

An average price of US\$152 per carat was achieved for Ghaghoo's production. The downward pressure on prices for the more commercial Ghaghoo production seen in 2016, materially influenced the sales and marketing strategy for these goods. Two of the three Ghaghoo production sales were concluded through direct sales, with the aim of maximising the price (US\$160 per carat and US\$155 per carat, respectively). The third and final sale for 2016 was concluded by way of open tender with viewings in Gaborone and Antwerp, achieving US\$142 per carat.



11.78 carat pink diamond which achieved US\$187 700 per carat during the year.

Sales, marketing and manufacturing continued

ROUGH DIAMOND ANALYSIS AND MANUFACTURING

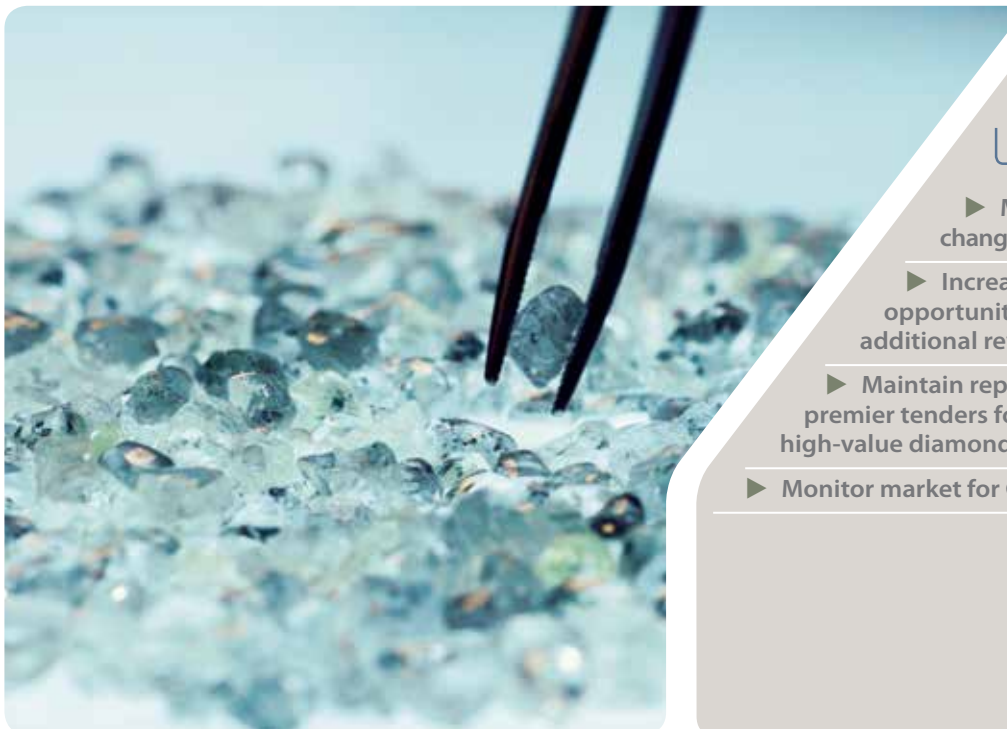
Baobab's advanced mapping and analysis of Letšeng's large exceptional rough diamonds supports the Group in analysing and assessing the value of Letšeng's rough diamonds that are presented for sale on tender or sold through other sales channels. This ensures that robust reserve prices are set for the Group's high-value diamonds at each tender and informs strategic selling, partnering or manufacturing decisions.

To access the highest value for Letšeng's top-quality diamonds, the Group, through Baobab, selectively manufactures certain of the high-value rough diamonds and additionally places other exceptional diamonds into strategic partnership arrangements with select clients. Baobab also performs analyses and management of the manufacturing of large, high-value diamonds for third-party customers.

OPERATIONAL PERFORMANCE

The challenging market, especially in the manufacturing sector of the diamond industry, necessitated a re-evaluation of Baobab's activities in 2016. Although Baobab continued to provide its advanced mapping and rough diamond analysis and manufacturing services to the Group and to third parties, a decision was taken to outsource the back-end cutting and polishing functions to decrease fixed overheads and provide the needed services in a more optimal and fit-for-purpose manner.

During 2016, 33.42 carats of rough diamonds were extracted for manufacturing, with a rough market value of US\$0.7 million. The sale of polished diamonds previously extracted contributed additional revenue of US\$0.5 million to the Group for the year. The lower volume of extractions reflects the flexible marketing strategy of the Group which was adapted to consider the current challenging polished diamond market and to capitalise on the sale of Letšeng's production of rough diamonds on tender, which remained firm during the year.



2017 FOCUS

- ▶ Maximise revenues in changing market conditions
- ▶ Increase downstream opportunities to capitalise on additional revenue
- ▶ Maintain reputation for holding premier tenders for Letšeng's large, high-value diamonds
- ▶ Monitor market for Ghaghoo-type production

2016 IN REVIEW

Zero fatalities

Five lost time injuries recorded

Lowest ever recorded AIFR

Zero major or significant stakeholder incidents

Zero major or significant environmental incidents

Letšeng retains its ISO 14001 and ISO 18001 certification

Sustainable development



SUSTAINABILITY FOR THE GROUP IS CONSIDERED A FUNDAMENTAL PART OF ITS STRATEGY, WHICH SEEKS TO CREATE LONG-TERM SHAREHOLDER VALUE BY EMBRACING OPPORTUNITIES AND MANAGING RISKS DERIVED FROM ECONOMIC, ENVIRONMENTAL AND SOCIAL DEVELOPMENTS



Sustainable development review

MANAGING THE MATTERS THAT ARE MOST MATERIAL TO SUSTAINABILITY FOR THE GROUP

Gem Diamonds considers material matters to be those topics that have a direct or indirect impact on its ability to create, preserve or erode economic, environmental and social value for the organisation, its stakeholders and society at large. Material matters, therefore, include risks that must be managed as well as opportunities that could be captured to enhance the viability of the business in the short, medium and long term.

This year, Gem Diamonds has organised its material matters under five core themes, namely

- ▶ financial and operational;
- ▶ governance and ethics;
- ▶ employees;
- ▶ social; and
- ▶ environmental.

Each theme makes up a core component of the business and the way in which Gem Diamonds sustainably mines diamonds. It is by monitoring these matters and remaining nimble in its approach to them that the business has continuity and that its impact on the places and communities where it operates are positive and any damage is appropriately mitigated.

This sustainable development review provides a summary of the information contained in the 2016 Sustainable Development Report. Readers are encouraged to read the information below in conjunction with the full Sustainable Development Report.

The review highlights the progress made and challenges faced during 2016 in pursuing the Group's sustainable development goals.

FINANCIAL AND OPERATIONAL

Gem Diamonds seeks to create economic value while delivering ongoing benefit to all its stakeholders. The Group's leadership approach is one that stimulates and encourages integrity at all levels of the business.

At Gem Diamonds, the need to protect its premium brand of diamonds is a key priority. During 2016, Gem Diamonds continued its work with the Diamond Producers Association (DPA) to enhance and uphold the premium brand of diamonds. During the year, the DPA released a campaign titled 'real is rare'.

The Group's sales and marketing team is tasked with developing the Letšeng brand and increasing and improving its customer base. In a challenging diamond market, the sales and marketing team in Antwerp has demonstrated their expertise in achieving top prices for Letšeng's diamonds.

GOVERNANCE AND ETHICS

As an organisation whose product derives its value from the perception of its consumers, the Group is committed to selling diamonds that are produced and distributed in accordance with legal and ethical standards. To achieve this, the Group has fostered a strong culture of corporate integrity and governance, which extends throughout the full business cycle. For more information, refer to the Governance section on pages 62 to 109.

Protecting human rights

Gem Diamonds recognises that diamonds can have a beneficial impact on the areas in which it operates when mined and traded responsibly. The Group acknowledges, however, that if diamonds are mined and sold irresponsibly, they may fuel conflict and contribute to human rights violations.

During 2016, Letšeng and Ghaghoo conducted human rights training for 264 employees. Beyond training, the Group enforces its policies on the fair treatment of employees through negotiated remuneration policies and stringent health and safety practices.

Gem Diamonds is strongly against human rights violations, including gender, age and racial injustices in the workplace. Non-discrimination policies are implemented across the Group, and stringent policies to prevent child and forced labour are adhered to. No cases of child or forced labour involving Gem Diamonds have ever been reported. Gem Diamonds also ensures rigorous controls are in place throughout its supply chain to ensure no slavery or human trafficking occurs, and during the year, Gem Diamonds signed a statement in accordance with the United Kingdom Modern Slavery Act. Furthermore, none of the Group's operations have engaged in the relocation or resettlement of any project-affected communities (PACs) during the reporting period.

Prioritising business integrity

The Group aims to supply clients with rough and polished diamonds while meeting its responsibilities as an ethical and accountable organisation.

The Group complies with the provisions of the Kimberley Process and all rough diamond exports are certified in terms of the Kimberley Process certification scheme, which aims to eliminate the global trade of conflict diamonds.

This commitment to upholding the highest ethical standards ensures compliance with relevant government regulations and voluntary codes concerning labelling, product and service information. To ensure that the Group's diamonds reach the market through the correct channels, strict controls are applied concerning potential clients. Potential clients are subject to a screening process, and trade is by invitation only. During the screening process, potential clients are assessed to confirm and validate their good standing and compliance with internal and external anti-money laundering protocols.

Gem Diamonds maintains the highest levels of transparency and integrity during the marketing and sales process. Diamond viewing opportunities are made available to clients prior to the conclusion of a tender. No warranties in respect of the diamonds are issued. Client confidentiality is protected in all instances. All tenders are governed by conditions agreed to by all clients. A complete list of the winning bids is electronically circulated to all tender participants on the close of the tender, ensuring a transparent tender process.

Raising standards across the pipeline

As part of its initiative to identify and mitigate risk, the Group has an established whistleblowing policy, which allows for anonymous reporting by employees of any unethical activity taking place in the workplace.

To ensure all those in the supply chain support the ethos of the Group, there are procurement policies in place, which drive rigorous vetting processes. Potential risk areas are scrutinised, and goods and services are only procured from reputable companies. Suppliers are required to adhere to the Group's ethical policies.

EMPLOYEES

The Group is committed to providing a work environment that actively promotes the health and safety, as well as the development and retention of its employees. This is achieved through investing in employees' skills and capabilities and promoting equality and diversity in the workforce.

Providing a safe working environment

Gem Diamonds' health and safety management system is based on the principles of ISO 18001 and relevant international best practice standards. These systems are independently audited on an annual basis to ensure compliance and provide the organisation with improvement opportunities.

Gem Diamonds reported a fatality-free year. However, five LTIs occurred resulting in a lost time injury frequency rate (LTIFR) of 0.18, up from 0.00 in 2015. The 2016 Group-wide all injury frequency rate (AIFR) was 1.93 – the lowest it has been in the history of the Group.

Gem Diamonds believes that concentrated efforts on the proactive management of safety will continue to assist in its pursuit of zero harm. The number of proactive safety management actions implemented throughout the Group in 2016 amounted to 74 110.

Attracting and retaining qualified people

Skills shortages in the mining sector highlight the importance of attracting and retaining staff.

At year end, the Group employed 446 employees and 1 739 contractor employees, compared with 589 employees and 1 359 contractor employees during 2015. The average number of own employees was 481 (compared with 560 in 2015), while the average number of contractor employees for 2016 was 1 650, compared with 1 369 in 2015.

The Group-wide absenteeism rate increased to 3.9 days per person in 2016 from 2.0 days in 2015.

High staff turnover can affect productivity and result in a loss of intellectual capital. Monitoring staff turnover helps manage this risk and gives an indication of employee satisfaction. The Group-wide staff turnover has increased from the 2015 value of 4.0% to 8.6% in 2016. This percentage takes into consideration voluntary turnover and does not include retrenchments. Although voluntary turnover increased during the year, this is taken to be a normal occurrence in organisations undergoing change. The Group will, however, monitor these turnover rates and employee satisfaction indicators to ensure, to the best of its ability, that quality people are retained.

Group-wide hours per capita vocational training in 2016 has increased by 25% from 2015. This increase can be attributed to a Group-wide focus on employee development.

Employees at all the Group's operations are remunerated in line with market-related rates. Gem Diamonds has a policy of remunerating male and female employees in the same grade at the same level. The lowest-graded employees continue to receive higher remuneration than the respective host country's minimum wage standards.

In Lesotho and Botswana, there is no prescribed minimum wage in the mining sector. Therefore, the construction industry minimum wage is used as a standard. In 2016, the lowest-graded employees at Letšeng and Ghaghoo were remunerated at 24% and 11% above this minimum wage respectively. 2% of the workforce at Ghaghoo and 0.2% at Letšeng were compensated at the operation's minimum wage. Labour rates are determined in line with market-related rates, with external factors such as availability of skills, qualification, seniority and work experience being taken into consideration. Minimum requirements regarding remuneration are contractually stipulated with principal labour contractors.

In addition to basic remuneration, benefits and incentives are offered to employees. In 2016, a total of US\$36.5 million was spent on employee wages, benefits and incentives (2015: US\$38.9 million), including contractor employees.

Staff demographics (%)

Employee level	% Male	% Female	% Local citizens	% Age <30	% Age 31 to 50	% Age >50
2016						
Governance Committee/Board*	93	7	36	0	39	61
Senior management	88	12	25	0	66	34
Middle management	81	19	96	6	82	12
Total workforce	81	19	99	13	75	12
2015						
Governance Committee/Board*	89	11	33	0	39	61
Senior management	88	12	37	0	56	44
Middle management	80	20	96	18	74	8
Total workforce	90	10	99	21	63	16

* Includes subsidiaries

Sustainable development review continued

100% of Basotho nationals employed at Letšeng subscribe to the mandatory government retirement provision scheme, to which Letšeng contributes 7.5% per employee. Permanent employees at Ghaghoo receive retirement provisions, as included in their remuneration package, while fixed-term contractors receive a gratuity.

All other operations and offices remunerate employees on a cost-to-company basis, and employees are free to elect their retirement schemes and contributions.

Gem Diamonds' mines operate continuously, with shift configurations determined by local legislative requirements, as well as operational and market demands.

Providing skills development opportunities for employees

By investing in developing employees' skills through the provision of training opportunities throughout the Group, employees develop personally and professionally.

The total hours of training provided to employees during 2016 were:

- ▶ senior management: 1 086 hours (2015: 691 hours);
- ▶ middle management: 3 122 hours (2015: 3 593 hours); and
- ▶ non-management: 21 062 hours (2015: 17 464 hours).

Performing annual career reviews at all its operations remains a goal across the Group. There was a small decrease in the percentage of career reviews performed during the year from 23% in 2015 to 22% in 2016 due to downsizing measures carried out within the Group. In total 26% of female employees received reviews, and 21% of male employees received reviews.

Ensuring employees remain healthy

Gem Diamonds is committed to providing an environment that actively promotes and supports employee health and well-being.

Part of the Group's comprehensive induction programme at the mining operations for new employees includes a complete medical examination, further promoting its approach to employee well-being and care.

In 2016, Letšeng and Ghaghoo achieved a 100% pre-employment medical rate, matching their 2015 figures.

The Group has implemented a standard process at the mining operations for exiting employees, which includes exit medical examinations. This further supports Gem Diamonds' stance on complete employee care and is necessary to reduce the Group's long-term exposure to any future health claims.

In 2016, 7 102 medical cases were recorded across the Group, an increase from the 6 447 cases reported in 2015. Of the cases reported in 2016, only 7.7% were related to occupational or environmental diseases, compared to 8.7% in 2015. The majority of cases treated at the mining operations were primary healthcare issues, rather than occupational ones.

Serious disease prevention and management programmes continue to expand and mature, resulting in a decreasing number of interventions required by the Group's operations. A total of

5 769 serious disease prevention and management interventions were carried out during the year. The interventions consisted of educational interventions and counselling, as well as prevention and risk control measures.

SOCIAL

The Group aims to contribute positively and sustainably to the social and economic state of the PACs and its host countries.

Ensuring positive stakeholder engagement

Gem Diamonds recognises that trust is hard earned and easily destroyed. Understanding this, the Group strives to foster mutually beneficial partnerships with its stakeholders. This is primarily achieved through active dialogue with stakeholders, focusing on listening and participation at all business levels.

Each operation has developed a framework for stakeholder consultation. These plans are put in place to ensure that all stakeholders are engaged and that the PACs are consulted on a regular basis. Recognising the cultural and traditional individualities of each of the Group's operational communities is essential, and the aim is to function in a manner which is transparent and respectful.

During 2016, no major or significant stakeholder incidents occurred at any of Gem Diamonds' operations. There were also no incidents involving any violation of the rights of the indigenous people on whose land the Group operates.

Minimising social impact

Social and environmental impact assessments are undertaken in line with international best practice standards including Equator Principles, World Bank and the International Finance Corporation, while meeting local requirements. Through this process, any negative impacts are minimised and positive opportunities and outcomes identified.

Recognising that mining operations often have an impact on the surrounding population, both positive and negative, extensive investigations are undertaken into the possible impacts before and during mining, and ways of continuing the positive impact in these communities, even during the mine closure process, are identified.

Working with communities to understand and meet their needs

Gem Diamonds' goal is to comply with legal requirements in meeting community needs in order to leave a positive legacy.

In 2016, the Group-wide corporate social investment (CSI) expenditure amounted to US\$0.4 million (2015: US\$0.6 million). This decrease can be attributed to a shift in focus at Ghaghoo from proactive intervention to project maintenance in line with our objective of honouring our commitments to communities while managing the pressures of strained market conditions.

The CSI expenditure at Letšeng during 2016 amounted to US\$0.3 million (2015: US\$ 0.3 million). The majority of this expenditure was allocated to educational initiatives, followed by health programmes, infrastructural development, small and

medium enterprises, and other donations in support of specific charities and events.

The CSI expenditure at Ghaghoo was approximately US\$50 000 during 2016 (2015: US\$0.1 million). Expenditure was focused on health and medical initiatives, with contributions to educational projects and various donations to other charities and corporations.

Providing a framework for communities to benefit themselves

By employing members of its PACs or by engaging local businesses in the Group's supply chain, a significant positive contribution can be made to local communities. These practices assist Gem Diamonds in maintaining its social licence to operate through job creation and skills development.

Localisation of the workforce is a priority across the Group. Where operations are able to match available skills in the PACs with on-site requirements, local recruitment takes place.

In 2016, 97% of the Letšeng workforce comprised Basotho nationals (2015: 97%). At Ghaghoo, 97% of the workforce was made up of Botswana citizens in 2016, compared with 98% in 2015.

During 2016, Group in-country procurement totalled US\$141.2 million (2015: US\$152.1 million). Total in-country procurement at Letšeng decreased from US\$124.7 million to US\$121.6 million in 2016. PAC local procurement at Letšeng decreased to US\$1.1 million from US\$4.6 million in 2015. The procurement from regional communities decreased to US\$24.9 million from US\$33.7 million in 2015. Due to the remoteness of our Ghaghoo operation, the majority of procurement takes place at a national level, rather than on a PAC or regional level. During 2016, procurement expenditure on a national level decreased to US\$13.5 million from US\$23.7 million. These decreases in local procurement spend were in line with a Group-wide focus on cost reduction.

Gem Diamonds no longer monitors local contributions for the offices and facilities located in Johannesburg and London; a decision based on the size and complexity of city-based economies.

ENVIRONMENTAL

To safeguard the natural environments in which it operates, Gem Diamonds invests in various protection measures. In 2016, the Group invested a total of US\$0.8 million (2015: US\$1.5 million) in environmental training, specialist consultation, research and development, green purchases, and other environmental protection measures.

The Group reassessed its rehabilitation liability during 2016, which resulted in an increased liability of US\$16.6 million, up from US\$12.5 million in 2015. The increase can be attributed to an updated assessment of the rehabilitation costs that would be involved at the Ghaghoo mine.

For the eighth consecutive year, Gem Diamonds recorded zero major environmental incidents. This was also the seventh consecutive year that no fines were incurred for environmental transgressions or non-compliance.

During 2016, zero major or significant environmental incidents (2015: zero) were reported for the operations. There were 481 minor environmental incidents reported, compared with 289 incidents reported in the prior year. This increase can be attributed to an improvement in both education on site and a drive to ensure issues, however small, are reported as soon as they are identified.

Corporate water stewardship has allowed the Group to identify and manage its water-related business risks, find ways to mitigate its water impacts, and contribute to the sustainable management of the catchment areas in which it operates. Water footprint studies provide an integrated understanding of water abstraction and water use. A water footprint can be defined as a measure of freshwater appropriation underlying a certain product, including fresh surface water, groundwater incorporated into the product, or lost during the manufacturing of the product.

In 2016, the Group's total water footprint was 37.8m³/carat and 1.21m³/tonne treated. The increases were directly related to a 12% increase in water usage and 25% decrease in recovered carats.

The stress water footprint of the Group, that is, the stress placed on the water system by mining activity consumption, was calculated and water usage at the operations was found to be sustainable.

Water quality is constantly monitored at the Group's operations, and any inconsistencies are addressed. At Letšeng, seepage occurred from the Patiseng Tailings Storage Facility and the Qaqa waste rock dump. The seepage flows into the Patiseng and Qaqa river systems respectively. In the Patiseng tributary, a return water system has been constructed to capture the seepage below the Patiseng Tailings Storage Facility. The Group is currently investigating innovative solutions to reduce the nitrate level in the water entering the Qaqa water catchment.

Managing carbon emissions and waste

The negative effects of carbon emissions, arising from increased industrial development around the world, present a long-term risk to global climate stability and the Group recognises the need to apply every effort in combating this.

Sustainable development review continued

In 2016, the total carbon footprint for the Group was 184 765tCO₂e (compared to 146 499tCO₂e in 2015), primarily driven by electricity consumption and mobile and stationary fuel combustion. This figure includes the direct GHG emissions (Scope 1), energy indirect GHG (Scope 2) emissions, and material (Scope 3) emissions, and was calculated with boundaries clearly defined by the GHG Protocol Corporate Accounting and Reporting Standard.

The total Group footprint signifies an increase of 26% from 2015. This observed increase is the result of a significant increase in diesel usage at Letšeng (an increase of 32% in diesel usage for mobile combustion and 70% for stationary combustion). The combined increase of 32% for liquid petroleum gas (LPG) and 25% increase in explosives further attributed to this increase.

All operations have waste management plans to ensure that correct waste handling mechanisms are enforced. Volumes of mineral waste generated increased at Letšeng during 2016, in line with the mine plan. Mineral waste at Letšeng is retained on site in structures designed for this purpose. These structures are operated in compliance with the host country's requirements, as well as international best practice standards.

Volumes of mineral waste decreased at Ghaghoo during 2016, due to the decrease in mining activity following a decision to downsize the operation.

Setting up and maintaining a mine closure plan, including rehabilitation of mining sites and surrounds

Every mine has a finite life span, and the complete rehabilitation of the mine land in the future is required. As such, project lifecycles are focused on the eventual restoration of the land.

The continuous development and review of comprehensive rehabilitation plans remained a focus during 2016. The Group leases 6 174ha of land, of which 6.8ha were newly disturbed by mining activities during the year, bringing the total disturbed land leased by Gem Diamonds to 565ha. The Group continued with the annual review and improvement of comprehensive rehabilitation plans for its mining operations.

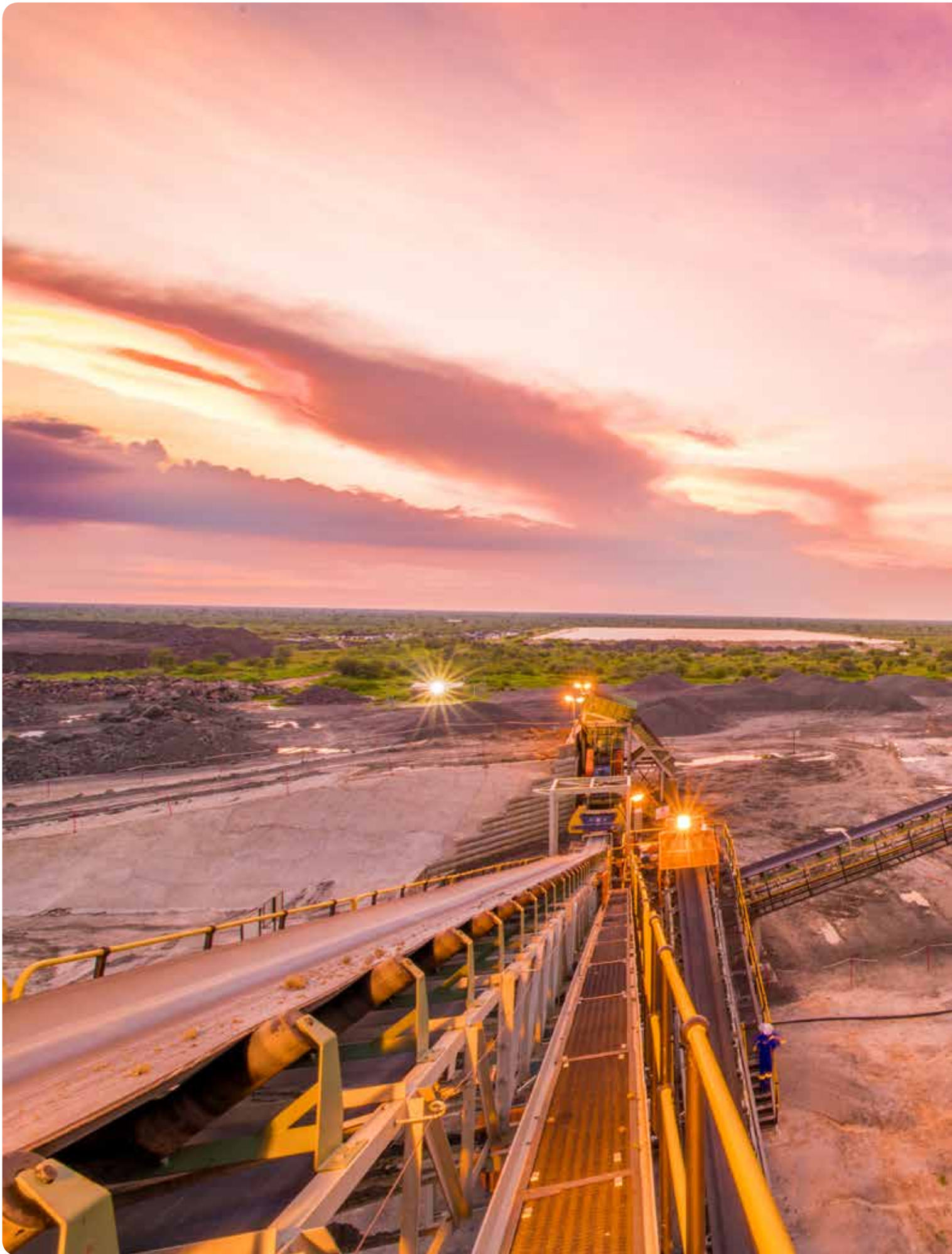
Sign off strategic report

Our Strategic Report, as set out on pages 2 to 59, has been reviewed and approved by the Board of Directors on 14 March 2017.

Roger Davies

Non-Executive Chairman

14 March 2017



Governance

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Directorate

Non-Executive Directors

1 ROGER DAVIS (60)

Non-Executive Chairman

MA (Oxon)

Roger spent eight years at Barclays, latterly as the Chief Executive Officer of the UK banking operation and as a member of the Board of Barclays Plc. Under his leadership, the UK business was significantly restructured. Prior to that, he spent 10 years in investment banking in London and held various positions in China and India for Flemings and BZW. Roger is currently the non-Executive Chairman of Sainsbury's Bank Plc and of GRC Limited, and is also a non-Executive Director at Experian Plc.

Appointed

February 2007.

Key skills and experience

Commercial and capital markets and public company board governance.

Board committee membership

Audit, Remuneration and Nominations Committees.

2 GAVIN BEEVERS (67)

Non-Executive Director

BSc Hons (Mechanical Engineering) (Lanchester Polytechnic)

Gavin spent most of his career at various De Beers operations in the positions of Assistant General Manager at De Beers Marine in Cape Town, General Manager at the Orapa and Lethlakane Mines, Deputy Managing Director of Debswana Diamond Company and Director of Operations of the De Beers group from April 2000 until his retirement in 2004. His unique tenure in mining brings a specialist oversight to the Group, with a particular focus on operational mining and, health, safety and sustainability responsibility.

Appointed

February 2007.

Key skills and experience

Operational mining, health and safety, sustainability and corporate social responsibility.

Board committee membership

Audit and HSE Committees.

3 MIKE SALAMON (61)

Senior Independent Director

BSc (Mining Engineering) (University of Witwatersrand); MBA (London Business School)

Mike has over 30 years experience in the mining sector. He was a founding Director of Billiton and was instrumental in Billiton's initial public offering (IPO) on the London Stock Exchange in 1997 and the subsequent merger with BHP in 2001. Mike retired from his position of Executive Director at BHP Billiton in 2006. Thereafter Mike was appointed Executive Chairman of New World Resources and led its IPO on the London Stock Exchange in 2008. He retired from this position in 2012.

Appointed

February 2008.

Key skills and experience

Operational mining, projects, health and safety, sustainability and corporate social responsibility and capital markets.

Board committee membership

Nominations, HSE and Remuneration Committees.

4 MICHAEL LYNCH-BELL (63)

Non-Executive Director

BA Hons (Economics and Accountancy) (University of Sheffield); FCA of the ICAEW

Michael spent a 38-year career with Ernst & Young (EY) having led its Global Oil and Gas, UK IPO and Global Oil and Gas and Mining transaction advisory practices. He was a member of the assurance practice from 1974 to 1996 when he transferred to the Transaction Advisory Practice. He was also UK Alumni sponsor and a member of the firm's EMEA and Global Advisory Councils. He retired from EY as a partner in 2012 and continued as a consultant to the firm until November 2013. Michael is currently a non-Executive Director at Kaz Minerals Plc and Lenta Limited. Michael is also currently honorary treasurer and board trustee of ActionAid International, a Human Rights campaigning NGO.

Appointed

December 2015.

Key skills and experience

Finance and capital markets, oil and gas and mining and metals.

Board committee membership

Audit and Remuneration Committees.

Executive Directors

5 CLIFFORD ELPHICK (56)

Chief Executive Officer

BCom (University of Cape Town); BCompt Hons (University of South Africa)

Clifford joined Anglo American Corporation in 1986 and was seconded to E. Oppenheimer and Son as Harry Oppenheimer's personal assistant in 1988. In 1990, he was appointed Managing Director of E. Oppenheimer and Son, a position he held until leaving in December 2004. During that time, Clifford was also a Director of Central Holdings, Anglo American and DB Investments. Following the privatisation of De Beers in 2000, Clifford served on the De Beers Executive Committee. Clifford is also the non-Executive Chairman of Zanaga Iron Ore Co. Limited and Jumelles Holdings Limited.

Appointed

Clifford formed Gem Diamonds in July 2005.

Key skills and experience

Diamond and mining industries, commercial and capital markets.

Board committee membership

Nominations Committee.

6 MICHAEL MICHAEL (46)

Chief Financial Officer

BCom Hons (Rand Afrikaans University); CA(SA)

Michael has over 20 years' experience in financial management. He joined RSM Betty & Dickson, an audit firm in Johannesburg South Africa in January 1993 and became Audit Partner at the firm in March 2000. From August 2006 to February 2008 Michael was seconded to Gem Diamonds Limited to assist with the financial aspects of the Main London Listing including the financial reporting, management accounting and tax relating to the IPO. In March 2008 Michael joined Gem Diamonds on a full-time basis and on 2 April 2013 he was promoted to the position of Chief Financial Officer.

Appointed

Michael joined Gem Diamonds in March 2008 and was appointed to the Board in April 2013.

Key skills and experience

Finance and capital markets and diamond industry.

7 GLENN TURNER (56)

Chief Legal and Commercial Officer and Company Secretary

BA LLB (University of Cape Town); LL.M (Cambridge)

Glenn was called to the Johannesburg Bar in 1987 where he spent 14 years practicing as an advocate specialising in general commercial and competition law, and took silk in 2002. Glenn was appointed De Beers' first General Counsel in 2002 and was also a member of the Executive Committee. Glenn was responsible for a number of key initiatives during his tenure, including overseeing De Beers' re-entry into the USA.

Appointed

Glenn joined Gem Diamonds in May 2006 and was appointed to the Board in April 2008. Glenn was appointed as the Company Secretary in January 2015.

Key skills and experience

Diamond industry and legal.

Board committee membership

HSE Committee.



Chairman's introduction to corporate governance

To maintain the best governance system, the Board is committed to encouraging integrity and transparency at all levels.

One of the key responsibilities of the Board is to maintain a high standard of corporate governance. This is a vital element in ensuring our future as a successful and sustainable group. As the Chairman, I am ultimately accountable for the application of the various provisions of the UK Corporate Governance Code.

Corporate governance is embedded in the way we organise our business, with local boards and sub-committees taking responsibility for our operations in local jurisdictions. As a Board, we are committed to maintaining regular open dialogue and effective communication with all our shareholders, customers, employees, suppliers and local communities.

The Board provides leadership to the Group within a framework of controls, which enables risk to be assessed and managed and to ensure the necessary financial and human resources are in place for the Group to meet its objectives and increase shareholder value.

We continue to assess the composition of the Board with the aim to obtain an effective balance and diversity of skills and experience to meet the Group's needs. We believe it is important that the independence of judgement of the non-Executive Directors will support and challenge the executive team on all areas of business strategy, risk management and internal controls.

Directors with a range of skill sets, capabilities and experience gained from different geographic and cultural backgrounds, enhance the Board by bringing a wide spectrum of experience and expertise to the business. We acknowledge the importance of diversity, including gender, to the effective functioning of our Board. We continue to be supportive of diversity in the boardroom. More information about our Board diversity policy can be found under the UK Corporate Governance Code Compliance Report on page 70.

At present, our Board comprises three Executive Directors and four non-Executive Directors representing different nationalities and disciplines (the details of which you will find in the biography for each individual on the directorate pages 62 and 63).

I will be standing down as Chairman and resigning as a member of the Board at the 2017 Annual General Meeting (AGM). My replacement will be announced ahead of the 2107 AGM, who I am confident will continue to lead and challenge the Board through the next stage of the business.

All Directors will be offering themselves for re-election at the 2017 AGM. Mr Gavin Beevers was appointed in 2007 and therefore in accordance with the Code, he is no longer considered independent. Although an extensive search and interview process for potential candidates with mining and technical experience was undertaken, due to the specific knowledge and experience required it proved difficult to find a suitable replacement to fulfil the Group's requirements. At the request of the Board, Mr Beevers has agreed to offer himself for re-election at the 2017 AGM and remain in post. The Board supports Mr Beever's re-election and has confidence that he will provide continuity to the Board given his significant knowledge of the business.

To maintain the highest standard of good governance we will continue to ensure the Board and its committees function appropriately to enable strong and valuable contribution and challenges to the deliberations and that no individual or group dominates the Board's decision-making process.

During the year, we have continued to be mindful of our duties as Directors to manage the Group for the long-term benefit of all its stakeholders. We conduct ongoing formal and informal training to keep apprised of all legislative and regulatory updates that

affect how we conduct our business. In 2016, the European Union Market Abuse Regime and the Modern Slavery Act 2015 introduced a number of new processes and procedures that we have implemented.

We undertook a Board evaluation process to follow up the matters raised in the 2015 evaluation and to assess the Board's approach to strategy and the ongoing effectiveness of the committees and risk management. The evaluation was carried out by way of a questionnaire. A detailed description of the evaluation process is set out on pages 69 and 70.

In the following pages, you will find overviews of our primary four Committees, together with detailed information regarding their overall operation within the governance framework.

All four Committees operate within clearly defined terms of reference. Each year we review the Terms of Reference for our Remuneration, Nominations, Audit and HSSE Committees, considering any new provisions introduced in the Code and current best practice standards.

We have a robust framework of risk management and internal controls which are reviewed quarterly by the Audit Committee. A key concern for good corporate governance is to eradicate bribery, fraud and corruption. I am confident that we have a stringent process in place throughout the Group. The ongoing monitoring and review of this process is led by our internal audit function.

Suspected wrong doings which are reported through our whistleblowing hotline, are brought to the attention of the Audit Committee through our internal audit function, with any irregularities being highlighted and actions taken. Following investigation, none of the cases reported in 2016 were significant and they were resolved without serious consequences.

The Remuneration Committee has been reviewing the Directors' Remuneration Policy to ensure that remuneration policy and practices are properly linked to corporate and individual performance and to deliver the Group's strategy on behalf of our investors. Every three years the Company is required to put the Remuneration Policy to shareholders for approval. The revised policy which shareholders will be asked to vote on at the 2017 AGM can be found on pages 86 to 93.

The Nominations Committee has been keeping under review the composition of the Board and succession planning for both Board members and Senior Management positions and it has made recommendations to the Board concerning appointments.

The HSSE Committee continues to ensure health, safety, social and environmental policies and practices are assessed and reviewed periodically to maintain a high level of relevance and appropriateness throughout the Group.

The Board and Committees' ongoing commitment to good governance and best practice principles for the benefit of all our stakeholders are demonstrated in the following pages of this report.

On a personal note, as I will be stepping down at the 2017 AGM, I would like to convey my thanks to the Board and employees of the Group. It has been my pleasure serving as your Chairman for the last ten years and it is an honour to have been part of a group that has continuously demonstrated and delivered excellent governance.

Roger Davis
Non-Executive Chairman

UK Corporate Governance Code Compliance

The Board sets standards of conduct which provide an ethical framework for the Group's business functions.

This report combines the Directors' Report, the Strategic Report and the Group's compliance with the principles and provisions of the UK Corporate Governance Code (the Code). It includes details of the key policies, processes and structures that apply to the Company. It incorporates sections on the role and work of the Audit, Nominations, HSSE and Remuneration Committees in line with the Disclosure Guidance and Transparency Rules (DTR).

The Board continues to review and assess all policies and practices throughout the organisation considering changes to the Code and best practice principles, as well as new EU and UK Legislation introduced. The Board also keeps apprised of all revisions and market practice recommendations issued by institutional investor bodies such as the Institutional Shareholder Services, the Institutional Voting Information Service and the Pension and Investment Research Consultant. The Company has remained below the FTSE 350 for the past four consecutive financial years and, therefore, is subject to the provisions applicable to the Smaller Company Regime. The Company considers that it is compliant with all provisions of the Code, unless highlighted otherwise in this report.

BOARD OF DIRECTORS

The role of the Board

The Board is responsible for the overall conduct of the Group's business as follows:

- ▶ setting the Group's strategy and for the management, direction and performance of the business;
- ▶ monitoring and understanding the risk environment in which the Group operates;
- ▶ providing accountability to shareholders for the proper conduct of the business;
- ▶ safeguarding the long-term success of the Group and taking into consideration the interests of all stakeholders; and
- ▶ ensuring the effectiveness of and reporting on the structure of corporate governance.

The Board has an agenda for each Board meeting, which includes discussion and decision-making surrounding:

- ▶ verbal reports given by the Chairman of each committee on the committee's activities;
- ▶ overall Group strategy, new business, and long-term plans incorporating viability assessment;
- ▶ operational reviews;
- ▶ major capital projects;
- ▶ annual business plans and operating plans;
- ▶ the Group's financial structure, including tax and treasury;
- ▶ annual and half-year financial results and shareholder communications;
- ▶ system of internal control and risk management; and
- ▶ administrative matters including corporate governance issues.

The Board sets standards of conduct, which provide an ethical framework for the Group's business functions. While the Board focuses on strategic issues, such as financial performance, risk management, and other critical business concerns, it also has a formal schedule of reserved matters. These reserved matters, which are documented in a comprehensive list of authorisation levels and prior approval requirements for key corporate decisions and actions, are reviewed and approved by the Board regularly. The matters reserved were last reviewed in March 2016.

While all Directors have equal responsibility in terms of the law for managing the Group's affairs, it is the role of the executive management to run the business within the parameters established by the Board and to produce clear, accurate and timely reports to enable the Board to monitor and assess the Group's performance. The executive management draws on the expertise and experience of the non-Executive Directors.

All Directors are free to express their views and may ask that these be recorded in the minutes where appropriate.

Board composition during 2016

Name	Title	Held appointment during 2016	Committee chairmen and number of members
Executive Board members			
CT Elphick	Chief Executive Officer	✓	
AR Ashworth	Chief Operating Officer	Resigned 7 June 2016	
M Michael	Chief Financial Officer	✓	
GE Turner	Chief Legal and Commercial Officer	✓	
Non-Executive Board members			
RW Davis	Chairman	✓	Nominations (3)
GA Beevers		✓	HSSE (3)
M Salamon	Senior Independent Director	✓	Remuneration (3)
MD Lynch-Bell		✓	Audit (3)

The non-Executive Directors possess a range of experience and competencies and bring independent judgement to bear on issues of strategy, performance and resources that are vital to the success of the Group.

With the exception of Mr Beevers, the other non-Executive Directors are regarded as independent by the Board as defined in the Code, as was the Chairman on his appointment.

Board and Committee meetings

Five scheduled Board meetings and one special meeting of the Board were held during 2016, all in the United Kingdom. Attendance by Directors at Board and Committee meetings is shown below.

There are six formally constituted Committees of the Board, each of which have specific terms of reference. Those for the Audit, Remuneration, Nominations and HSSE Committees can be

viewed on the Group's website together with the matters reserved for the Board. The remaining two Committees (Standing and Share Scheme) facilitate the administration of the Board's delegated authority. Following the introduction of the EU Market Abuse Regulations in July 2016, an internal committee was set up to identify, control and disseminate inside information and to ensure set procedures and processes are in place and in line with EU legislation and financial conduct authority (FCA) regulations.

In the event that Board approval is required between Board meetings, Board members are emailed the details, including supporting information in order to make a decision. The decision of each Board member is communicated and recorded at the following Board meeting.

The terms of reference for each Committee require members to be renominated every three years (subject to annual re-election).

Attendance at Board and Committee meetings during 2016

Director	Board 6 held	Audit 5 held	Remuneration 4 held	Nominations 4 held	HSSE 4 held
RW Davis	6	5	4	4	–
CT Elphick	6	–	–	4	–
GA Beevers	6	5	–	–	4
M Salamon	5	–	3	3	3
MD Lynch-Bell	6	5	3*	–	–
M Michael	6	–	–	–	–
GE Turner	6	–	–	–	4
AR Ashworth (resigned 7 June 2016)	1	–	–	–	–

*Mr Lynch-Bell was appointed a member of the Remuneration Committee with effect from 14 March 2016.

Non-Executive Directors' meetings

Before each scheduled Board meeting, the non-Executive Directors meet independently of the Executive Directors, in accordance with the practice adopted by many listed companies. During the year, four such meetings were held.

Chairman and Chief Executive Officer

A clear separation is maintained between the responsibilities of the Chairman and the Chief Executive Officer. This separation was established during 2007 with the appointment of Roger Davis as Chairman.

The Chairman is responsible for creating the conditions for the effective working of the Board. The Chief Executive Officer is responsible for the leadership, operations and management of the Group within the strategy and business plan agreed by the Board. Their individual responsibilities, together with the responsibilities of the Senior Independent Director (SID) and non-Executive Directors are detailed on the following pages.

UK Corporate Governance Code Compliance continued

Roles of the Chairman and Chief Executive Officer

Chairman, Roger Davis	Chief Executive Officer, Clifford Elphick
The effective operation and leadership of the Board and setting the highest standards of corporate governance.	Developing a business strategy for the Group to be approved by the Board on an annual basis.
Providing strategic guidance to the executive team.	Producing the business plans for the Group to be approved by the Board on an annual basis.
Setting the agenda, style and tone of Board discussions.	Overseeing the management of the executive resource and succession planning processes and presenting the output from these to the Board and Nominations Committee annually.
Through the Nominations Committee, ensuring that the Board comprises individuals with appropriate skill sets, experience and knowledge.	Ensuring that effective business and financial controls and risk management processes are in place across the Group, as well as compliance with all relevant laws and regulations.
Ensuring that the Company maintains effective communication with shareholders and that the Board understands their views and concerns.	Making recommendations to the Board on the appropriate delegation of authority within the Group.
Working with the Chief Executive Officer to ensure that the Board receives accurate and timely information on the performance of the Group.	Keeping the Board informed about the performance of the Group and bringing to the Board's attention all matters that materially affect, or are capable of materially affecting, the performance of the Group and the achievement of its strategy.
Leading the evaluation of the performance of the Board, its Committees and individual Directors.	Developing, for the Board's approval, appropriate values and standards to guide all activities undertaken by the Group.
Encouraging a culture of openness and discussion to foster a high-performing collegial team of Directors.	Providing clear and visible leadership in responsible business conduct.
Ensuring that relevant stakeholder and shareholder views, as well as strategic issues, are regularly reviewed, clearly understood and underpin the work of the Board.	
Facilitating the relationship between the Board and the Chief Executive Officer.	
Ensuring that adequate time is available for discussion on all agenda items.	

Roles of the Senior Independent Director and non-Executive Directors

Senior Independent Director based in the UK, Mike Salamon	Non-Executive Directors
Acting as a sounding board for the Chairman.	Scrutinising the performance of management in meeting agreed goals and objectives and monitoring the reporting of performance.
Serving as an intermediary for other Directors if necessary.	Reviewing the integrity of financial information and determining whether internal controls and systems of risk management are robust.
Being available to shareholders if concerns they have raised with the executive team and/or the Chairman have not been satisfactorily resolved.	Determining the Company's policy for executive remuneration, as well as the remuneration packages for the Chairman and Executive Directors through the Remuneration Committee.
	Providing a wide range of skills and independence, including independent judgement on issues of strategy, performance and risk management.

BOARD SKILLS, BALANCE AND INDEPENDENCE

As a mining company, the efficiency of the day-to-day operations, in both the medium and long term, is essential to the Group's progress in producing shareholder value.

Knowledge of the diamond industry is crucial to foster new business opportunities and to enhance the Group's operations in cutting and polishing and sales and marketing strategies.

Knowledge of financial markets are also necessary to ensure fulfilment of the Group's strategy. The biographies, which can be found on pages 62 and 63, provide more information on each Director's competencies. All Directors allocate sufficient time to the Group to fulfil their responsibilities effectively.

The Company complies with the requirement of the Code that there should be a balance of Executive and non-Executive Directors so that no individual or group can dominate the Board's decision-making.

Non-Executive Directors should be independent in character and judgement. All four non-Executive Directors are considered by the Board to be independent of management and the Group. In applying the independence test, the Board considers relationships with management, major shareholders, subsidiary and associated companies and other parties with whom the Company transacts business against predetermined materiality thresholds.

The letters of appointment for the non-Executive Directors and the contracts of the Executive Directors are available for inspection at the place of business of the Company in London.

The Board annually reviews the composition and chairmanship of its primary Committees, namely the Audit, Remuneration, Nominations and HSSE Committees.

APPOINTMENTS AND RE-ELECTIONS TO THE BOARD (SEE ALSO BOARD DIVERSITY ON PAGE 70)

The Code requires there to be a formal, rigorous and transparent procedure for the appointment of new Directors, which should be made on merit, against objective criteria and with due regard to the benefits of diversity on the Board. Since 2007, recruitment to the Board has been based on recommendation; therefore, no outside consultants have been engaged. The Board currently comprises a broad and highly relevant skill set and the Nominations Committee will continue to make appointments based on merit while considering diversity and the specialist skill set which is required by the business.

The Nominations Committee's section of this report is set out on pages 80 and 81.

It is required that all Directors retire at the AGM and, if appropriate, offer themselves for re-election in accordance with Code provision B.7.1. This practice will continue for future re-elections. The Nominations Committee has considered and concluded that the Board has demonstrated commitment to its role. The committee is also satisfied that the collective skills, experience, background and knowledge of the Company's Directors enables the Board and its Committees to conduct their respective duties and responsibilities effectively.

CONTINUING BOARD DEVELOPMENT, INDEPENDENT PROFESSIONAL ADVICE AND THE COMPANY SECRETARY

Board evaluation

Aim

The Board understands the importance of ensuring that excellent standards of behaviour and governance are maintained, not only by the Directors, but integrated through all levels of the Group.

One of the overarching objectives of the 2016 Board evaluation was to carry out a comprehensive review on the effectiveness of the Board, not only as a unit, but also to assess and evaluate the contributions made by individual Directors.

The Board evaluation exercise looked at the composition of the Board and Committees of the Board; conduct and decision-making; how strategy is approached and addressed; risk management, management information and reporting; training, development and succession planning; and internal and external communication.

It also evaluated specific issues raised in the 2015 evaluation, such as succession planning, risk management and external communications.

Approach

In line with best practice on Board evaluation, as set out in provision B.6.2 of the Code, the Board appointed Bruce Wallace Associates to undertake an externally facilitated independent review of Board effectiveness during November and December 2016. The scope of the 2016 evaluation review was agreed with the Chairman and Company Secretary and implemented by means of a questionnaire. The questionnaire was sent to each Director and their responses were collated by Bruce Wallace Associates who then presented their analysis, findings and recommendations in a report to the Board.

Analysis

The report from Bruce Wallace Associates to the Board noted that considerable progress had been made addressing recommendations in the 2015 Board evaluation. In particular, risk management and external communications were identified in the 2016 Board evaluation as the two main areas where the Board had performed well. In particular there had been an improvement in the reporting and communication of risk management.

UK Corporate Governance Code Compliance continued

The Nominations Committee spent a substantial amount of time focusing on Board and Senior Management succession planning and meeting with potential candidates to ensure the composition of the Board remained 'fit for purpose' and in line with good governance standards.

In addition, risk management was categorised as an ongoing item on the agendas of the scheduled Board and Audit Committee meetings with regular updates and assessment reports being received from the external auditors and the internal audit control team.

Next step

The findings and recommendations have been discussed with the Board by the Chairman. The Board agreed that continued focus on developing succession plans was key. The Board also confirmed that internal communications would also be considered for further improvements.

Independent advice

All Directors are aware that they may take independent professional advice, at the expense of the Company, in the conduct of their duties, subject to prior consultation with the Chairman. Furthermore, all Directors have access to management and the advice and services of the Company Secretary. The Company Secretary is accountable to the Board for ensuring that all governance matters are complied with and assisting with professional development as required.

Board-approved arrangements ensure that new Directors receive a full, formal and tailored induction upon joining the Board. In addition, ongoing support and resources are provided to Directors, enabling them to extend and refresh their skills, knowledge and familiarity with the Group. Professional development and training is provided through three measures:

Company Secretary

An independent firm of Chartered Secretaries in Public Practice advises the Company Secretary. Bruce Wallace Associates is engaged to ensure that all company secretarial and governance issues are attended to and the Board is kept apprised of all compliance and best practice matters throughout the year.

Bruce Wallace also attended to the Board evaluation exercise in 2016.

CONFLICTS OF INTEREST

The UK Companies Act requires Directors to avoid any situation where they may have a direct or indirect interest that conflicts, or may conflict, with the Group's interests, unless approved by the non-interested Directors. In accordance with this Act, the Company operates a procedure to ensure the disclosure of conflicts and, if appropriate, for the consideration and authorisation of them by non-conflicted Directors. The Board maintains a register of 'conflicts of interest' that it reviews annually

(most recently in March 2017). The Company voluntarily complies with this requirement.

DEALINGS IN SHARES AND THE EU MARKET ABUSE REGIME

The Company has revised its Share Dealing Policy and reporting procedures in line with the EU Market Abuse Regulations implemented in July 2016 (Regulations). The Directors and Senior Executives carried out formal training and processes were put in place to ensure all persons discharging managerial responsibilities and their persons closely associated and insiders (as defined in the Regulations) were informed of their obligations and sanctions for non-compliance under the new Regulations.

DIRECTORS' REMUNERATION

While the Board is ultimately responsible for Directors' remuneration, the Remuneration Committee, consisting of independent non-Executive Directors, is responsible for determining the remuneration and conditions of employment of Executive Directors, as well as the Chairman. The Directors' Remuneration policy which will be put before shareholders for approval at the 2017 AGM has been reviewed by the Remuneration Committee and Kepler, the remuneration consultants. The policy has been updated in line with market practice and includes such provisions as 'malus' and 'clawback' as well as shareholding guidelines for Executive Directors. The details of all Directors' remuneration are covered in the Directors' Remuneration Report and the Annual Report on Remuneration on pages 94 to 104.

BRIBERY ACT

In 2015, Group internal audit carried out a review of the Anti-Bribery and Corruption Policy to ensure continued compliance with the UK Bribery Act. The policy was updated, in consultation with the Group's legal advisers, Linklaters, to incorporate the three areas of improvement identified during the review, thereby ensuring the policy retained robust compliance and diligence procedures. The Board approved the updated Anti-Bribery and Corruption Policy in June 2016 which has now been rolled out to all operations.

The Group's terms of business require all customers and third parties with whom business is transacted to adopt the same zero tolerance approach to bribery and corruption as implemented by the Board.

BOARD DIVERSITY

The Board continues to support diversity and strives to improve the gender balance within the Group with an increasing number of suitably qualified females being employed at senior levels throughout the organisation.

More information on gender-based employment is contained in the Sustainable Development Review on pages 55 and 56.

COMMUNICATION OF BUSINESS DEVELOPMENT DURING THE YEAR



Detailed information on the Group's business developments and projects can be found on the Company's website in the investors section, where all published information and shareholder communication is available. This includes trading updates; year-end and half-year results; resource and reserve statements, and all other announcements.

ACCOUNTABILITY AND AUDIT

Information and financial reporting systems

The Board is conscious of its responsibility to present a fair, balanced and understandable assessment of the Group's position and prospects and is satisfied that the Strategic Report on pages 2 to 59 has met this obligation. The Responsibility Statement of the Directors in respect of the Annual Report and Accounts is set out on page 112.

The Board is supplied in a timely manner with information in the form and of a quality appropriate to enable it to discharge its duties. Financial reporting to the Board is continuously modified and enhanced to cater for changing circumstances. The Group's comprehensive planning and financial reporting procedures include detailed operational business plans for the year ahead and a three-year rolling plan. The Board reviews and approves the Group's annual business plan.

These are prepared in co-operation with all Group functions based on specified economic assumptions. Performance is monitored and relevant action taken throughout the year through monthly reporting of KPIs and updated forecasts for the year, together with information on key risk areas.

In addition, routine management reports on an operational and consolidated basis, including updated forecasts for the year, are prepared and presented to the Board. These reports form the cornerstone of the Group's system of internal control. Detailed consolidated management accounts, as well as an executive summary, are circulated prior to each scheduled Board meeting. Between Board meetings, summary update reports covering matters such as operational performance, sales results, cash flow and progress on strategic issues are circulated to Board members and Senior Executives.

Internal control

The Board of Directors has responsibility for the Group's overall approach to risk management and internal control, which are embedded in all key operations. In accordance with the Guidance on Risk Management, Internal Control and Related Financial and Business Reporting Guidance published by the Financial Reporting Council in September 2014 (the Risk Guidance), the

Board has defined the processes adopted for its ongoing monitoring and assessment and relies on reviews undertaken by the Audit Committee throughout the year, as well as the approval of the Annual Report and Accounts. In addition, regular management reporting and a balanced assessment of key risks and controls, is an important component of Board assurance.

The principal aim of the system of internal control is the management of business risks that significantly threaten the fulfilment of the Group's business and strategic objectives, with a view to enhance the value of shareholders' investments and safeguarding assets. The internal control systems have been designed to manage, rather than eliminate, the risk of failure, to achieve business objectives and to provide reasonable but not absolute assurance that the Group's business objectives will be achieved within the risk tolerance levels identified by the Board. The Directors have reviewed the effectiveness of the system of internal control. For the review, the Audit Committee considered reports dealing with internal audit plans and outcomes, as well as risk logs and sign-off from external audit and management representations. These did not reveal any significant findings or weaknesses. A full report of the work carried out by the Audit Committee on behalf of the Board is set out in the Audit Committee Report on pages 74 to 79.

Internal audit

The Group internal audit function, as an independent assurance provider, is an important element of the overall process by which the Audit Committee and the Board obtain the assurance it requires that risks are being effectively managed and controlled.

Group internal audit, reporting directly to the Audit Committee, is responsible for co-ordinating the Group's risk-based approach to internal audit and to evaluate the effectiveness and contribute to the improvement of risk management, controls and governance systems.

A risk-based internal audit plan for 2016 was approved by the Audit Committee. The risk-based audit plan covers all operating units, focusing in particular on the principal risks. It involves discussions with management on the risks identified in the local and Group risk registers, emerging risks, operational changes, capital projects and related internal controls identified in the risk self-assessment process. Findings and agreed actions are reported to management and the Audit Committee.

UK Corporate Governance Code Compliance continued

Internal audit services are provided by means of a co-sourced agreement with KPMG managed through the Group internal audit function. The objective of the co-sourced agreement is that KPMG will perform certain internal audits on behalf of the Group internal audit as and when required. No such services were required during the current year.

External audit

A principle of the Code is that the Board should establish formal and transparent arrangements for considering how it should apply the financial reporting and internal control principles and for maintaining an appropriate relationship with the Group's external auditors, EY. These responsibilities are delegated to and discharged by the Audit Committee, whose role is defined on pages 74 to 79.

RISK ASSESSMENT AND MANAGEMENT

The Board, through the Audit Committee, considers effective risk management as an essential element of professional management and has implemented robust risk assessment and internal control systems across the Group.

In accordance with the Risk Guidance, a process has been established for continually identifying, evaluating and managing the Group's principal risks. The Group's Risk Management Policy aims to cover and review all important risks faced by the Group, including, but not limited to, operational, financial, commercial, legal, regulatory and compliance risks, which could undermine the Group's ability to achieve its strategic and business objectives.

These risks are monitored continually and formally reviewed annually. A more comprehensive report of the Group's principal risks and how these are managed and/or mitigated can be found on pages 18 to 24 of the Strategic Report.

The Company has a value-driven approach to meet its objective of ensuring it operates in a stable environment. Through monitoring the locations in which we operate, enhancing the Group's assets and protecting employees and the surrounding ecosystem, the Group is able to uphold its processes in turn creating greater shareholder value and enhancing the Group's moral reputation.

The Group's operations perform regular risk assessment reviews and maintain risk registers. Objectives in the business plan are aligned with risks and a summary of the key risks, related internal controls, accountabilities and further mitigating actions are tabled and approved by the Audit Committee. The Committee at times

delegates its authority to the Board for completeness. The Audit Committee and the Board, where appropriate, are kept informed on progress against the plans and any significant changes to review the risk profile. This enables the suitable management and non-Executive Directors to holistically review the risk, mitigate and implement controls as necessary.

INVESTMENT APPRAISAL

Capital expenditure is managed through a budgetary process and authorisation levels. For expenditure beyond specified levels, detailed written proposals are submitted to the Board. There is an approval procedure for investment, which includes a detailed calculation of return based on current assumptions that are consistent with those included in management reports.

Post-investment reviews are carried out after the project is completed and, for material projects, steering committees are established to monitor the progress against the approved plan.

Commercial, legal and financial due diligence is carried out, using external consultants as appropriate, in respect of acquisitions and disposals.

WHISTLEBLOWING PROGRAMME

The Company has formal means of reporting suspected fraud, corruption and irregularities via independently operated and confidential toll-free phone hotlines in each country in which the Group operates. Employees can report any breach of the Group's business principles, including, but not limited to, bribery, breaches of ethics and fraud.

All incidents reported are fully investigated, and the results are reported to the boards of local operations and the Group's Audit Committee. To raise awareness of the hotline throughout the Company, literature is issued to employees detailing the whistleblowing tool and relevant contact details. Group internal audit periodically reviews the design and effectiveness of the hotline and reports the results to the Audit Committee.

The whistleblowing reporting process was reviewed in 2016 to strengthen the independence of the process whereby all whistleblowing incidences reported are distributed by the Group internal auditor and Company Secretary for investigation by the relevant operations. In addition, the access of automated reporting systems was enhanced.

The Board is satisfied that the whistleblowing programme is being utilised in the correct manner by concerned individuals and

that all queries raised during the year have been properly investigated and reported.

DIALOGUE WITH SHAREHOLDERS

Communication with industry analysts, institutional investors and shareholders is of great importance to the Board. Understanding the views of our stakeholders and shareholders has proven to be highly beneficial to the Group. The responsibility of investor relations is that of the Chief Legal and Commercial Officer, Glenn Turner, who is based at the Company's London office.

Investor seminars and analyst presentations, including those following the Group's announcement of the year-end and half-year results are available as webcasts and other presentations made to institutional investors and at external events are available on the Company's website.

Any concerns raised by shareholders in relation to the Group and its affairs are communicated to the Board and a summary of shareholders' views are tabled at each Board meeting.

Glenn Turner keeps in contact with the Company's institutional and other shareholders, as well as industry experts on a regular basis. It is his task to ensure there is a continuous flow of reliable information between the Company and its investors. Glenn Turner is frequently invited to speak at National and International Diamond Mining Forums and the Investor Relations team organise regular site visits to Letšeng for both investors and analysts.

The Executive Directors conduct quarterly roadshows to engage with several of the Group's larger investors creating a suitable platform for them to express any concerns.

The shareholder base comprises 138.4 million issued ordinary shares of US\$0.01 each. There are 187 institutional shareholders that hold 126.3 million shares (91%) and 370 private shareholders who hold 12.1 million shares (9%).

The Company's Senior Independent Director, Mike Salamon, is available to shareholders if contact through normal channels fails to resolve their concerns, or if such contact would be inappropriate.

CONSTRUCTIVE USE OF THE AGM

The Code strongly encourages boards to use the AGM to communicate with all investors. All Directors attend the AGM, and shareholders are invited to ask questions during the meeting and

to meet Directors after the formal proceedings have closed. Shareholders attending the Company's next scheduled meeting will be advised as to the level of proxy votes received, as well as the percentages for and against in respect of each resolution.

If the Board considers that a significant proportion of votes have been cast against any resolution, the Directors will explain how they intend to engage with shareholders to assess their concerns. The results of the resolutions will be announced through the Regulatory News Service and on the Company's website.

All shareholders can access the Group's annual and half-year reports; trading updates; and other published information about the Group through the Company's website.

Details of the resolutions to be proposed at the AGM can be found in the Notice of AGM. In accordance with the Code, the Notice of AGM and relevant papers will be sent to shareholders a minimum of 20 business days before the meeting. The 2017 AGM will be held on Tuesday, 6 June 2017.

SHAREHOLDERS

Majority interest in shares

On 15 February 2017, the Company was notified of the following major interests (at or above 3%) in the issued ordinary shares of the Company in accordance with the DTR 5:

Shareholders	Number of ordinary shares	% shareholding
Graff Diamonds International	20 906 699	15.11
Lansdowne Partners	20 721 413	14.98
Majedie Asset Management	9 628 586	6.96
Gem Diamonds Holdings	9 325 000	6.74
Aberforth Partners	8 074 133	5.84
Lazard Asset Management	6 998 831	5.06
FMR LLC	6 295 461	4.55
BlackRock	5 368 722	3.88
Hosking Partners	5 187 487	3.75
Dimensional Fund Advisors	4 348 562	3.14

Audit Committee



Michael Lynch-Bell, Chairman

The Committee comprises:

- ▶ MD Lynch-Bell – Chairman
- ▶ RW Davis
- ▶ GA Beevers

COMPOSITION, EXPERIENCE AND SKILL SET

In accordance with provision C.3.1 of the Code, at least two members of the Audit Committee should be non-Executive Directors, independent in character and judgement, and free from relationships or circumstances which are likely to affect, or could appear to affect, their judgement.

The skill set of the Audit Committee satisfies that all accounting, risk and internal control issues are addressed in such a manner to ensure high standards of corporate governance and to continue to uphold shareholders' interests.

Michael Lynch-Bell has recent and relevant financial experience for the purpose of the Code, having spent 27 years as a partner at Ernst & Young (EY) of which six years were spent leading its Global Oil and Gas and Mining transaction advisory practices. For more information about Michael's experience, refer to the directorate pages 62 and 63.

Roger Davis brings many years of business experience across international banking and financial sectors having previously served on the Barclays Plc Board.

Gavin Beevers possesses a wealth of sector-specific experience relevant to the nature of the Group's operations, having previously served as a Director of operations at De Beers.

TERMS OF REFERENCE

The Audit Committee's Terms of Reference were updated in 2015 in line with the new provisions introduced by the Code applicable to the smaller company regime. These were again reviewed in March 2017 to ensure they continue to be fit for purpose and in line with best practice and governance principles. They can be viewed on the Company's corporate website.



MEETINGS

Five meetings of the Audit Committee were held in 2016. The Chief Executive Officer, the Chief Financial Officer, the Group's internal auditor, and a representative of the Group's external auditors attend each meeting by invitation. Other Directors of the Company and Senior Executives may also attend by invitation to speak, but not vote, at a meeting. The full Committee also met with the Audit Partner without the Executive Directors present during the year. Mr Lynch-Bell, as Chairman of the Committee, allocates a significant amount of time to this role. In addition to chairing formal meetings of the Committee and attending sessions with the external auditors, he travelled to Johannesburg in 2016 where he met with the Chief Financial Officer and the financial team, as well as the Group internal auditor, in order to discuss the financial controls and audit activities of the Group. A further visit in February 2017 was supplemented with a visit to the Group's operation in Lesotho. Similarly, Gavin Beevers carried out site visits during the year to the Group's operations in Lesotho and Botswana, thereby gaining an update to operational matters and activities on the ground. Such meetings and site visits enable the Chairman and the Committee to uphold a comprehensive understanding of corporate and finance developments and activities, any associated risks, as well as the controls in place at the operations. Following each meeting, the Committee communicates its main discussion points and findings to the Board.

ROLE AND ACTIVITIES

The principal functions, in line with the Committee's Terms of Reference, are listed below, along with the corresponding activity and performance during 2016.

Role	Activities in 2016
<p>To provide advice to the Board on whether the Half-yearly Report and Annual Report and Accounts, are fair, balanced and understandable and to monitor the integrity of the published financial information of the Company and review and report to the Board on the significant financial reporting issues and judgements made in connection with the preparation of the published financial information of the Company</p>	<p>The Committee formally reviewed the Group's Annual Report and Half-yearly Report and considered that they present a fair, balanced and understandable assessment of the Group's performance and prospects and provide information necessary for shareholders to assess the Company's performance, business model and strategy.</p> <p>The Committee reviewed the key auditing and financial reporting matters which typically focused on areas of significant judgement, estimation or accounting policy selection. These areas of focus were assessed through discussions with the Group's Audit Partner and Group CFO, ahead of and/or during Committee meetings, in which the Committee, where appropriate, challenged the basis for such judgements and estimates. Details of the significant matters considered by the Committee in respect of the 2016 Half-yearly and Annual Report are set out on pages 76 and 77.</p> <p>The Committee reviewed and assessed the systems and processes in place required to formulate the Viability Statement and support its conclusions and recommended the statement issued in the Annual Report to the Board for approval.</p> <p>The Committee considered institutional comments raised on previous Annual Reports for relevance and incorporation into subsequent Annual Reports.</p> <p>Further published information which was reviewed by members of the Committee included the following:</p> <ul style="list-style-type: none"> ▶ quarterly trading announcements published; and ▶ report on payments to governments for the year ended 31 December 2015, being a new report requirement to satisfy the requirements of the Disclosure and Transparency Rules of the Financial Conduct Authority in the United Kingdom.
<p>To review the effectiveness of the internal control and risk management processes and provide input to the Board's consideration of risk and risk appetite</p>	<p>The Committee assesses the Company's risk management systems and internal controls on an ongoing basis. As part of this, the Group internal auditor attends all meetings. The Committee received reports from the external auditors and the Group's internal auditor on their assessment of the control environment. The Committee was provided with updates on the Group's risk management activities and the members considered the risk and control implications on an ongoing basis. Additionally, the Board received presentations and reports by management on operational and financial performance each quarter that allowed for assessment of risk and internal controls.</p> <p>The Committee meetings during the year included presentations by EY regarding planning and outcomes of the annual audits and interim review.</p>
<p>To review the adequacy of the Company's whistleblowing system, controls for ethical behaviour and prevention of bribery, and procedures to detect fraud</p>	<p>The Committee reviewed matters reported to the external whistleblowing hotline and reports on the findings of the investigations. There were no matters reported which were considered significant. Following findings and recommendations by the Group's internal auditor, the Anti-Bribery and Corruption Policy was updated, which the Committee considered and approved. There were no bribery matters reported during the year.</p> <p>All incidences of fraud and irregularities together with any reports on investigations were reviewed and the Committee monitored the implementation of corrective controls where appropriate.</p>
<p>To give consideration to relevant laws and regulations, the provisions of the Code and the requirements of the UK Listing Rules</p>	<p>The Committee received adequate timely information from EY relating to significant audit, accounting and governance developments during the year. The Company Secretary provided assurance with regard to compliance with the London Stock Exchange, the UK Listing Authority and other regulatory requirements in the preparation of the Annual Report and Regulatory News Services announcements.</p>

Audit Committee continued

Role	Activities in 2016
<p>To monitor and review the effectiveness and independence of the internal audit function</p>	<p>The Group's internal auditor attends all meetings and reports directly to the Committee. After every meeting, the Committee meets with the Group internal auditor independently. Outside of meetings, the Chairman met with the Group internal auditor to discuss the strategy behind the internal audit function and the results of completed audits. At the end of the previous year the Committee considered and approved the internal audit plan that included audits of an operational, financial and governance compliance nature across the Group. During the year the Committee reviewed findings from these internal audits, the actions taken to implement the recommendations made in the reports and the status of progress against previously agreed actions. The Committee reviewed and approved the 2017 internal audit plan.</p>
<p>To review the quality and effectiveness of the external audit and the procedures and controls designed to ensure auditor independence</p>	<p>During the year the Committee considered the performance and audit fees of the external auditor, and the level of non-audit work undertaken, and recommended to the Board that a resolution for the reappointment of EY for a further year as the Company's auditor be proposed to shareholders at the AGM in June 2016.</p> <p>In advance of the 2016 audit, the Committee reviewed and approved the external auditor's audit plan and assessed the appropriateness of the audit strategy, scoping, materiality and audit risks.</p> <p>The Committee approved the audit fees as part of the audit planning process.</p> <p>The Committee approved an updated policy on the provision of non-audit services by the external auditor having considered the Auditing Practices Board's Ethical Standards.</p> <p>The Committee reconsidered the requirement for the rotation of external auditors through a tender process. Following its assessment, the Committee has recommended the reappointment of EY at the AGM on 6 June 2017.</p> <p>Details of the Committee's assessment of the auditor's independence, its assessment of their effectiveness and its audit firm rotation considerations are provided on pages 78 and 79.</p>

Significant issues considered by the Committee relating to the 2016 financial year

The Committee considers the following to be the significant issues in respect of the Group's financial statements, based upon its interaction with management. These areas also represent significant audit risk areas for EY and, accordingly, the Committee was provided with detailed reports and conclusions on these areas to ensure there are no inconsistencies or misstatements of the financial statements.

<p>Revenue recognition</p>	<p>The judgement applied to revenue recognition is based on the timing of risks and rewards of ownership transfer on rough diamond sales and in particular on the uplift element of rough diamonds sold into partnership arrangements. This is an area of higher audit risk and accordingly, the Committee received detailed verbal and written reports from EY regarding management's appropriate application of its revenue recognition policy.</p>
<p>Critical accounting estimates and judgements applied to the 'production start date' of the Ghaghoo mine</p>	<p>The judgement in relation to 'production start date' is to determine when a mine moves from its construction phase into its production phase. The criteria used to assess the start date are determined by the nature of each mine's construction. Relevant criteria are considered to assess when the mine is substantially complete and ready for its intended use and moves into the production phase at which point the capitalisation of certain mine construction costs cease and depreciation of the mine asset commences. The Committee addressed such issues through reports submitted by management. This created a platform for open discussion where management communicated the reasoning behind their views to conclude that 'production start date' had not yet been reached.</p>

Assessing the Ghaghoo development asset for impairment

The judgements in relation to asset impairment largely relate to the assessment of whether impairment indicators exist and key assumptions used in determining recoverable amounts. The Committee addresses these matters through receiving reports from management outlining the basis for the assumptions used, of which the business plan is the most significant, which is approved by the Board.

During the half-year review, the Group recognised an impairment charge of US\$40.0 million for the Ghaghoo asset which was outside the normal course of business. The Committee carefully reviewed this impairment to ensure that the judgements applied by management were reasonable and any accounting guidance followed correctly. A special Audit Committee meeting was convened to consider this matter and thereafter the matter referred to the Board. The Committee and Board agreed that as a result of the continued market uncertainty experienced the ongoing difficult market conditions for Ghaghoo's production, strengthening of the Botswana pula against the US dollar and the challenges in the operation reaching its targeted production, that the impairment charge be recognised. The Committee also concluded that assumptions and judgements taken by management with regard to diamond prices and market recovery in the short term were on a basis consistent with market indications.

During the second half of 2016, the market for the Ghaghoo production saw an even further decline and the Board concluded to place the mine on care and maintenance in 2017. Following the same approach as the half-year, the Committee and Board agreed with management's recommendation to realise a further impairment of the Ghaghoo assets, and a further US\$130.8 million impairment charge was recognised, resulting in a total impairment charge of US\$170.8 million for the year.

ANNUAL REVIEW

The Committee's performance is reviewed through the broader Board evaluation process and, at least annually, the Committee reviews its own Terms of Reference to ensure it is operating at maximum effectiveness and recommends any changes it considers necessary to the Board for approval.

Overall, the Board evaluation performed during the year concluded that the Committee is responding appropriately to its Terms of Reference. Priorities for the forthcoming year will include continuing to monitor the effectiveness of risk management processes and internal controls and to further review the quality and effectiveness of the external audit and the procedures and controls to ensure auditor independence.

RISK MANAGEMENT AND INTERNAL CONTROLS

Risk management

The Committee continued to consider the process for managing risk within the business and assisted the Board in relation to compliance with the Code and development of the risk appetite framework.

The Committee reviewed, and considered appropriate, the updated Group Enterprise Risk Management Policy which forms the basis of developing the strategic risks of the Group once all operational risks are assessed. The Committee also considered management's response to strategic risk, including the level of assurance provided around the risk and how the risk is tracked using key risk indicators.

The Committee also receives management reports satisfying the adequacy of asset and liability insurance cover across the Group and in addition, during the year, satisfied itself with the adequacy of the level of Director and Officer's liability insurance, when compared to market practice, through a presentation by the Company's insurance brokers.

Further information on the strategic risks and uncertainties and risk management process is included within the Strategic Report on pages 2 to 59.

Audit Committee continued

Internal controls

The Board has overall responsibility for the Group's systems of internal control and for regularly reviewing the effectiveness of those systems. The Committee assists the Board in reviewing the systems of internal control. The primary responsibility for the operation of these systems is delegated to management. Such systems can only provide reasonable and not absolute assurance against material misstatement or loss. Key control procedures are designed to manage rather than eliminate risk.

The Committee regularly reviews the adequacy and effectiveness of the Group's internal control procedures through regular reports from the Group's internal auditor and chief financial officer, and through consideration of the external auditor's audit reports and face to face discussion between the Audit Partner, the Committee Chairman and Committee members.

For 2016, the Committee remained satisfied that no material weaknesses in internal control systems were identified. Whilst being satisfied that controls and risk management remain appropriate for the Group's activities, the Committee continues to undertake a thorough review and to challenge internal controls, risk management procedures and internal audit strategy to ensure that its practices develop and remain appropriate. When internal control reviews identified necessary or beneficial improvements, appropriate steps have been taken to ensure the control environment is effective. This includes systems to track management's responses to the areas for improvement and follow-up internal audits to test the implementation.

Whistleblowing

The Group has arrangements in place that enable employees to raise concerns in confidence about any possible risks to employees or the Company. The Committee considers the process and procedures each year and is of the view that they are operating appropriately and that colleagues are aware of and trust the process.

OUR AUDITORS

Internal

In 2014, the Group established an internal audit function, staffed by a Group internal auditor who reports directly to the Committee. On approval of the internal audit plan for the year, the Committee reviews findings from internal audit reports, the actions taken to implement the recommendations made in the reports and the status of progress against previously agreed actions. All internal audit reports are available to the Committee.

At the end of every Committee meeting, the Committee meets with the internal auditor independently to obtain assurance that management is adequately addressing the internal audit report findings.

External auditor Engagement

The Committee is responsible for agreeing the terms of the engagement letter. Throughout the year, the Committee received reports from EY on its plans, progress and results of its review and audit. The Committee considers carefully the scope of planned work and the assessment of risk and materiality on which it is based. The Committee reviews the negotiated audit fee arrangements to ensure that there is an appropriate balance between the scope of work and the cost of assurance. The Committee's aim is to support a robust and effective audit and strong reporting lines to the Committee.

Effectiveness and quality

Audit quality is reviewed throughout the year and in 2016 the Committee considered the effectiveness, objectivity, skills, capacity and independence of EY. In forming its assessment of the effectiveness of the audit, prior to the audit, the Committee received formal planning documentation from EY regarding the proposed audit strategy and the Chairman met separately with the Audit Partner to discuss the audit strategy in detail. These forums enabled the Committee to assess the extent to which the audit strategy was appropriate for the Group's activities and addressed the risks the business faces. In addition, the following factors were discussed:

- ▶ independence;
- ▶ materiality;
- ▶ the auditor's risk assessment;
- ▶ the extent of the Group auditors' participation in the subsidiary component audits;
- ▶ the limited audit firms representation in Lesotho and Botswana;
- ▶ the planned audit procedures to mitigate risks; and
- ▶ regulatory updates affecting the Company.

Following the audit, EY presented its findings to the Committee and met separately with the Committee Chairman to discuss key audit judgements and estimates and its report. This provided an opportunity to assess the audit work performed, understand how management's assessments had been challenged and assess the quality of conclusions drawn. The Committee also made enquiries of Senior Management to obtain their feedback on the audit process and considered this feedback in its assessment.

Each of the key attributes for audit effectiveness was considered to be appropriately met by the Group's auditors and the Committee considers the external audit to be robust and effective.

Independence, objectivity and fees

The Committee seeks to ensure the objectivity and independence of the auditor through:

- ▶ focus on the assignment and rotation of key personnel;
- ▶ the adequacy of audit resource; and
- ▶ policies in relation to non-audit work.

The Senior Audit Partner serves no more than five years continuously and the independent review partner serves no more than seven years continuously. Other key partners serve for no longer than seven consecutive years. The Committee monitors the tenure of partners and senior staff as well as former employees working for the Company. Following completion of the 2015 audit, the Audit Partner, Mirco Bardella, rotated off the engagement and was replaced by Steven Dobson, a Senior Partner, which was approved by the Committee.

The Committee regularly monitors the other services being provided to the Group by its external auditor, and has approved a formal policy and sign-off process with management to ensure this does not impair their independence or objectivity. The policy was reviewed and updated during the year.

Other than in exceptional circumstances, management and the Committee do not expect non-audit fees to be in excess of fees for audit and audit-related services. The fees for such work amounted to US\$0.2 million in total. This was against external audit fees of US\$0.7 million representing approximately 29% of external audit fees. The significant non-audit engagements relate mainly to the half-yearly interim review and to a lesser extent corporate tax services. Full details are set out in Note 3 of the financial statements. A report on the level of non-audit work provided by the auditor is given to the Committee half-yearly.

The Committee has formally reviewed the work undertaken by EY throughout the Group and is satisfied that the advice it has received has been objective and independent.

Reappointment

EY has been the Group's external auditors for 10 years since the year ended 31 December 2006. The Company recognises the importance of audit independence and the requirements of audit rotation through tender. A full assessment was carried out during the year in relation to the tender of audit firms, the results of which identified that the requirement to rotate auditors every 10 years is a requirement of the EU Audit Regulation and Directive. As the Company is not subject to this Directive, as it is not a UK registered entity, it was concluded that it is not obliged to rotate its auditors. The Committee was satisfied that based on the audit effectiveness and quality assessment conducted, and the independence following the Audit Partner rotation, the audit would not be put on tender at this stage and that the Group will continue with EY.

Resolutions allowing the Board to reappoint and determine the external auditor's remuneration will therefore be proposed at the Company's AGM on Tuesday, 6 June 2017.

Nominations Committee



Roger Davis, Chairman

The Committee comprises:

- ▶ RW Davis – Chairman
- ▶ M Salamon
- ▶ CT Elphick

COMPOSITION AND MEETINGS

The Nominations Committee comprises two non-Executive Directors and one Executive Director. The Committee’s Terms of Reference provide for a formal and transparent procedure for the Committee to follow in executing its responsibilities. The Terms of Reference of the Nominations Committee were updated in September of 2015 to reflect the changes made to the Code in September 2014, and to further reflect current best practice. They were again reviewed in March 2017 to ensure they continued to be in line with good governance.

ROLE AND ACTIVITIES

Role	Activities in 2016
To review the structure, size and composition of the Board (including appropriate skills, knowledge, experience and diversity), and to make recommendations to the Board with regard to any changes that are deemed necessary	With the retirement from the Company and the Board of Mr Ashworth, the Chief Operating Officer, in June 2016, the Committee reviewed the structure and size of the Board and it was agreed that the Company had the optimum balance of skills and independence on the Board and therefore the appointment of the Chief Operating Officer would be best served as a non-Board position. The Chief Operating Officer is invited to attend all Board meetings.
To satisfy itself, with regard to succession planning, that plans are in place with regard to both Board and Senior Management positions	Short and long-term succession planning was a key focus for the Committee during the year. For the short term, an emergency succession plan was approved to ensure that suitably qualified and experienced executives and senior members of the management team would step in to fill vacancies arising from unforeseen circumstances and thereby provide business continuity. For the long term, the Committee considered suitable replacements for Mr Davis, the Chairman of the Board, as well as for Mr Beevers who has reached his 10-year tenure as a non-Executive Director. The Committee carried out an extensive search and interviewed a range of potential candidates with the appropriate skills, knowledge and experience to ensure any suitable replacement not only had the requisite skills and experience but also whose attributes complemented the current Board composition and structure.

Four meetings were held in 2016 with succession planning being the key focus for the Committee in 2016. Alan Ashworth retired as Chief Operating Officer and was replaced by Johnny Velloza who was considered a suitable candidate based on his operational experience and reputation within the industry. As reported at the 2016 AGM, the Chairman of the Board, Roger Davis, will be stepping down at the 2017 AGM as he has served a ten-year tenure. Gavin Beevers, a non-Executive Director, has also served a ten-year tenure on the Board and the Committee has been looking for suitable candidates to replace him. The Committee carried out an extensive search and interviewed a range of potential candidates with mining and technical experience. Due to the specific knowledge and experience required, it has proved difficult to find a suitable candidate that fulfils the Group’s requirements. Mr Beevers has agreed to remain in post (subject to re-election at the AGM). Mr Beevers has considerable technical skills and knowledge in operational mining and corporate social responsibility. His diligence, dedicated commitment and expertise are invaluable on site visits.

In the year ahead, the Committee will continue to assess the Board’s composition, evaluate the composition of the various Committees and monitor developments in corporate governance to ensure the Group remains at the forefront of good governance practices.

Role	Activities in 2016
To identify, nominate and recommend, for the approval of the Board, appropriate candidates to fill Board and Committee vacancies as and when they arise	The Committee considered that the reduced size of the Board following the retirement of Mr Ashworth was appropriate and agreed that the appointment of Mr Velloza as the Chief Operating Officer would be a non-Board position.
To recommend to the Board the re-election by shareholders at the AGM of any Director under the retirement and re-election provisions of the Company's by-laws	The Committee confirmed the stepping down of Mr Davis and Mr Beevers at the 2017 AGM. The Committee subsequently considered and approved that, subject to re-election at the 2017 AGM, Mr Beevers remain in post. The Committee recommended all other Directors for re-election to the Board at the forthcoming AGM.
To ensure all new Directors undertake appropriate training and induction to ensure that they are fully informed about strategic and commercial issues affecting the Company and the markets in which it operates as well as their duties and responsibilities as a Director	Mr Lynch-Bell's induction was completed during the year with the assistance of the Company Secretarial team. In addition, he visited the financial and internal audit teams in Johannesburg during the year and again in February 2017, together with a site visit to the Letšeng mining operation in Lesotho.
To keep under review potential conflicts of interests of Directors disclosed to the Company and develop appropriate processes for managing such conflicts if considered necessary	The Committee was satisfied with the process of disclosure of conflicts of interest and no instances of such conflicts arose during the year. The Directors are required to inform the Board of any potential or possible conflicts immediately and prior to Board meetings. The Register of Conflicts is circulated and approved each year and as and when any changes are reported.
To assist the Chairman of the Board with the implementation of an annual evaluation process to assess the overall and individual performance and effectiveness of the Board and its Committees	A questionnaire-based board evaluation was conducted by an external adviser to assess the performance and effectiveness of the Board and the Committees. The Committee reviewed the results to ascertain if there were any issues that may require addressing. A full summary of the evaluation process can be found on pages 69 and 70.

EXPERIENCE AND SKILLS OF THE DIRECTORS

The Committee is satisfied that the Directors add the relevant skills to the Board that is required for the Company to succeed in achieving its strategy of growth, value creation and sustainability through diamond mining. All the Directors worked in the mining and/or financial and capital market sector prior to joining the Group and their key skills and experience can be found in the directorate section, pages 62 and 63.

DIVERSITY

The Board acknowledges that diversity extends beyond the boardroom and supports management in its efforts to build diversity throughout the Group. It endorses the Group's policy to

attract and develop a highly qualified and diverse workforce, to ensure that all appointments are based on merit and recruitment activities are fair, non-discriminatory and that due diligence is performed. The Committee recognises that to further enhance the effectiveness of the Board there must be combined qualities, capabilities and skill set gained from different geographical and cultural backgrounds. It is also recognised that there is a shortage of suitable appropriate Directors currently in the market. The Nominations Committee continues to encourage and support diversity of business skills and experience. Details including the proportion of women in Senior Management, can be found in the Sustainable Development Review on pages 55 and 56.

HSSE Committee



Gavin Beevers, Chairman

The Committee comprises:

- ▶ GA Beevers – Chairman
- ▶ M Salamon
- ▶ GE Turner

COMPOSITION, EXPERIENCE, AND SKILL SET

The Committee members have a wealth of knowledge which supports the objectives of ensuring HSSE risks are mitigated and best practice is attained. Gavin Beevers, the Chairman of the Committee, and Mike Salamon have extensive experience in operational mining which not only enables a great understanding of current challenges within the industry, but provide the tools and expertise to overcome these challenges and to lead best practice. Glenn Turner, with his legal expertise has extensive knowledge of local and international law, enabling the Company to have the relevant policies and agreements in place in respect of HSSE.

TERMS OF REFERENCE

The Terms of Reference for the HSSE Committee are reviewed annually at the March Committee meeting to ensure the terms guiding the Committee are relevant, fit for purpose and generate open discussion in line with best practice. The Committee Terms of Reference are available to view on the Company website.



MEETINGS

Four meetings of the HSSE Committee were held in 2016. The Chief Operating Officer and the Group's HSSE Superintendent attend and present at the meetings upon invitation.

ROLE AND ACTIVITIES

The Chairman of the HSSE Committee visited the Group's operations to obtain first-hand knowledge of current practices. The HSSE management teams at the Group's operations continually assist the Committee to ensure policies and procedures remain current, effective and in line with industry practice.

ROLE AND ACTIVITIES

Role	Activities in 2016
To evaluate the effectiveness of the Group's policies and systems in identifying and managing HSSE risks as well as ensuring compliance with applicable legal and regulatory requirements	<p>The Committee evaluated the effectiveness of the Group's HSSE management policies and reviewed reports on HSSE performance on a quarterly basis. The Committee reviewed legal and regulatory compliance of the Group's mining operations by considering the results of legal compliance audits which were presented at the Committee meetings. In addition to the legal compliance audits, the Chairman and Committee members requested quarterly updates on the management of critical HSSE features. These critical features were identified by the Committee following discussions ahead of and/or during Committee meetings and took into consideration activities within the Group as well as the global mining environment. Some of the critical features monitored by the Committee during 2016 included:</p> <ul style="list-style-type: none"> ▶ radiation management at Letšeng; ▶ tailings and water storage facility management at Letšeng and Ghaghoo; and ▶ water management, more specifically at Ghaghoo.
To assess the impact of HSSE decisions and actions on the Group's employees, project-affected communities (PACs) and other stakeholders as well as the reputation of the Group	<p>The Committee considers reports on any significant or major HSSE incidents during meetings. There were no significant or major environmental or social incidents recorded, five significant safety incidents were reported. The Committee assesses the impact of HSSE decisions on the Group's reputation on an ongoing basis, with specific attention being given to the Group's social licence to operate. HSSE decisions and/or actions that have the potential to impact the Group's relationship with its stakeholders, or its reputation are proactively identified by the Committee and monitored during or outside the Committee meetings, depending on the potential severity of the impact. Social upliftment projects are closely monitored by the Committee to ensure the correct process is followed and stakeholder relationships are safeguarded.</p>

Role	Activities in 2016
<p>To review reports from management concerning all fatalities and serious accidents within the Group and actions taken by management because of such serious accidents</p>	<p>No fatalities occurred during the year, but the Committee received reports on all five of the serious accidents that occurred in the Group. The Committee reviewed incident investigation reports on the lost time injuries and found the reports to adequately identify the root causes of the incidents and recommend appropriate corrective actions. The Committee received reports on the implementation of corrective actions as well as health and safety system reviews to mitigate against the reoccurrence of such accidents in future.</p>
<p>To evaluate and oversee the quality and integrity of any reporting to external stakeholders concerning HSE issues and review the Group's HSE performance indicators</p>	<p>The Committee evaluates HSE data presented in reports on a quarterly basis and has, on occasion, requested further review of data to ensure accuracy throughout the reporting process. In addition to the HSE issues reported on in the half-year reports, the Committee also reviews the Annual Sustainable Development Report, which details the Group's HSE performance throughout the year.</p> <p>The Committee reviewed the Group's HSE performance indicators and trends for both current and forward looking periods to ensure relevance and appropriateness. The performance indicators are heavily influenced by the Group's past performance as well as the Global Reporting Initiative's Sustainability Guidelines.</p>
<p>To review the results of independent audits of the Group's performance in respect of HSE matters</p>	<p>During the year the Committee considered external audit reports regarding the mining operations' performance in respect of HSE systems, management as well as legal compliance. The Committee received feedback with regard to the following independent audits:</p> <ul style="list-style-type: none"> ▶ HSE systems and management at Ghaghoo; ▶ HSE legal compliance at Ghaghoo; ▶ social and environmental management plan (SEMP) compliance at Ghaghoo; ▶ ISO 14001 environmental management system at Letšeng; ▶ ISO 18001 occupational health and safety management at Letšeng; ▶ HSE legal compliance at Letšeng; and ▶ SEMP compliance at Letšeng. <p>The Committee monitored the close out of HSE-related findings resulting from these independent audits through quarterly status reports.</p>
<p>To review any strategies and action plans developed by management in response to issues raised in terms of HSE and where appropriate, make recommendations to the Board</p>	<p>The Committee assessed the appropriateness of HSE action plans and strategies developed by operational management to address HSE matters and reviewed the effectiveness of these strategies in addressing HSE trends or shortfalls. During the year the Committee monitored, among others, the following action plans and strategies:</p> <ul style="list-style-type: none"> ▶ nitrate management action plan at Letšeng; ▶ surface water management strategy at Ghaghoo; ▶ behaviour-based care at Letšeng; and ▶ rockfall safety awareness campaign at Ghaghoo. <p>The Committee also recommended further actions to the Board where appropriate.</p>

Annual Statement on Directors' remuneration



Mike Salamon, Chairman

The Committee comprises:

- ▶ M Salamon – Chairman
- ▶ RW Davis
- ▶ MD Lynch-Bell

Dear Shareholder

On behalf of the Board I am pleased to present the Remuneration Committee's Directors' Remuneration Report for 2016.

PROPOSED 2017 REMUNERATION POLICY

In line with last year, this report is split into three sections: the Annual Statement, the Directors' Remuneration Policy and the Annual Report on Remuneration.

During 2016, the Remuneration Committee reviewed the appropriateness and effectiveness of the existing Remuneration Policy, which was approved by shareholders at the 2014 Annual General Meeting (AGM). The Committee believes that, on the whole, the policy has served the Company well to motivate and reward Senior Executives, and align their interests with those of the Company and our shareholders. This year we will be asking our shareholders to approve a new Remuneration Policy for Executive Directors at the 2017 AGM. The proposed 2017 policy remains broadly unchanged from the 2014 policy. However, the Committee is aware of a small number of areas where the 2014 policy was not fully in line with current general shareholder preferences, and we are therefore taking this opportunity to introduce a number of best practice changes in the proposed 2017 policy as follows.

Malus and clawback provisions

The Committee notes the requirement for malus and clawback provisions in incentives in the UK Corporate Governance Code, and the increasing prevalence of these provisions in FTSE incentive plans. The Company is therefore introducing malus and clawback provisions from 1 January 2017 in respect of the annual bonus, and from awards due to be made in March 2017 in respect of the Employee Share Option Plan (ESOP).

Share ownership and retention guidelines

The Company will be introducing shareholding guidelines from 1 January 2017 in order to encourage Executive Directors to acquire and maintain a level of ownership of shares that more closely aligns their interests with those of the Company's other shareholders. The guideline is for Executive Directors to hold 100% of salary in beneficially owned shares. Until the guideline has been met, Executive Directors will be required to retain 50% of vested awards under the ESOP or any other share-based incentive.

REMUNERATION DECISIONS IN 2016

Letšeng met its operational performance targets notwithstanding the effect of inclement weather. The lack of large value diamonds recovered during the year, coupled with weak diamond prices amid continued poor market conditions, contributed to disappointing results in 2016.

In this context, the Committee's key decisions during the year related to the following areas:

Annual bonus

For 2016 the formulaic annual bonus outcome for the business scorecard was 35%. However, in the context of challenging operating conditions and the Group's performance in 2016, the Executive Directors and the Remuneration Committee jointly agreed that no bonus should be paid to the Executive Directors for 2016.

ESOP

Based on performance to 31 December 2016, 28.26% of the share awards made under the 2014 ESOP will vest in June 2017. In respect of the relative Total Shareholder Return (TSR) element (25% of the award), performance is measured versus the constituents of the FTSE 350 Mining Index; 0% vested. In respect of the production element (37.5% of the award), 7.18% will vest and for the profit element (37.5% of the award), 21.08% will vest.

In March 2016, Executive Directors were granted awards under the ESOP which will vest based on performance over the three financial years to 31 December 2018. In line with the prior year, these awards will vest to the extent that challenging relative TSR, production and profit targets are achieved over the period.

IMPLEMENTATION OF THE REMUNERATION POLICY IN 2017

The Executive Directors' salaries were reviewed in March 2017, and in light of the current environment no increases were awarded.

For 2017, the annual bonus opportunity will remain 100% of salary. Performance will continue to be measured with reference to a business scorecard linked to growth, operating performance and HSSE performance (weighted 80% of maximum), and to personal performance (20% of maximum). Malus and clawback provisions will apply for a period of two years following payment.

Executive Directors were granted awards under the ESOP in March 2017, subject to the shareholders' approval of the Remuneration Policy in June 2017, of between 55% and 62% of salary. Awards will vest on performance over the three financial years to 31 December 2019. The performance conditions remain 25% on relative TSR versus the FTSE 350 Mining Index, 37.5% on production and 37.5% on profit. Malus and clawback provisions will apply during the vesting period and for a period of two years following vesting.

Further details on the implementation of the policy for 2017 are included on pages 86 to 93.

DIRECTORATE CHANGE

AR Ashworth retired from the Board and ceased to be employed on 30 June 2016. All payments made to AR Ashworth are in line with default treatment under the Company's existing Remuneration Policy for a good leaver, as approved by shareholders at the 2014 AGM, and consistent with his service agreement and his statutory employment rights. Further details on exit payments made to AR Ashworth are included on page 99.

Resolutions to approve the proposed Remuneration Policy (subject to a binding vote) and the Annual Report on Remuneration (subject to an advisory vote) will be put to our shareholders at the forthcoming AGM. We continue to value feedback from our shareholders and hope to receive your support at the AGM.

Mike Salamon

Chairman of the Remuneration Committee

14 March 2017

Directors' Remuneration Policy

The Company's Remuneration Policy is designed to provide a level of remuneration which attracts, retains and motivates executives of a suitable calibre to carry out the Company's business strategy and maximise long-term shareholder wealth.

The report has been prepared in accordance with the principles of the Companies Act 2006 and Schedule 8 of The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. The Regulations require our auditors to report to shareholders on the audited information within this report and to state whether, in their opinion, the relevant sections have been prepared in accordance with the Act. The auditors' opinion is set out on pages 113 to 119 and we have clearly marked the audited sections of the report.

As required by legislation, the Remuneration Policy as set out in this section of the report will be put to a binding shareholder vote and, subject to shareholder approval, will become effective from the date of the 2017 AGM. The proposed policy is broadly consistent with the approved 2014 policy, save the changes highlighted in the Remuneration Committee Chairman's Statement.

THE COMPANY'S REMUNERATION POLICY

The Company's Remuneration Policy is designed to provide a level of remuneration which attracts, retains and motivates executives of a suitable calibre to carry out the Company's business strategy and maximise long-term shareholder wealth. It

is intended that, as far as possible, remuneration policies and practices will conform to best practice in the markets in which the Company operates and will be aligned with shareholder interests and promote effective management of business risk.

The Committee takes into account the UK Listing Rules, the principles and provisions of the Code and the guidance provided by institutional investor representative bodies in determining executive remuneration arrangements. In deciding on the appropriate structure and quantum of remuneration, the Committee reviews remuneration practices at comparator companies, comprising mining companies and UK-listed companies of a similar size and complexity, to ensure remuneration policies reflect, as appropriate, prevailing industry and market conditions. Furthermore, remuneration policies have taken, and will continue to take, account of pay and employment conditions elsewhere in the Group.

The Committee's policy is to weight remuneration towards variable pay. The aim is to provide base salaries and benefits that are fair, and variable pay incentives linked to the achievement of realistic performance targets relative to the Company's strategy and corporate objectives.

Policy table for Executive Directors

Element	Purpose and link to strategy	Operation	Opportunity	Performance measures
SALARY	To offer a market competitive base salary to recruit and retain individuals of the necessary calibre to execute the Company's business strategy.	<ul style="list-style-type: none"> ▶ Base salaries are reviewed annually with changes effective from 1 April. ▶ Salaries are typically set after considering the salary levels in companies of a similar size, complexity and risk profile, the responsibilities of each individual role, progression within the role, and individual performance. ▶ In setting salaries for Executive Directors, the Committee takes note of the overall approach to salary reviews for the wider workforce. 	<ul style="list-style-type: none"> ▶ No prescribed maximum annual increase. ▶ It is expected that salary increases for Executive Directors will ordinarily be (in percentage of salary terms) in line with those of the wider workforce in countries of a similar inflationary environment. ▶ In certain circumstances (for example where there is a change in responsibility, role size or complexity, or progression in the role), the Committee has discretion to award a higher increase to ensure salary levels remain competitive. 	N/A
BENEFITS	To provide competitive benefits taking into account market value of role and benefits offered to the wider UK management population, in line with the Company's strategy to keep remuneration simple and consistent.	<ul style="list-style-type: none"> ▶ Executive Directors receive a cash allowance in lieu of non-cash benefits. 	<ul style="list-style-type: none"> ▶ Benefit value may vary by role to reflect market practice. It is not anticipated that the current cost of benefits (as set out in the Annual Report on Remuneration) will increase materially over the term of this policy, though the Committee retains discretion to approve a higher cost in exceptional circumstances (for example relocation or increase in insurance premiums). 	N/A

Directors' Remuneration Policy continued

Element	Purpose and link to strategy	Operation	Opportunity	Performance measures
PENSION	To provide retirement benefits that are appropriately competitive.	<ul style="list-style-type: none"> ▶ No formal pension provision is made by the Company. 	<ul style="list-style-type: none"> ▶ Executive Directors receive a cash allowance in lieu of pension which is currently equal to 14.5% and 13.0% of base salary for the CEO and other Executive Directors, respectively. ▶ It is not anticipated that the cash allowance in lieu of pension will exceed this level over the term of this policy, though the Committee retains discretion to approve a higher cost if deemed appropriate 	N/A
ANNUAL BONUS	To drive and reward performance against personal objectives and selected financial and operational KPIs which are directly linked to business strategy.	<ul style="list-style-type: none"> ▶ The executive incentive scheme is reviewed annually by the Committee at the start of the year to ensure the opportunity and performance measures are appropriate and continue to support business strategy. ▶ The Committee has discretion to adjust the formulaic outcome of the bonus to more accurately reflect business and personal performance during the year. ▶ The annual bonus is paid entirely in cash. ▶ Malus and clawback provisions may be applied for a period of two years following payment in exceptional circumstances, including but not limited to misstatement, misconduct or error. 	<ul style="list-style-type: none"> ▶ Maximum opportunity of up to 100% of base salary. ▶ For threshold level and target level performance, the bonus earned is 50% and up to 68% of maximum opportunity, respectively. 	<ul style="list-style-type: none"> ▶ Performance is determined by the Committee on an annual basis by reference to a scorecard of Group targets as detailed in the Group's business plan and encapsulated in specific key performance indicators (KPIs) as well as a discretionary assessment of personal performance. ▶ Group scorecard targets may include growth which is judged by the Committee on a discretionary basis, HSE and operating performance, and will typically be weighted at least 70% in any one year. ▶ Details of the measures and weightings for the current year are provided in the Annual Report on Remuneration.

Element	Purpose and link to strategy	Operation	Opportunity	Performance measures
<p>EMPLOYEE SHARE OPTION PLAN (ESOP)</p>	<p>To balance the delivery of absolute and relative returns to shareholders in the long term, support alignment with shareholders, and attract, retain and motivate executives of the appropriate calibre.</p>	<ul style="list-style-type: none"> ▶ Executive Directors are granted awards of performance shares and/or options as determined by the Committee, which vest after a minimum of three years based on performance. ▶ Awards are normally made annually after the announcement of the full-year results but may be made at other times deemed appropriate by the Committee. ▶ The Committee may vary the ratio of performance shares and options from year to year, but it is the current intention of the Committee that only awards of performance shares are made over the term of this policy. ▶ The Committee will consider the impact of any external factors when determining the final vesting outcome of awards under the ESOP. Any such discretion would be disclosed and explained in the following year's Annual Report on Remuneration. ▶ For performance shares, any dividends paid would accrue over the vesting period and would be paid only on those awards that vest. ▶ Malus and clawback provisions may be applied for a period of two years post-vesting in exceptional circumstances, including but not limited to misstatement, misconduct or error. ▶ For future awards, the Committee may introduce a holding period of up to two years (or such other period the Committee may determine) for vested awards, during which time Executive Directors may not sell shares save to cover tax. 	<ul style="list-style-type: none"> ▶ Maximum opportunity is up to 125% of salary in performance shares and 250% in performance options (subject to overall maximum with fair value equivalent to 125% of salary in performance shares). ▶ For threshold performance, 20% of the maximum award vests. 	<ul style="list-style-type: none"> ▶ Awards vest based on continued employment and the Company's performance measured over a minimum of three years. It is the Committee's current intention that the performance measures be based on relative TSR, profit and production, but may for future awards include additional measures such as HSSE or strategic objectives, as determined by the Committee. ▶ Vesting is ultimately also subject to the Committee's assessment of the Company's underlying performance.

Directors' Remuneration Policy continued

NOTES TO POLICY TABLE

Payments from existing arrangements

Executive Directors will be eligible to receive remuneration or other payments in respect of any award granted or payment agreed prior to the approval and implementation of the 2017 policy, or prior to the individual becoming a Director. Details of any such awards or payments are disclosed in the Annual Report on Remuneration.

Selection of performance measures (annual bonus and ESOP)

The performance measures used in the Company's executive incentive scheme have been selected to ensure incentives reinforce the Company strategy and align executive interests closely with those of shareholders. The Committee considers that the financial and operational measures used in the annual bonus, support the strategic objectives of value creation, growth and sustainability, and are well-accepted measures for the mining sector. The use of profit and production is consistent with the Company's KPIs, and the use of relative TSR is strongly aligned with shareholders and ensures that executives are rewarded only if they exceed the returns which a shareholder could achieve elsewhere in the sector.

Performance targets are set to be stretching and achievable, taking into account the Company's strategic priorities and the economic environment in which the Company operates. Targets are set taking into account a range of reference points including the Group's business plan. The Committee believes that the performance targets set are adequately stretching and that the maximum outcomes are achievable only for exceptional performance.

Remuneration policy for other employees

The approach to salary reviews is consistent across the Group, with consideration given to the level of responsibility, experience, individual performance, market levels and the Company's ability to pay.

Below Board level, Senior Management employees participate in an annual bonus scheme on a similar basis as the Executive Directors, although the weighting on Group performance measures increases with seniority. A number of management level employees also receive ESOP awards. Performance conditions and award sizes vary to be appropriate to the organisational level.

Shareholding guidelines

The guideline for Executive Directors is that they hold 100% of salary in beneficially owned shares. Until the guideline has been met, Executive Directors will be required to retain 50% of vested awards under the ESOP or any other share-based incentive.

Pay for performance: scenario analysis

The following graphs provide an estimate of the potential future remuneration for the Executive Directors and the potential split between the different elements of pay under three performance scenarios: 'fixed', 'at target' and 'maximum'. Potential remuneration is based on incentive opportunities as set out in the proposed 2017 policy, applied to the salaries effective 1 April 2017. For the annual bonus, the maximum is 100% of salary. ESOP values are based on the proposed number of shares to be awarded in 2017 and the three-month average share price to 31 December 2016 of 112 pence (equivalent to 55% to 62% of salary). Note that the projected values exclude the impact of any share price movements.

The 'fixed' scenario includes base salary, pension and benefits only.

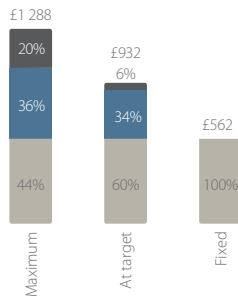
The 'at target' scenario includes fixed remuneration as above, plus target payout of annual bonus, and threshold vesting for the ESOP.

The 'maximum' scenario includes fixed remuneration, plus full payout and vesting of all incentives.

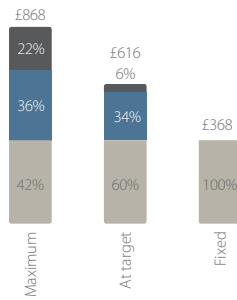
The assumptions are summarised in the table below.

Component	Fixed	At target	Maximum
Salary	Base salary for 2017		
Benefits	Taxable value of annual benefits provided		
Pension	14.5% and 13% of salary for the CEO and other Executive Directors, respectively		
Annual bonus	0% of maximum	68% of maximum	100% of maximum
ESOP	0% of maximum	20% of maximum	100% of maximum

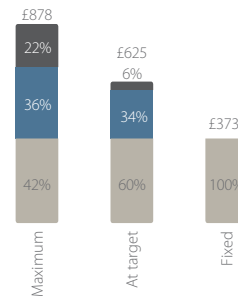
Chief Executive Officer (£000)



Chief Financial Officer (£000)



Chief Legal and Commercial Officer



■ Salary, pension and benefits ■ Annual bonus ■ Long-term income

Approach to remuneration on executive recruitment

In recruiting new Executive Directors, the Committee will follow the Remuneration Policy as set out in the policy table. On appointment of an external Executive Director, any arrangement specifically established to recruit an individual would be capped at the limits described in the policy table. The Committee does not envisage a payment such as a 'golden hello' would be offered, although the Committee may consider it appropriate to compensate for incentive arrangements the Director forfeits on leaving their current employer. Any such buy-out compensation would be on a comparable basis taking into account factors including the performance conditions attached to these awards, the likelihood of conditions being met, and the remaining vesting period of these awards. The Committee would normally use the remuneration components under the regular policy to make such buy-out awards, but may also exercise its discretion under Listing Rule 9.4.2 if an alternative incentive structure were required.

In the case of internal promotions, any commitments made prior to promotion and the approval of the Remuneration Policy will be honoured. Where the new appointee has an initial salary set below market, any shortfall will be managed with phased increases over a period of several years, subject to the individual's performance and development in the role.

SERVICE CONTRACTS

The Company's policy is to limit termination payments on termination to pre-established contractual arrangements. In the event that the employment of an Executive Director is terminated, any compensation payable will be determined in accordance with the terms of the service contract between the Company and the employee, as well as the rules of any incentive plans. Details of the Executive Directors' service contracts are summarised in the table below.

Directors	Contract date	Unexpired term	Notice period	Contractual termination payment ¹
CT Elphick	13 February 2007			
M Michael	22 April 2013	Rolling contract	12 months	Pay basic salary on summary termination. Benefits are payable only at the Committee's discretion
GE Turner	1 July 2008			

¹ There are no special provisions in the contracts extending the notice period on a change of control or other corporate events.

Directors' Remuneration Policy continued

Payments for loss of office under all service contracts

If an Executive Director's contract is terminated, payments equal to salary in lieu of notice can be made monthly during the notice period. Benefits are payable only at the Committee's discretion. Payment in lieu of unused annual leave entitlement can be made at the effective salary rate at the point of termination.

If employment is terminated by the Company, the departing Executive Director may have a legal entitlement (under statute or otherwise) to additional amounts, which would need to be met. Where the Company wishes to enter into a settlement agreement and the individual must seek independent legal advice, the Committee retains discretion to settle any claims by or on behalf of the Executive Director in return for making an appropriate

payment and contributing to the legal fees incurred by the Executive Director in connection with the termination of employment.

In exceptional circumstances, the Committee may approve new contractual arrangements with departing Executive Directors including (but not limited to) settlement, confidentiality, outplacement services, restrictive covenants and/or consultancy arrangements. These will be used only in circumstances where the Committee believes that it is in the best interests of the Company and its shareholders to do so.

The table below provides details of exit payments under different leaver scenarios.

Incentive plan	Scenario	Time of payment/vesting	Calculation of payment/vesting
ANNUAL BONUS	<ul style="list-style-type: none"> ▶ Death, disability, ill health, redundancy, retirement, or any other reasons the Committee may determine (normally not including resignation or where there are concerns as to performance). ▶ Change of control (whether or not employment is terminated as a result). 	<ul style="list-style-type: none"> ▶ Normal payment date, although the Committee has discretion to accelerate (eg in relation to death). ▶ Immediately, on change of control. 	<ul style="list-style-type: none"> ▶ Performance against targets will normally be assessed by the Committee at the end of the year and any resulting bonus is normally pro-rated for proportion of the year worked. ▶ Performance against targets will normally be assessed by the Committee up to the date of change of control and any resulting bonus is normally pro-rated for time.
ESOP	<ul style="list-style-type: none"> ▶ All other reasons. ▶ Death, disability, ill health, redundancy, retirement, or any other reasons the Committee may determine (normally not including resignation or where there are concerns as to performance). ▶ Change of control (whether or not employment is terminated as a result). 	<ul style="list-style-type: none"> ▶ Not applicable. ▶ Normal vesting date, although the Committee has discretion to accelerate. ▶ Immediately, on change of control. 	<ul style="list-style-type: none"> ▶ No bonus is paid. ▶ Unvested awards will normally be pro-rated for time unless the Committee decides otherwise and based on performance. ▶ Unvested awards will normally be pro-rated for time unless the Committee decides otherwise and based on performance up to the date of change of control. Executive Directors can elect to exchange ESOP awards for those of the acquiring company, if offered. ▶ Awards lapse.
	<ul style="list-style-type: none"> ▶ All other reasons. 	<ul style="list-style-type: none"> ▶ Not applicable. 	

Non-Executive Directors

Non-Executive Directors do not receive benefits from the Company and they are not eligible to participate in any bonus or share incentive scheme.

Details of the policy on non-Executive Director fees are set out in the table below.

Element	Purpose and link to strategy	Operation	Opportunity
DIRECTORS' FEES	<ul style="list-style-type: none"> To attract and retain a high-calibre Chairman and non-Executive Directors with experience relevant to the Company. 	<ul style="list-style-type: none"> Fees are reviewed annually, with any changes effective from 1 April. Fees are typically set after considering current market levels and taking into account time commitment and responsibilities involved. All non-Executive Directors, including the Chairman, are each paid an all-inclusive fee. No additional fees are paid for chairmanship of Committees. All fees are payable in cash in arrears. The non-Executive Directors do not participate in any of the Group's incentive plans. No other benefits or remuneration are provided to non-Executive Directors. 	<ul style="list-style-type: none"> No prescribed maximum annual increase. It is expected that fee increases will typically be in line with market levels of fee inflation. In certain circumstances (for example where there is a change in time commitment required or a material misalignment with market), the Committee has the discretion to make adjustments to fee levels to ensure they remain competitive. The maximum aggregate annual fee for all non-Executive Directors, including the Chairman, allowed by the Company's Articles of Association is £750 000.

Non-Executive Directors do not have service contracts. Summary details of terms and notice periods for non-Executive Directors are included below.

Director	Contract date	Unexpired term	Notice period	Contractual termination payment
RW Davis	1 February 2007	Rolling appointment	Three months	No provision for payment of compensation.
GA Beevers	1 February 2007			
M Salamon	3 February 2008			
MD Lynch-Bell	15 December 2015			

CONSIDERATIONS OF CONDITIONS ELSEWHERE IN THE GROUP

The Committee considers the remuneration and employment conditions elsewhere in the Group when determining remuneration for Executive Directors. Although the Committee does not currently consult specifically with employees on the executive Remuneration Policy, it receives regular updates from the Chief Financial Officer on the pay conditions for employees across the Group, and takes these into account when determining Executive Director remuneration.

CONSIDERATIONS OF SHAREHOLDER VIEWS

When determining remuneration, the Committee considers shareholder views and the guidelines of investor bodies. The Committee always welcomes feedback from shareholders on the Company's Remuneration Policy and commits to undergoing shareholder consultation in advance of any significant changes to policy. Details on the votes received on the Directors'

Remuneration Report at the prior AGM is provided in the Annual Report on Remuneration.

EXTERNAL DIRECTORSHIPS

Executive Directors are permitted to accept external directorships with prior approval of the Chairman. Approval will only be given where the appointment does not present a conflict of interest with the Group's activities and the experience gained will be beneficial to the development of the individual. Where fees are payable in respect of such appointments, these would be retained by the Executive Director. Refer to page 104 for further details.

Mike Salamon

Chairman of the Remuneration Committee

14 March 2017

The Annual Report on Remuneration

The following section provides details of how the Company's 2014 Remuneration Policy was implemented during the financial year ended 31 December 2016, and how the Remuneration Committee intends to implement the proposed policy in 2017.

COMPOSITION AND ROLE OF THE REMUNERATION COMMITTEE

Committee members	Member throughout 2016	Number of meetings attended/held 2016
M Salamon – Chairman	✓	3/4
RW Davis	✓	4/4
MD Lynch-Bell	Appointed 14 March 2016	3/4

RW Davis served three terms as a member of the Remuneration Committee, which was the maximum length of time as set out in the Committee's terms of reference. His reappointment for a fourth term was approved by the Board.

The Chief Executive Officer and the Chief Financial Officer attend Committee meetings by invitation and assist the Committee in its deliberations except when issues relating to their own remuneration are discussed. Representatives of Kepler, a brand of Mercer, also attend the meetings by invitation.

The Committee is a formal Committee of the Board. Its terms of reference are available on the Company's website and comply with the UK Corporate Governance Code.

The Committee's main responsibilities are to:

- ▶ consider and agree on the Company's Remuneration Policy for approval by shareholders at the AGM;
- ▶ determine individual remuneration packages for the Chairman, the Executive Directors and the Company Secretary;
- ▶ monitor and recommend the level and structure of remuneration for Senior Management;
- ▶ approve the design of performance-related pay schemes operated by the Group and approve total annual payments;
- ▶ review the design of all share-based incentive plans and approve the awards to be made;
- ▶ determine the basis for calculating bonuses payable to the Executive Directors and Senior Management;
- ▶ make recommendations to the Board on the fees offered to the non-Executive Directors;
- ▶ consider major changes in employee remuneration in the Group; and
- ▶ select and appoint consultants to advise the Committee.

The Committee's policy is to encourage an open and transparent dialogue with shareholders on remuneration matters and would seek to consult with major shareholders prior to implementing any significant changes to the Remuneration Policy.

ACTIVITIES OF THE REMUNERATION COMMITTEE IN 2016

During the year, activities undertaken by the Committee included:

- ▶ review of incentive plans across the Group (including operating unit incentive plans), and review of the Remuneration Policy;
- ▶ review and approval of the Directors' Remuneration Report for 2015, and preparation of the Directors' Remuneration Report for 2016;
- ▶ review and approval of incentive outcomes for Executive Directors for 2015;
- ▶ determination of the Executive Directors' annual bonus and ESOP opportunities and performance targets for 2016;
- ▶ review of recent developments in remuneration market trends and best practice;
- ▶ review and approval of the Chairman's fee; and
- ▶ review and approval of base salaries and total remuneration for the Executive Directors and the Company Secretary.

ADVISERS TO THE REMUNERATION COMMITTEE

Kepler was appointed by the Committee in February 2010, and provided independent remuneration advice to the Committee and attended Committee meetings during 2016. Kepler provides remuneration advice to a large portfolio of clients including many in the FTSE 350 and FTSE Small Cap; this gives the Committee comfort that the advice provided is appropriate and relevant. Kepler is a signatory to, and abides by, the Remuneration Consultants Group Code of Conduct. Further details can be found at www.remunerationconsultantsgroup.com.

Neither Kepler nor Kepler's parent company, Mercer, provides non-remuneration services to the Group or is in any other way connected to the Group, and Kepler is therefore considered to be independent. The fees payable in relation to work for the Committee in 2016 were £53 160 (US\$72 023) excluding VAT.

SUMMARY OF SHAREHOLDER VOTING AT THE 2016 AGM

The table below shows the results of the advisory vote on the 2015 Annual Report on Remuneration at the 7 June 2016 AGM.

		For	Against	Total votes cast	Withheld
Annual Report on Directors' Remuneration	Total number of votes	112 080 839	481 712	112 562 551	1 341 445
	Percentage of votes cast	99.6%	0.4%	100%	1.2%

Audited

TOTAL SINGLE FIGURE OF REMUNERATION FOR DIRECTORS

The table below sets out the total single figure remuneration received by each Director for 2016 and the prior year. Although the Group's reporting currency is US dollar, these figures are stated in sterling as the Directors' emoluments are paid in sterling.

	Salary and fees ¹		Benefits ²		Pension ²		Annual bonus ³		Long-term incentives ⁴		Total	
	2016 £	2015 £	2016 £	2015 £	2016 £	2015 £	2016 £	2015 £	2016 £	2015 £	2016 £	2015 £
CT Elphick	464 802	451 264	25 564	24 819	67 396	65 433	-	338 203	65 194	-	622 956	879 719
AR Ashworth ⁵	170 826	334 151	10 250	20 049	22 207	43 440	78 892	250 432	33 179	-	315 354	648 072
M Michael	306 750	284 740	18 405	17 085	39 878	37 016	-	232 200	35 445	69 679	400 478	640 720
GE Turner	311 373	302 304	18 682	18 138	40 478	39 300	-	226 564	43 674	-	414 207	586 306
Total of Executive Directors	1 253 751	1 372 459	72 901	80 091	169 959	185 189	78 892	1 047 399	177 492	69 679	1 752 995	2 754 817
RW Davis	110 000	107 500	-	-	-	-	-	-	-	-	110 000	107 500
GA Beevers	55 000	54 375	-	-	-	-	-	-	-	-	55 000	54 375
M Salamon	55 000	54 375	-	-	-	-	-	-	-	-	55 000	54 375
MD Lynch-Bell	55 000	2 538	-	-	-	-	-	-	-	-	55 000	2 538
Total of non-Executive Directors	275 000	218 788	-	-	-	-	-	-	-	-	275 000	218 788
Total of all Directors	1 528 751	1 591 247	72 901	80 091	169 959	185 189	78 892	1 047 399	177 492	69 679	2 027 995	2 973 605

Audited

¹ Salary and fees: amount earned for the year.

² Benefits and pension: cash payments in lieu.

³ Annual bonus: payments in relation to performance for the year.

⁴ ESOP: value at vesting of awards vesting on performance over the three-year period ended 31 December 2016. The share price on the vesting date is currently unknown, therefore the awards are valued using the three-month average share price to 31 December 2016 of 112 pence.

⁵ AR Ashworth retired from the Board on 30 June 2016. The 2016 remuneration reported in the table relates to the period 1 January 2016 to 30 June 2016.

PENSION AND OTHER BENEFITS

No formal pension provision is made by the Company. Instead, Executive Directors receive a cash allowance a cash in lieu of pension which was equivalent to 14.5% and 13% of base salary for the Chief Executive Officer and other Executive Directors, respectively. Executive Directors received a cash allowance in lieu of other non-cash benefits, the value of which ranged between 5.5% and 6% of base salary during 2016.

INCENTIVE OUTCOMES FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2016

Annual bonus in respect of 2016 performance

Executive Directors participate in a discretionary annual bonus arrangement designed to focus participants on the following business critical factors: (i) growth strategy implementation, (ii) funding, (iii) financial and operational performance, (iv) health, safety, social, environment, sustainability, image and relationships, and (v) sales, marketing and manufacturing, all of which are underpinned by specific KPIs and included in the business plan approved by the Board.

In 2016, the maximum bonus opportunity for Executive Directors was 100% of base salary, with 80% linked to a business scorecard and 20% linked to a discretionary assessment of personal performance.

The Annual Report on Remuneration continued

The performance measures, targets and actual outturn in respect of 2016 are disclosed in full in the table below.

Performance measure		Weighting (% of max)	Threshold target	Stretch target	Actual performance	Payout (% of max)
Growth		30	Judged by Committee on a discretionary basis			8
Operating performance	Underlying EBITDA (US million)	10	84.2	126.4	62.8	0
	EPS (US cents)	10	14.65	21.97	12.80	0
	Waste tonnes mined (millions)	10	29.1	30.6	29.8	7
	Ore tonnes treated (millions)	10	6.9	7.6	6.9	0
	Carats recovered	10	164 937	223 149	149 182	0
HSSE performance	Fatalities	5	0	0	0	5
	All injury frequency rate	5	4.56	3.80	1.93	5
	Major environmental or community incidents	5	0	0	0	5
	HSSE legal compliance	5	Judged by Committee on a discretionary basis			5
Overall business scorecard outcome						35 (out of 100)

Growth

The growth component of the bonus is assessed at the discretion of the Committee. In terms of performance against the Group's growth targets, the Committee considered the progress made in the year and the additional capacity generated from the Plant 2 expansion project completed in 2015. A post-implementation review confirmed that the project was successful with a 12% capacity increase. The Committee also considered the Executive Directors' efforts in assessing possible strategic activities. The anticipated progress at Ghaghoo was constrained due to the operational challenges and the current market conditions impacting the Ghaghoo type production. The placing of Ghaghoo onto care and maintenance was taken into account and restricted the score for this component. The Committee has therefore concluded that the growth component of the bonus be limited to a payout of 8% (relative to the maximum of 30%).

HSSE legal compliance

Letšeng retained its ISO 14001 and ISO 18001 accreditation for environmental and occupational health and safety management for a second year in a row, while following an NOSA audit, Ghaghoo retained its four-star rating.

Personal performance

Objectives under the personal element of the bonus were linked to each Executive Director's individual areas of responsibility, and designed to collectively support the achievement of the Group's strategic targets for the year. Individual targets comprised contributions to the Group's overall performance and the delivery of strategic projects and initiatives as set out by the Board, including but not limited to: operational performance, strengthening of key stakeholder relationships, bank financing and treasury management and HSSE objectives.

In light of the decision that no bonuses will be payable to the Executive Directors, the personal performance was not assessed for purposes of annual bonus calculation.

Actual bonuses awarded for 2016

Based on the business scorecard, the resulting formulaic annual bonus outcome for Group performance was 35%. However, in the context of the challenging operating conditions and the Group's performance in 2016, the Executive Directors and the Remuneration Committee jointly agreed that no bonus should be paid to the Executive Directors for 2016.

AR Ashworth retired from the Board and ceased to be employed on 30 June 2016. At the start of 2016, it was agreed that he would be eligible for a time pro-rated bonus of 50% of annual salary for 2016. Performance would be linked to a similar mix of business (weighted 80% of maximum bonus) and personal (weighted 20% of maximum bonus) objectives as for other Executive Directors,

measured over the period 1 January to 30 June 2016. Based on the Group's published half-year results, actual outcome for the business scorecard element was 37% of maximum, equivalent to 15% of annual salary after pro-rating for time served. The performance measures, targets and actual outturn are disclosed in full in the table below.

Performance measure	Weighting (% of max)	Threshold target	Stretch target	Actual performance	Payout (% of max)	
Operating performance	Revenue (US million)	20	119.8	132.4	112.1	0
	Waste tonnes mined (millions)	10	15.2	16.0	15.3	5
	Development metres	10	1 193	1 256	1 169	0
	Ore tonnes treated (millions)	20	3.4	3.8	3.4	5
	Carats recovered	20	76 548	103 566	78 256	8
HSSE performance	Fatalities	5	0	0	0	5
	All injury frequency rate	5	4.56	3.80	4.00	4
	Major environmental or community incidents	5	0	0	0	5
	HSSE legal compliance	5	Judged by Committee on a discretionary basis			5
Overall business scorecard outcome					37 (out of 100)	

In respect of performance in the HSSE legal compliance category, no major findings were registered for the period 1 January to 30 June 2016.

The Committee also assessed AR Ashworth's personal performance during the period, and agreed an outcome of 80% of maximum, equivalent to 8% of annual salary pro rata. In assessing the personal performance, the Committee took into account the strong operational performance at Letšeng and the

achievement of HSSE objectives with zero fatalities. The Committee agreed that AR Ashworth successfully carried out his duties in line with the Group's objectives. The total bonus paid was therefore 23% of an annual salary of £346 700, ie £78 892.

Employee Share Option Plan (ESOP): 2014 awards vesting in 2016

The Executive Directors were granted awards of performance shares in June 2014, which are set out in the table below.

Executive Director	Date of grant	Awards made during 2014	Share price on date of award £	Face value on date of award £	Face value as % of salary	Vesting date
CT Elphick	10 June 2014	206 000	£1.61	331 372	75	10 June 2017
M Michael		112 000		180 163	75	
GE Turner		138 000		221 987	75	
AR Ashworth		153 000		246 116	75	

Vesting of the awards was dependent on relative TSR versus the constituents of the FTSE 350 Mining Index (25% of the award), profit (37.5%) and production (37.5%), measured over the three-year performance period ended 31 December 2016. Relative TSR was measured over the period 1 January 2014 to

31 December 2016. Profit and production were measured on an annual basis with respect to the business plan for the year, with final vesting based on the average achievement of targets over the three years. The performance conditions that applied to these awards are summarised in the table below.

The Annual Report on Remuneration continued

ESOP scorecard

Annual performance	Profit		Production		Total vesting 100%
	Underlying EBITDA 25%	Earnings per share 25%	Ore tonnes treated 25%	Carats recovered 25%	
2014	25.00%	25.00%	20.71%	0.00%	70.71%
2015	11.18%	23.13%	8.00%	0.00%	42.31%
2016	0.00%	0.00%	0.00%	0.00%	0.00%
Average vesting outcome					37.67%

Performance measure		Weighting (% of max)	Performance period	Threshold (20% vesting)	Stretch (80% vesting)	Super-stretch (100% vesting)	Actual performance	Vesting outcome (% of max)
TSR versus FTSE 350 Miners		25%		Median	75th percentile	85th percentile	46th percentile	0%
Profit	Underlying EBITDA (US million)	18.75%		80% of business plan	120% of business plan	132% of business plan		
			2014	46.0	69.0	76.0	104.3	18.75%
			2015	85.5	128.3	141.1	103.5	8.39%
			2016	84.2	126.3	139.0	62.8	0%
	Average						9.05%	
Profit	EPS (US cents)	18.75%		80% of business plan	120% of business plan	132% of business plan		
			2014	5.85	8.77	9.65	24.24	18.75%
			2015	18.94	28.40	31.24	30.21	17.35%
			2016	14.65	21.97	24.17	12.80	0%
	Average						12.03%	
Production	Ore tonnes treated (millions)	18.75%		95% of business plan	105% of business plan	115.5% of business plan		
			2014	5.7	6.3	6.9	6.5	15.53%
			2015	6.9	7.6	8.3	7.0	6.00%
			2016	6.9	7.6	9.6	6.9	0%
	Average						7.18%	
Production	Carats recovered	18.75%		85% of business plan	115% of business plan	126.5% of business plan		
			2014	145 509	196 865	216 551	118 736	0%
			2015	232 057	313 959	345 355	200 079	0%
			2016	164 937	223 149	248 036	149 182	0%
	Average						0%	
Total award		100%						28.26%

For each measure, for achievement between threshold and stretch, and stretch and super-stretch, the award vested on a straight-line basis. For achievement of less than threshold, vesting was nil.

Based on performance to 31 December 2016, 28.26% of the maximum award will vest for CT Elphick, M Michael and GE Turner

in June 2017, subject to continued employment. AR Ashworth retired from the Board and ceased to be employed on 30 June 2016, and therefore his 2014 ESOP award was reduced on a time pro-rata basis to reflect the period served (see page 99 for further information on treatment of his outstanding incentives).

ESOP AWARDS GRANTED IN 2016

On 15 March 2016, performance shares with a face value of between 56% and 62% of salary were awarded to the Executive Directors, as summarised in the table below.

Executive Director	Date of grant	Awards made during the year	Share price on date of award £	Face value on date of award £	Face value as % of salary ¹
CT Elphick		230 000		253 000	56
M Michael	15 March 2016	170 000	1.10	187 000	62
GE Turner		170 000		187 000	61

¹ The face values of awards as a percentage of salary have been updated since the 2015 Annual Report on Remuneration based on the actual share price on the date of award.

AR Ashworth did not receive an award as he was due to retire from the Board in June 2016.

The performance conditions that apply to these awards remain the same as those for the 2015 awards, and are summarised in the table below.

Performance measure	Weighting (% of award)	Threshold (20% vesting)	Stretch (80% vesting)	Super-stretch (100% vesting)
TSR versus FTSE 350 Miners	25%	Median	75th percentile	85th percentile
Profit	37.5%	80% of business plan	120% of business plan	132% of business plan
Production	37.5%	90% of business plan	110% of business plan	121% of business plan

For each measure, for achievement in between threshold and stretch, and stretch and super-stretch, the award will vest on a straight-line basis. For achievement of less than threshold, vesting will be nil. As before, TSR will be measured over three years, from 1 January 2016 to 31 December 2018. Profit and production will be measured on an annual basis with respect to the business plan for the year, with final vesting based on the average achievement of targets over the three years. The profit and production targets are considered commercially sensitive as they relate to the Company's business plan and strategy, and will therefore be disclosed in full after the performance period has ended.

EXIT PAYMENT

AR Ashworth retired from the Board and ceased to be employed on 30 June 2016. All payments made to AR Ashworth are in line with default treatment under the Company's existing Remuneration Policy for a good leaver, as approved by shareholders at the 2014 AGM, and consistent with his service agreement and his statutory employment rights.

AR Ashworth is entitled to 12 months' notice under his service agreement and received an amount of £346 700 in lieu of base salary, and an amount of £65 873 in respect of cash allowances in lieu of pension contribution and benefits.

AR Ashworth further received a time pro-rated annual cash bonus of £78 892 in respect of 2016, based on performance over the period 1 January to 30 June 2016.

Treatment of AR Ashworth's outstanding ESOP awards (ie awards made in 2014 and 2015) is in line with default treatment for a good leaver. Awards will vest on their respective normal vesting dates subject to performance measured in the normal manner at the end of the respective performance periods, and will be reduced on a time pro-rata basis to reflect time served. Based on performance to 31 December 2016, 68% of AR Ashworth's time pro-rated 2014 award, ie 29 624 shares, will vest in June 2017. Performance for the 2015 award will be measured after 31 December 2017, and any shares will vest in April 2018. As appropriate, any dividends on the above awards will accrue and be paid on the relevant vesting dates. AR Ashworth did not receive an ESOP award in 2016.

The Annual Report on Remuneration continued

IMPLEMENTATION OF REMUNERATION POLICY FOR 2017

The Committee approved the following salary increases from 1 April 2017:

	2016 salary £	2017 salary £	% increase
Executive Director			
CT Elphick	468 211	468 211	0
M Michael	309 000	309 000	0
GE Turner	313 657	313 657	0

Audited

Pension and benefits

Under the proposed Policy, the Executive Directors will continue to receive cash supplements in lieu of pension and benefits. The values will remain unchanged from 2016.

Annual bonus

For 2017, the maximum annual bonus opportunity will remain 100% of salary. Performance measures will continue to include a range of financial, operational and personal objectives that support the delivery of the Group's key strategic goals, with 80% linked to business performance and 20% to personal performance. Performance measures and targets will be disclosed in full on a retrospective basis in next year's report. As mentioned in the Chairman's statement, from 2017 bonus onwards malus and clawback provisions will apply for a period of two years following payment, in line with best practice.

ESOP

In advance of each ESOP cycle, the Committee reviews the performance measures and corresponding targets to ensure they are appropriately stretching over the performance period. For 2017 the ESOP will continue to operate on the same basis as in 2016. The Chief Executive Officer will receive an award of 230 000 performance shares (equivalent to 55% of salary) and the other Executive Directors will each receive an award of 170 000 performance shares (equivalent to between 62% and 61% of salary).

The performance conditions remain 25% on relative TSR versus the FTSE 350 Mining Index, 37.5% on production and 37.5% on profit, measured over the three-year performance period ending on 31 December 2019. The relative TSR targets remain unchanged from 2016 and the profit and production targets will be disclosed after the performance period has ended as these targets relate to the Company's business plan and are therefore considered commercially sensitive. With effect from ESOP awards made in 2017, malus and clawback provisions will apply during the vesting period and for a period of two years following vesting, respectively.

Shareholding guidelines

In order to further align Executive Directors' interests with those of the Company's other shareholders, the Company is introducing a shareholding guideline of 100% of salary from 1 January 2017. Until the guideline has been met, Executive Directors will be required to retain at least 50% of vested awards under the ESOP or any other share-based incentive.

CHAIRMAN AND NON-EXECUTIVE DIRECTOR FEES

Chairman and non-Executive Director fees were reviewed in March 2015 when it was agreed that the Chairman's fee would be increased by 10% from £100 000 to £110 000 and the non-Executive Directors' fees by 4.8% from £52 500 to £55 000 to bring the fees more in line with market fee levels for companies of similar size and sector. The fees remained unchanged in 2016 and were reviewed again in March 2017 where it was agreed that no changes would be made at this time.

THE PERCENTAGE INCREASE IN CHIEF EXECUTIVE OFFICER REMUNERATION COMPARED WITH OTHER EMPLOYEE PAY

The table below shows the percentage change in the Chief Executive Officer's remuneration from 2015 compared to the average percentage change in remuneration for all other own employees (excluding contractors).

	CT Elphick			Other employees		
	2016 £	2015 £	% change	2016 £	2015 £	% change
Base salaries	464 802	451 264	3.0	13 295 170	12 908 516	3
Benefits	92 960	90 252	3.0	1 798 858	1 429 570	26
Annual bonuses	0	338 203	(100)	386 331	2 363 700	(84)
Total	557 762	879 719	(36)	15 480 359	16 701 786	(7)

Audited

RELATIVE IMPORTANCE OF SPEND ON PAY

The table below shows the percentage change in total employee pay expenditure and shareholder distributions (ie dividends, share buy-backs and return of capital) from the financial year ended 31 December 2015 to the financial year ended 31 December 2016.

	2016 US\$	2015 US\$	% change
Distribution to shareholders	–	11 755 200	(100)
Employee remuneration ¹	23 689 173	23 727 685	(0.2)
Return of capital	n/a	n/a	n/a

Audited

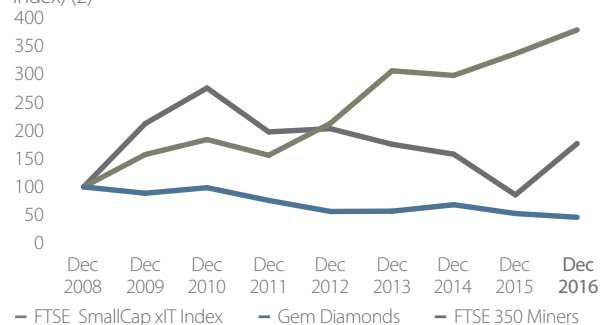
¹ Includes salary, pension and benefits, bonus, accounting charge for the ESOP, and employer national insurance contribution.

PAY FOR PERFORMANCE

The graph below shows the Company's TSR performance compared with the performance of the FTSE 250 (excluding investment trusts) and the FTSE 350 Mining Index over the eight-year period to 31 December 2016. The FTSE 250 has been selected to provide a broad market comparator group, and the FTSE 350 Mining Index has been selected because the Group and the constituents of the index are affected by similar commercial and economic factors. The table below the graph details the Chief Executive Officer's single figure of remuneration and actual variable pay outcomes over the same period.

Value of £100 invested on 1 January 2009

(Gem Diamonds versus FTSE 350 Mining Index and FTSE SmallCap xIT Index) (£)



The Annual Report on Remuneration continued

	2009	2010	2011	2012	2013	2014	2015	2016
Chief Executive Officer single figure of remuneration (£)	640 150	726 050	797 755	564 419	776 406	892 935	879 719	557 762
Annual bonus outcome (% of maximum)	54	67	75	13	61	83	74	–
ESOP vesting outcome (% of maximum)	Nil	Nil	Nil	Nil	Nil	Nil	Nil	28.26

Audited

DILUTION

ESOP awards may be satisfied with newly issued shares subject to aggregate dilution limits. The issue of shares to satisfy awards under the Company's share schemes will not exceed 10% of the

Company's issued ordinary share capital in any rolling 10-year period. As of 31 December 2016, a total of 3 528 548 shares (2.6% of issued share capital) have been or may be issued pursuant to all current awards outstanding over the last 10 years.

DETAILS OF OUTSTANDING AWARDS OF PERFORMANCE SHARES TO DIRECTORS

	Date of grant	Performance shares ¹ as at 1 January 2016	Granted in the year	Vested in the year	Lapsed in the year	Exercised in the year	Exercise price US\$	Market value at date of grant US\$	Earliest normal exercise date	Expiry date	Performance shares outstanding at 31 December 2016
Directors											
CT Elphick	10 June 2014	206 000	–	–	–	–	0.01	556 200	10 June 2017	10 June 2024	206 000
	1 April 2015	230 000	–	–	–	–	0.01	453 100	1 April 2018	1 April 2025	230 000
	15 March 2016	–	230 000	–	–	–	0.01	322 000	15 March 2019	15 March 2026	230 000
	Total	436 000	230 000								666 000
M Michael	11 Sept 2012	18 544	–	–	–	–	0.01	68 400	1 Jan 2016	31 Dec 2023	18 544
	10 June 2014	112 000	–	–	–	–	0.01	302 400	10 June 2017	10 June 2024	112 000
	1 April 2015	170 000	–	–	–	–	0.01	334 900	1 April 2018	1 April 2025	170 000
	15 March 2016	–	170 000	–	–	–	0.01	238 000	15 March 2019	15 March 2026	170 000
Total	300 544	170 000								470 544	
GE Turner	10 June 2014	138 000	–	–	–	–	0.01	372 600	10 June 2017	10 June 2024	138 000
	1 April 2015	170 000	–	–	–	–	0.01	334 900	1 April 2018	1 April 2025	170 000
	15 March 2016	–	170 000	–	–	–	0.01	238 000	15 March 2019	15 March 2026	170 000
Total	308 000	170 000								478 000	

Audited

¹ Conditional right to acquire shares.

DETAILS OF OUTSTANDING AWARDS OF PERFORMANCE OPTIONS TO DIRECTORS

Directors	Performance options ¹ as at 1 January 2016	Granted in the year	Vested in the year	Lapsed in the year	Exercised in the year	Exercise price GB pence	Date of grant	Earliest normal exercise date	Expiry date	Performance options outstanding at 31 December 2016
M Michael	37 088 ²	–	–	–	–	177.60	11 September 2012	1 January 2016	31 December 2023	37 088

Audited

¹ Option is a right to acquire shares granted under the plan including, unless indicated otherwise, a nil-cost option. The market price of an ordinary share at the year end was 107.50 pence. The highest and lowest closing prices in the year were 147.50 pence and 98.00 pence respectively. Details of the vesting conditions, which are subject to audit, for awards made under the ESOP are included in Note 25 of the financial statements and a full set of the rules will be available for inspection at the AGM.

² These awards were granted to M Michael before he became a Director.

DIRECTORS' SHAREHOLDINGS AND INTERESTS IN SHARES

Details of interests in the share capital of the Company of those Directors in office as at 31 December 2016 are given below. It is confirmed that there were no changes to the Directors' holdings

between 31 December 2016 and up to the date of this report. No Director held an interest in the shares of any subsidiary company.

In addition to these interests in shares, the Executive Directors, along with other employees, also have conditional rights to acquire shares under the Company's Long-Term Incentive Plan disclosed in Note 25 to the financial statements.

Executive Directors	Shares owned outright as at 31 December 2016	Subject to performance conditions	Performance shares held		Performance options held		Total shareholding
			Unvested and subject to continued employment only	Vested but not exercised	Subject to performance conditions	Vested but not exercised	
CT Elphick	9 325 000 ¹	460 000	58 209	Nil	–	Nil	9 843 209
M Michael	10 000	340 000	31 648	18 544	–	37 088	437 280
GE Turner	400 000	340 000	38 994	Nil	–	Nil	778 994

Audited

¹ CT Elphick is interested in these ordinary shares by virtue of his interest as a potential beneficiary in a discretionary trust which has an indirect interest in those ordinary shares.

The Annual Report on Remuneration continued

Number of shares as at 31 December 2016 held in own right

Non-Executive Directors

RW Davis	1 267 752
GA Beevers	159 964
M Salamon	316 944

DIRECTORS' EXTERNAL APPOINTMENTS

Apart from private Group interests listed in the prospectus dated 1 April 2009, no Executive Director holds any significant executive directorship or appointments outside the Group with the exception of Clifford Elphick, who was appointed non-Executive Chairman of Jumelles Holdings Limited in 2009 and Zanaga Iron Ore Co Limited, which listed on the AIM Market of the London Stock Exchange in November 2010. Total fees paid to Clifford Elphick by Zanaga are £83 000. Any fees paid to Clifford Elphick in fulfilling these external roles are retained by him.

By order of the Board

Mike Salamon

Chairman of the Remuneration Committee

14 March 2017

Directors' Report

The Directors take pleasure in submitting the financial statements of the Group for the year ended 31 December 2016.

As a British Virgin Islands (BVI) registered company, Gem Diamonds Limited is not obliged to comply with the Companies Act, 2006. However, the Directors have elected to conform to the requirements of the Companies Act, 2006.

This requires that the Directors present a Strategic Report and a Directors' Report to inform shareholders of the Company and help them assess the extent to which the Directors performed their duty to promote the success of the Company.

For the purposes of compliance with DTR 4.1.5R(2) and DTR 4.1.8R, the required content of the Management Report can be found in the Strategic Report and the Directors' Report, including the sections of the Annual Report and Accounts incorporated by reference.

The Strategic Report has been prepared to provide the Company's shareholders with a fair review of the business of the Company and a description of the principal risks and uncertainties facing it. It may not be relied upon by anyone, including the Company's shareholders, for any other purpose.

The Strategic Report and other sections of this report contain forward-looking statements. By their nature, forward-looking statements involve several risks, uncertainties and future assumptions because they relate to events and/or depend on circumstances that may or may not occur in the future which could cause actual results and outcomes to differ materially from those expressed or implied by the forward-looking statements. No assurance can be given that the forward-looking statements in the Strategic Report will be realised. Statements about the Directors' expectations, beliefs, hopes, plans, intentions and strategies are inherently subject to change and are based on expectations and assumptions about future events, circumstances and other factors which are, in some cases, outside the Company's control. The information contained in the Strategic Report has been prepared based on the knowledge and information available to Directors at the date of its preparation and the Company does not undertake any obligation to update or revise the Strategic Report during the financial year ahead. It is believed that the expectations set out in the forward-looking statements are reasonable, but they may be affected by a wide range of variables which could cause actual results or trends to differ materially. In particular, the forward-looking statements should be read in context with actual historic information provided. The Company's shareholders are cautioned not to place undue reliance on the forward-looking statements. Shareholders should note that the Strategic Report has not been audited, but the Auditor's Report does include a statement that the Strategic Report is consistent with the financial statements herein.

RELATED-PARTY TRANSACTION

Other than those disclosed in Note 23 of the financial statements, the Company did not have any transactions with, nor made loans to related parties during the period in which any Director is or was interested.

RESOURCE DEVELOPMENT

Resource development activities were concentrated on improving the understanding of existing resources at Letšeng and Ghaghoo, and no additional resources and reserves were added.

The re-assessment of historical geological studies at Letšeng was augmented by detailed pit floor mapping and updating of geological models, and provided motivation for another phase of core drilling in both the Main and Satellite pipes, scheduled to start in the first half of 2017. Various techniques are being considered in the search for tools to predict not only grade at depth, but also the occurrence of the rare high value Type II diamonds upon which Letšeng is so dependent.

At Ghaghoo, the evaluation of the lower grade VKMain domain was initiated. This domain was originally excluded from the underground mining reserves due to its low grade. The sample confirmed the reserve estimates. Additional resource delineation drilling was completed to confirm geological contacts for levels one and two.

Further details can be found in the mineral resource management section on pages 46 to 49.

RESULTS AND DIVIDENDS

The Group's attributable profit after taxation (before exceptional items) amounted to US\$17.7 million (2015: US\$41.8 million). Post-exceptional items, the Group's attributable loss was US\$158.8 million.

The Group's detailed financial results are set out in the financial statements section on pages 112 to 169.

The Board has adopted a dividend policy that determines the appropriate dividend each year, based on consideration of the Company's cash resources; the level of free cash flow and earnings generated during the year; and expected funding commitments for capital projects relating to the Group's growth strategy. In current market and operational constraints, Gem Diamonds has remained focused on cost discipline and its fundamental goal of extracting the maximum value from its resources for long-term shareholder value creation. In light of the current trading conditions, the disappointing results and the reduced cash resources, the Board has not approved a dividend for the 2016 results.

Directors' Report continued

CORPORATE SOCIAL RESPONSIBILITY AND SUSTAINABILITY

A review of health, safety, corporate social responsibility, environmental performance and community participation is presented in the Sustainable Development Review on pages 53 to 58.

GREENHOUSE GAS (GHG) EMISSIONS

Our approach to emission management

The Group carefully manages its Scope 1 emissions, that is, direct GHG emissions that occur from sources that are owned or controlled by the Group, for example, stationary and mobile combustion. Scope 2 emissions consist of GHG emissions from the generation of purchased electricity. The Group focuses on reducing these emissions by enhancing efficiencies across its operations. Scope 3 emissions that are most material to the organisation are carefully managed. These include emissions resulting from employee and contractor transportation.

In 2016, the total carbon footprint for the Group was 184 765tCO₂e (compared to 146 499tCO₂e in 2015), primarily driven by electricity consumption and mobile and stationary fuel combustion. This figure includes the direct GHG emissions (Scope 1), energy indirect GHG (Scope 2) emissions, and material Scope 3 emissions, and was calculated with boundaries clearly defined by the GHG Protocol Corporate Accounting and Reporting Standard.

The total Group footprint signifies an increase of 26% from 2015. This observed increase is the result of a significant increase in diesel usage at Letšeng (an increase of 32% in diesel usage for mobile combustion and 70% for stationary combustion). The combined increase of 32% for liquid petroleum gas and 25% increase in explosives further attributed to this increase.

Electricity consumption accounted for 68 306tCO₂e (37%) of the carbon footprint, down from 68 885tCO₂e in 2015. The combined emissions from mobile and stationary combustion accounted for 83 974tCO₂e (45%) of the total footprint, compared to 63 914tCO₂e (43%) in 2015. The increase year on year has resulted from an increase in mining activity and generator use at Letšeng due to electricity supply distributions and disruptions that were caused by the inclement weather conditions.

The Group also tracks the tonnes of CO₂ emitted per employee and per carat recovered (from total Scope 1 and 2 emissions). The ratio of 240tCO₂e in 2015 per employee has increased to 347tCO₂e per employee in 2016. The increases were directly related to an overall increase in the carbon footprint and a 24% decrease in permanent employee numbers (down to 446 from 589). The ratio of 0.66tCO₂ per carat in 2015 increased to 1.04tCO₂e per carat in 2016. This change can be attributed to an increase in the total carbon footprint and a decrease of 25% in the number of carats recovered during the year as well as the decrease in employee numbers.

As a Group, Gem Diamonds recognises that understanding its environmental impact and reducing its level of GHG emissions involves more than simply assessing its carbon footprint. Therefore, the Group is actively implementing measures to reduce emissions, especially at its Letšeng operation.

WATER FOOTPRINT

Fresh water is one of the most important, and increasingly scarce, commodities on earth. As water stewards, Gem Diamonds seeks to understand the risks posed by water scarcity and pollution and undertakes to ensure that water is managed sustainably. As such, caring for water sources and monitoring water usage are crucial practices in both a commercial and moral respect. Protecting water sources helps the Group to maintain its social licence to operate.

The Group's water footprint (WF) studies provide an integrated understanding of its water abstraction and water use. A WF can be defined as a measure of freshwater appropriation underlying a certain product, including fresh surface water, groundwater incorporated into the product or lost during the manufacturing of the product.

The total WF for Gem Diamonds' operations during the 2016 technical year was 8 701 985m³. The water sources included municipal supplies, groundwater, surface water and direct rainfall. The total water recycled and reused by the operations was 5 826 137m³ (67%) and the net water usage related to evaporation (88%), entrainment (9%), consumption (3%) and dust suppression (0.2%). The amount of water that finds its way back into the environment through discharge and seepage accounted for 3 023 034m³.

In 2016, total WF for the Group was 37.8m³ per carat and 1.21m³ per ore tonne treated. The increases were directly related to a 12% increase in water usage and 25% decrease in recovered carats.

The stress WF of the Group, which is the stress placed on the water system by mining activity consumption, was found to be sustainable.

POLITICAL DONATIONS

The Group made no political donations during 2016.

CORPORATE SOCIAL INVESTMENT (CSI) EXPENDITURE

The Group's CSI expenditure supports initiatives that benefit its PACs in the areas of health, education, infrastructure development, development of small to medium enterprises and general donations to relevant causes in the Group's PACs. In 2016, the Group contributed US\$0.4 million to social initiatives, down from US\$0.6 million in 2015. This decrease can be attributed to a shift of focus at Ghaghoo from proactive intervention to project maintenance in line with the Group's objective of honouring its commitments to communities while managing the pressures of strained market conditions.

EMPLOYEE POLICIES AND INVOLVEMENT

To gain a fuller understanding of matters related to employee policies and involvement, this segment should be read in conjunction with the information on employment matters contained in the Sustainable Development Review in this report on pages 53 to 58 together with the full 2016 Sustainable Development Report which is available on the Company's website.



The Group's employment practices have been developed to ensure that the Group attracts and retains the required calibre of management and staff by creating an environment which incentivises enhanced performance. The health, safety and effective performance of employees, together with maintaining positive employee relations is of key importance across the Group's operations.

Employees are kept informed about the performance and objectives of the Group through direct involvement and access to the Company's website, published information, the circulation of press cuttings and Group announcements, as well as continuous communication between employees and management.



It is the Group's policy to communicate openly with employees and encourage dialogue between employees and management.

The Company strives to have a direct relationship between its employees and business function management founded on quality, leadership, effective communication and trust. The Group is committed to the principle and achievement of equal opportunities in employment, irrespective of gender, religion, race or marital status. Full consideration is given to applications from people with disabilities who apply for positions which they can adequately fill, having regard for their particular abilities and aptitude. Where existing employees become disabled, it is the Group's policy, where practical, to provide continuing employment under normal terms and conditions and to provide training, career development and promotion to disabled employees wherever possible.

The Group sets guidelines and frameworks in respect of Company policy on remuneration benefit, performance management, career development, succession planning, recruitment, expatriate employment and for the alignment of human resources management and policy with international best practice. Each operating unit manages its human resources requirements locally, within the Group's guidelines and framework.

CORPORATE GOVERNANCE

The UK Financial Conduct Authority's Disclosure Guidance and Transparency Rules (DTR 7.2) require that certain information be included in a corporate governance statement set out in the Directors' Report. The Group has an existing practice of issuing a separate Corporate Governance Code Compliance Report as part of its Annual Report. The information required by the Disclosure Guidance and Transparency Rules and the UK Financial Conduct Authority's Listing Rules (LR 9.8.6) is located on pages 66 to 73 of this Annual Report.

GOING CONCERN

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 2 to 59. The financial position of the Company, its cash flows and liquidity position are described in the Strategic Report on pages 34 to 39. In addition, Note 24 and Note 26 to the financial statements include the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments; and its exposures to credit and liquidity risk.

Directors' Report continued

After making enquiries which review forecasts and budgets, timing of cash flows, borrowing facilities and sensitivity analyses and considering the uncertainties described in this report either directly or by cross-reference, the Directors have a reasonable expectation that the Group has adequate financial resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going-concern basis in preparing the Annual Report and Accounts of the Company.

VIABILITY STATEMENT

In accordance with provision C.2.2 of the 2014 revision of the UK Corporate Governance Code, the Directors have assessed the prospect of the Company over a longer period of 12 months as required by the 'Going Concern' provision. The viability statement can be found in the Strategic Report on page 25.

DIRECTORS

The Directors, as at the date of this report, are listed on pages 62 and 63 together with their biographical details. Details of the Directors' interests in shares and share options of the Company can be found in the Annual Report on Remuneration on page 103.

Directors who held office during the year and date of appointment/resignation

Executive Directors

CT Elphick	20 January 2006
AR Ashworth	22 April 2008/7 June 2016
GE Turner	22 April 2008
M Michael	22 April 2013

Non-Executive Directors

RW Davis	1 February 2007
GA Beevers	1 February 2007
M Salamon	3 February 2008
MD Lynch-Bell	15 December 2015

Re-election of Directors

The Articles of Association (81) provides that a third of Directors retire annually by rotation and, if eligible, offer themselves for re-election. However, in accordance with the Code, at each AGM all the Directors retire and, subject to being eligible, offer themselves for re-election. Each Director has been the subject of a recent Board evaluation.

Protection available to Directors

By law, Directors are ultimately responsible for most aspects of the Group's business dealings. Consequently, they face potentially significant personal liability under criminal or civil law, or the UK Listing, Prospectus and Disclosure and Transparency Rules and

face a range of penalties including private or public censure, fines and/or imprisonment. In line with normal market practice, the Group believes that it is in its best interests to protect the individuals prepared to serve on its Board from the consequences of innocent error or omission, as this enables the Group to attract prudent individuals to act as Directors.

Therefore, the Group has, and continues to maintain, at its expense, a Director and Officer's liability insurance policy to provide indemnity, in certain circumstances, for the benefit of Directors and other Group personnel. The insurance policy does not provide cover where the Director or Group personnel member has acted fraudulently or dishonestly.

In accordance with the Company's Articles of Association, the Company has and continues to maintain indemnities granted by the Company to the Directors of the Company and the Company's associated companies to the extent permitted by and consistent with BVI law and the UK Companies Act, 2006 and rules made by the UK Listing Authority.

ANNUAL GENERAL MEETING

Details of the resolutions which will be put to the AGM are given in the Notice of AGM, which is a separate document from the Annual Report.

SHARE CAPITAL AND VOTING RIGHTS

Details of the authorised and issued share capital of the Company, including the rights pertaining to each share class, are set out in Note 16 to the financial statements.

As at 14 March 2017, there were 138.4 million fully paid ordinary shares of £0.01 each in issue and listed on the official list maintained by the FCA in its capacity as the UK Listing Authority.

The Company has one class of ordinary shares. Shareholders have the right to receive notice of and attend, speak and vote at any general meeting of the Company. Each shareholder who is present in person (or, being a corporation, by representative) or by proxy at a general meeting on a show of hands has one vote and, on a poll, every such holder present in person (or, being a corporation, by representative) or by proxy shall have one vote in respect of every ordinary share held by them. To be valid, the appointment of a proxy to vote at a general meeting must be received not less than 48 hours before the time appointed for holding the meeting. In addition, the holders of ordinary shares have the right to participate in dividends and other distributions according to their respective rights and interests in the profit of the Company.

There are no shareholders who carry any special rights with regard to the control of the Company. The Company is not aware of any agreements between holders of securities which may result in restrictions on transfers or voting rights, save as mentioned below.

There are no restrictions on the transfer of ordinary shares other than:

- ▶ as set out in the Company's Articles of Association;
- ▶ certain restrictions may from time to time be imposed by laws and regulations; and
- ▶ pursuant to the Company's share dealing code whereby the Directors and employees of the Company require approval to deal in the Company's ordinary shares.

At the AGM held in 2016, shareholders authorised the Company to make on-market purchases of up to 13 829 646 of its ordinary shares, representing approximately 10% of the Company issued share capital at that time. During 2016, the Company did not make any on-market or off-market purchases of its shares or shares under any buy-back programme. Shareholders will be asked at the 2017 AGM to renew this authority. The Directors have no present intention to exercise this authority, if granted. Details of deadlines for exercising voting rights and proxy appointments will be set out in the 2017 Notice of AGM.

MAJOR INTERESTS IN SHARES

Details of the major interests (at or above 3%) in the issued ordinary shares of the Company are set out in the UK Corporate Governance Code Compliance Report on page 73.

DIRECTORS' INTERESTS

No Director had, at any time during the year, a material interest in any contract of significance in relation to the Company's business. The interest of Directors in the shares of the Company is included in the Annual Report on Remuneration on page 103.

CREDITORS' PAYMENT PRACTICE

In view of the international nature of the Group's operations, there is no specific Group-wide policy in respect of payments to suppliers. Individual operating companies are responsible for agreeing terms and conditions for their business transactions and ensuring that suppliers are aware of the terms of payment. It is Group practice that payments are made in accordance with those terms, provided that all trading terms and conditions have been met by the supplier. Trade creditors at 31 December 2016 represented 28 days of the Company's annual purchases.

SUBSEQUENT EVENTS

Refer to Note 29 of the financial statements for details of events subsequent to the reporting date.

ELECTRONIC COPIES OF DOCUMENTS

Copies of the 2016 Annual Report, HSSE policies and other corporate publications, reports, press releases and announcements are available on the Company's website.

DISCLOSURE OF INFORMATION AND AUDITOR RE-ELECTION

The Lead Audit Partner is based in London, UK. Further information regarding audit firm rotation and re-election requirements are detailed in the Audit Committee Report on pages 78 and 79.

As required under section 418 of the Companies Act, 2006, to which the Directors have voluntarily elected to conform, each Director confirms that to the best of his knowledge and belief, there is no information relevant to the preparation of the Auditor's Report of which the Company's auditors are unaware of and that each Director has taken all reasonable steps 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.

A resolution to reappoint EY as the Company's auditors and to authorise the Board to determine the auditors' remuneration will be proposed at the 2017 AGM.

The Strategic Report, the Directors' Report and the Directors' Remuneration Report were approved by the Board on 14 March 2017.

By order of the Board

Glenn Turner
Company Secretary

14 March 2017





Financial statements

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Responsibility Statement of the Directors in Respect of the Annual Report and Financial Statements

The Directors are responsible for preparing the Annual Report and the Group financial statements in accordance with International Financial Reporting Standards (IFRS). Having taken advice from the Audit Committee, the Board considers the report and accounts taken as a whole, are fair, balanced and understandable and that they provide the information necessary for shareholders to assess the Company's performance, business model and strategy.

The Strategic Report and 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.

PREPARATION OF THE FINANCIAL STATEMENTS

The Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group, and of their profit or loss for that period. In preparing the Group financial statements, the Directors are required to:

- ▶ select suitable accounting policies and then apply them consistently;
- ▶ make judgements and estimates that are reasonable and prudent;
- ▶ state whether they have been prepared in accordance with IFRS;
- ▶ state whether applicable IFRS have been followed, subject to any material departures disclosed and explained in the Group financial statements; and
- ▶ prepare the financial statements on the going-concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's transactions and disclose, with reasonable accuracy at any time, the financial position of the Group. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors confirm that the financial statements, prepared in accordance with IFRS, give a true and fair view of the assets, liabilities, financial position and profit of the Company and the undertakings included in the consolidation taken as a whole. In addition, suitable accounting policies have been selected and applied consistently.

Information, including accounting policies, has been presented in a manner that provides relevant, reliable, comparable and understandable information, and additional disclosures have been provided when compliance with the specific requirements in IFRS have been insufficient to enable users to understand the financial impact of particular transactions, other events and conditions on the Group's financial position and financial performance. Where necessary, the Directors have made judgements and estimates that are reasonable and prudent.

The Directors of the Company have elected to comply with the Companies Act 2006, in particular the requirements of Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 of the United Kingdom pertaining to Directors' remuneration which would otherwise only apply to companies incorporated in the UK.

Michael Michael
Chief Financial Officer

14 March 2017

Independent Auditor’s Report to the Members of Gem Diamonds Limited

OUR OPINION ON THE FINANCIAL STATEMENTS

In our opinion:

- ▶ the financial statements of Gem Diamonds Limited (the Group) give a true and fair view of the state of the Group’s affairs as at 31 December 2016 and of its profit for the year then ended; and
- ▶ the financial statements have been properly prepared in accordance with IFRS.

The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards.

OVERVIEW OF OUR AUDIT APPROACH

Risks of material misstatement	<ul style="list-style-type: none"> ▶ Revenue recognition ▶ Assessing the Ghaghoo development asset for impairment
Audit scope	<ul style="list-style-type: none"> ▶ We performed a full scope audit of three components and audit procedures on specific balances for a further six components ▶ The components where we performed full or specific audit procedures accounted for 99% of pre-tax profit, 100% of revenue and 99% of total assets
Materiality	<ul style="list-style-type: none"> ▶ Overall Group materiality was US\$2.6 million which represents 5% of pre-tax profit; excluding exceptional items. We exclude the exceptional items, being the impairment on Ghaghoo and the abandonment of the Calibrated Diamonds Investment Holdings (Proprietary) Limited Group (CDIH), as they represent unusual non-recurring events

Independent Auditor’s Report to the Members of Gem Diamonds Limited continued

OUR ASSESSMENT OF RISK OF MATERIAL MISSTATEMENT

We identified the risks of material misstatement described below as those that had the greatest effect on our overall audit strategy, the allocation of resources in the audit and the direction of the efforts of the audit team. In addressing these risks, we have performed the procedures below which were designed in the context of the financial statements as a whole and, consequently, we do not express any opinion on these individual areas.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Revenue recognition</p> <p><i>Refer to the Audit Committee Report (page 76); Accounting policies (page 139); and Note 2 of the Annual Financial Statements (page 144).</i></p>		
<p>The Group recognised revenue of US\$189.8 million in the year (2015: US\$249.5 million). Diamonds are sold through the following revenue streams:</p> <ul style="list-style-type: none"> ▶ Rough diamonds sold on tender; ▶ Selected diamonds sold through partnership arrangements; ▶ Diamonds extracted for purposes of manufacturing and sold thereafter in polished form; and ▶ Diamonds sold through joint operation arrangements. <p>We focused on this area due to the inherent risk related to the recognition and measurement of revenue, particularly on partnership arrangements and diamonds extracted for purposes of manufacturing (cutting and polishing).</p> <p>For partnership arrangements, revenue is earned on the sale of the rough diamond, with an additional uplift recognised on the polished margin achieved. Judgement is involved in determining when the risks and rewards of ownership transfer on the sale of the rough diamond.</p> <p>For diamonds extracted for purposes of manufacturing, no revenue is recognised by the Group until the diamonds are sold to third parties; as a result, there are a number of intercompany transactions that must be eliminated in the consolidated financial statements. There is a risk relating to the completeness of sales recognised through the extraction process in light of the polishing losses that result from the manufacturing process.</p>	<ul style="list-style-type: none"> ▶ We considered all diamond revenue streams as significant, and therefore, observed the design effectiveness of the controls around the revenue process in understanding management’s internal processes and the control environment. ▶ We verified management’s recognition of revenue, covering all revenue streams of the Group. This involved agreeing revenue transactions to underlying customer agreements, invoices and supporting calculations to confirm the accuracy and occurrence of the sales recorded. ▶ For partnership arrangements, we assessed the appropriateness of management’s judgement, in determining when risks and rewards are transferred, by reviewing correspondence between management and the partner that confirms no managerial involvement after the sale of the rough stone. ▶ We assessed the accounting treatment of all stones sold through joint operation arrangements ensuring they are recognised in accordance with IFRS 11 Joint Arrangements. ▶ We performed cut off testing at year end by selecting transactions close to the year end, ensuring the revenue was recognised in the correct period. ▶ We also reviewed management’s reconciliation of inventory movements from stones recovered and exported from Letšeng to those sold during the year and the remaining inventory on hand at Gem Diamonds Marketing Services at year end to validate the completeness of revenue. 	<p>We concluded that revenue recognised in the year has been appropriately recognised on the basis of our procedures.</p>

Risk	Our response to the risk	Key observations communicated to the Audit Committee
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Assessing the Ghaghoo development asset for impairment

Refer to the Audit Committee Report (page 77); Accounting policies (page 141); and Note 12 of the Annual Financial Statements (page 152).

<p>We focused on this area due to the size of the Ghaghoo development asset (pre-impairment) that had increased to US\$130.7 million from US\$117.6 million (post-impairment) in June 2016 (2015: US\$141.9 million) and because of the judgements and estimates involved in determining the expected future performance of the mine.</p> <p>Management's decision to place the mine on care and maintenance in February 2017 was determined to be evidence of the existence of impairment indicators at year end.</p> <p>Having reassessed Ghaghoo's recoverable amount, management has provided for the impairment of US\$170.8 million for the year ended 31 December 2016 (which includes the US\$40.0 million recognised at 30 June 2016), being the development asset and all property, plant and equipment comprising the Ghaghoo cash-generating unit.</p> <p>Management has classified the Ghaghoo US\$25.0 million facility as current at year end as it is required to be repaid once the mine is placed on care and maintenance.</p>	<ul style="list-style-type: none"> ▶ We tested the methodology applied in the value-in-use calculation relative to the requirements of International Accounting Standards (IAS) 36 Impairment of Assets, and the mathematical accuracy of management's model. ▶ We obtained an understanding of and assessed the basis for key underlying assumptions in the mine's business plan: focussing on diamond prices and discount rates. ▶ We challenged management's cash flow forecasts by considering evidence available to support assumptions for reasonableness and the reliability of past forecasts. ▶ We checked that hindsight was not used in determining the amount of the year end impairment. ▶ We engaged EY specialists to assess the reasonableness of the methodology used in determining the discount rate and challenge management's price and discount rate assumptions by benchmarking against industry peers. ▶ We performed sensitivity testing on the price and discount rate assumptions used. ▶ We assessed the implications of the announcement, post-balance sheet date, to place the mine on care and maintenance. ▶ Verified that all required disclosures in the consolidated financial statements were complete and adequately reflected the outcome of management's care and maintenance decision. 	<p>Based on the above findings we note that the model is sensitive to any changes in assumptions. Given the current market conditions and the history of the asset, we believe any such changes that would result in less than a full impairment would be optimistic. Therefore we concur with management's decision to fully impair the non-current assets.</p> <p>We believe management's recognition and related disclosure of the impairment in the financial statements to be reasonable and in line with IAS 36 Impairment.</p>
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The risk around the key judgements relating to production start date is no longer applicable following the decision to place the mine on care and maintenance.

Independent Auditor’s Report to the Members of Gem Diamonds Limited continued

THE SCOPE OF OUR AUDIT

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each entity within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the Group and effectiveness of Group-wide controls, changes in the business environment and other factors when assessing the level of work to be performed at each entity.

In assessing the risk of material misstatement to the Group financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements, of the 20 reporting components of the Group, we selected 13 components (the remaining seven components are dormant) covering entities within Belgium, Botswana, Lesotho, South Africa, United Arab Emirates, and the United Kingdom, which represent the principal business units within the Group.

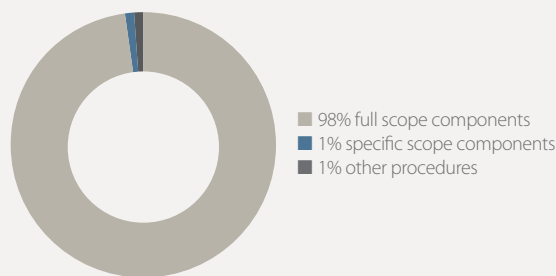
Of the 13 components selected, we performed a full scope audit of three components which were selected based on their size or risk characteristics. For six components (specific scope components), we performed audit procedures on specific accounts within that component that we considered had the potential for the greatest impact on the significant accounts in the financial statements either because of the size of these accounts or their risk profile.

The components where we performed audit procedures accounted for 99% (2015: 99%) of the Group’s pre-tax profit, 100% (2015: 100%) of the Group’s revenue and 97% (2015: 97%) of the Group’s total assets. For the current year, the full scope components contributed 98% (2015: 98%) of the Group’s pre-tax profit, 98% (2015: 98%) of the Group’s revenue and 95% (2015: 95%) of the Group’s total assets. The specific scope components contributed 1% (2015: 1%) of the Group’s pre-tax profit, 2% (2015: 2%) of the Group’s revenue and 2% (2015: 2%) of the Group’s total assets. The audit scope of these components may not have included testing of all significant accounts of the component but contributed to the coverage of significant accounts tested for the Group.

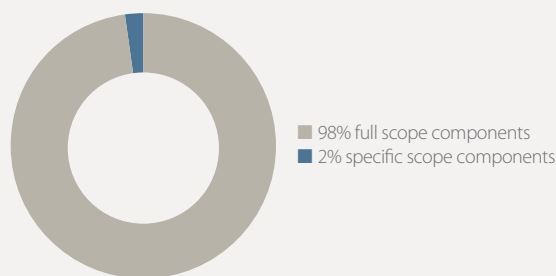
Of the remaining four components that together represent 1% of the Group’s pre-tax profit, we performed other procedures, including analytical reviews, testing of consolidation journals and intercompany eliminations, and assessing entity level controls to respond to any potential risks of material misstatement to the Group financial statements.

The charts below illustrate the coverage obtained from the work performed by our audit teams.

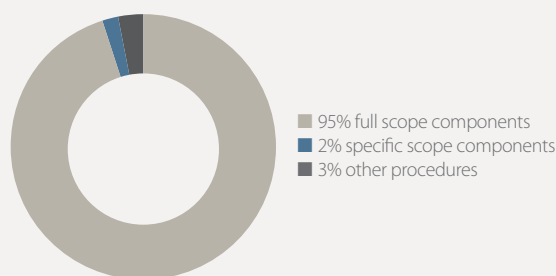
Pre-tax profit



Revenue



Total assets



CHANGES FROM THE PRIOR YEAR

Our scope allocation in the current year is broadly consistent with 2015 in terms of overall coverage of the Group, however, we did make some changes in the identity of components subject to full and specific scope audit procedures. Changes in our scope since the 2015 audit included moving the audit of the Gem Diamonds Limited standalone entity from full audit scope to a specific scope component due to only specific accounts having been considered to have a potential material impact on the significant accounts in the financial statements.

INVOLVEMENT WITH COMPONENT TEAMS

In establishing our overall approach to the Group audit, we determined the type of work that needed to be undertaken at each of the components by us, as the primary audit engagement team, or by component auditors from other EY global network firms operating under our instruction. For the three full scope components, audit procedures were performed on one of these directly by the primary audit team and by our component audit teams in Botswana and Lesotho. For the six specific scope components, audit procedures were performed on three of these directly by the primary audit team. Of the three specific scope components where the work was performed by component auditors, we determined the appropriate level of involvement to enable us to determine that sufficient audit evidence had been obtained as a basis for our opinion on the Group as a whole.

The Group audit team continued to follow a programme of planned visits that has been designed to ensure that the Senior Statutory Auditor visits each of the full scope locations at least once a year. During the current year's audit cycle, visits were undertaken by the primary audit team to the component teams in Belgium, Lesotho, and South Africa. The Global Team Planning Event was held in South Africa with representatives of the components from Botswana, Lesotho and South Africa all attending. The primary audit team also held a separate team planning event with the component audit team in Belgium. Dependent on the timing of our visits, these involved discussion of the audit approach with the component team and any issues arising from their work, consideration of the approach to revenue recognition, and meeting with local management. The primary team interacted regularly with the component teams where appropriate during various stages of the audit, reviewed key working papers, attended audit closing meetings, including discussions of fraud and error, and were responsible for the scope and direction of the audit process. This, together with the additional procedures performed at Group level, gave us appropriate evidence for our opinion on the Group financial statements.

OUR APPLICATION OF MATERIALITY

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Group to be US\$2.6 million (2015: US\$5.4 million), which is 5% (2015: 5%) of pre-tax profits, excluding exceptional items. We have excluded the exceptional item, being the impairment, recognised on Ghaghoo and the abandonment of the CDIH group, as they represent non-recurring events. We consider pre-tax profit provides us with the most relevant performance measure to the stakeholders of the entity given the production stage of the Group's Letšeng mine. Our planning materiality has decreased by 52% compared to 2015 given the reduction in pre-tax profit recognised by the Group in 2016.

During the course of our audit, we reassessed initial materiality and changed our final materiality to reflect the actual reported performance of the Group in the year.

Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 50% (2015: 50%) of our planning materiality, namely US\$1.3 million (2015: US\$2.7 million). We have set performance materiality at this percentage due to our expectation of misstatements identified based on prior experience.

Audit work at component locations for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was US\$0.2 million to US\$1 million (2015: US\$0.4 million to US\$1.4 million).

Independent Auditor's Report to the Members of Gem Diamonds Limited continued

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We have agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of US\$0.1 million (2015: US\$0.2 million), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

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 and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITOR

As explained more fully in the Directors' responsibilities statement set out on page 112, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

In addition, the Company has also instructed us to:

- ▶ report whether the section of the Directors' Remuneration Report that is described as audited has been properly prepared in accordance with the basis of preparation described therein;
- ▶ report on whether in the course of the audit:
 - the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.
 - the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements;
- ▶ report as to whether the information given in the Corporate Governance Statement set out on pages 66 to 73 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures and in compliance with rules 7.2.5 and 7.2.6 of the Disclosure Guidance and Transparency Rules sourcebook made by the Financial Conduct Authority:
 - is consistent with the financial statements and
 - has been prepared in accordance with applicable legal requirement.

Report on whether in the course of the audit rules 7.2.2, 7.2.3 and 7.2.7 in the Disclosure Guidance and Transparency Rules sourcebook made by the Financial Conduct Authority (with respect to the Company's corporate governance code and practices about its administrative, management and supervisory bodies and their committees) have been complied with if applicable.

This report is made solely to the Company's members, as a body, in accordance with the terms of our engagement letter dated 4 March 2016.

Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

<p>ISAs (UK and Ireland) reporting</p>	<p>We are required to report to you if, in our opinion, financial and non-financial information in the Annual Report is:</p> <ul style="list-style-type: none"> ▶ materially inconsistent with the information in the audited financial statements; or ▶ apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; ▶ otherwise misleading. <p>In particular, we are required to report whether we have identified any inconsistencies between our knowledge acquired in the course of performing the audit and the directors' statement that they consider the Annual Report and accounts taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the entity's performance, business model and strategy; and whether the Annual Report appropriately addresses those matters that we communicated to the Audit Committee that we consider should have been disclosed.</p>	<p>We have no exceptions to report.</p>
<p>Engagement letter requirements</p>	<p>The Company has instructed us to report on whether, in light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have identified any material misstatements in the Strategic Report or Directors' Report or Corporate Governance Statement set out on pages 30 to 109.</p> <p>The Company has also instructed us to report whether in our opinion:</p> <ul style="list-style-type: none"> ▶ adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or ▶ the financial statements are not in agreement with the accounting records and returns; or ▶ we have not received all the information and explanations we require for our audit; or ▶ certain disclosures of directors' remuneration specified by law are not made; or ▶ a Corporate Governance Statement has not been prepared by the Company. 	<p>We have no exceptions to report.</p>
<p>Listing Rules review requirements</p>	<p>We are required to review:</p> <ul style="list-style-type: none"> ▶ the Directors' statement in relation to going concern (set out on page 107), and longer-term viability (set out on page 108). This statement is specified for review by the Listing Rules of the Financial Conduct Authority for premium listed UK incorporated companies. ▶ the part of the Corporate Governance Statement relating to the Company's compliance with the provisions of the UK Corporate Governance Code specified for our review. 	<p>We have no exceptions to report.</p>

STATEMENT ON THE DIRECTORS' ASSESSMENT OF THE PRINCIPAL RISKS THAT WOULD THREATEN THE SOLVENCY OR LIQUIDITY OF THE ENTITY

<p>ISAs (UK and Ireland) reporting</p>	<p>We are required to give a statement as to whether we have anything material to add or to draw attention to in relation to:</p> <ul style="list-style-type: none"> ▶ the Directors' confirmation in the Annual Report that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity; ▶ the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated; ▶ the directors' statement in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity's ability to continue to do so over a period of at least 12 months from the date of approval of the financial statements; and ▶ the Directors' explanation in the Annual Report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions. 	<p>We have nothing material to add or to draw attention to.</p>
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Steven Dobson (Senior Statutory Auditor)
For and on behalf of Ernst & Young LLP
London

14 March 2017

Consolidated Income Statement

for the year ended 31 December 2016

	Notes	2016 US\$'000 Before exceptional items	2016 US\$'000 Exceptional items	2016 US\$'000 Total	2015 US\$'000 Before exceptional items	2015 US\$'000 Exceptional items	2015 US\$'000 Total
CONTINUING OPERATIONS							
Revenue	2	189 815	–	189 815	249 475	–	249 475
Cost of sales		(109 063)	–	(109 063)	(122 483)	–	(122 483)
Gross profit		80 752	–	80 752	126 992	–	126 992
Other operating income	3	306	–	306	458	8 126	8 584
Royalties and selling costs		(17 170)	–	(17 170)	(21 929)	–	(21 929)
Corporate expenses		(11 234)	–	(11 234)	(11 941)	–	(11 941)
Share-based payments	25	(1 790)	–	(1 790)	(1 738)	–	(1 738)
Foreign exchange gain	3	1 715	–	1 715	6 997	1 472	8 469
Impairment of assets	4	–	(172 932)	(172 932)	–	–	–
Recycling of foreign currency translation reserve on abandonment of operation	4	–	(3 546)	(3 546)	–	–	–
Operating profit/(loss)	3	52 579	(176 478)	(123 899)	98 839	9 598	108 437
Net finance (costs)/income	5	(209)	–	(209)	120	–	120
Finance income		2 411	–	2 411	1 505	–	1 505
Finance costs		(2 620)	–	(2 620)	(1 385)	–	(1 385)
Profit/(loss) before tax for the year from continuing operations		52 370	(176 478)	(124 108)	98 959	9 598	108 557
Income tax expense	6	(19 966)	–	(19 966)	(31 553)	–	(31 553)
Profit/(loss) for the year from continuing operations		32 404	(176 478)	(144 074)	67 406	9 598	77 004
DISCONTINUED OPERATION							
Profit after tax for the year from discontinued operation	7	–	–	–	–	668	668
Profit/(loss) for the year		32 404	(176 478)	(144 074)	67 406	10 266	77 672
<i>Attributable to:</i>							
Equity holders of parent		17 668	(176 478)	(158 810)	41 759	10 266	52 025
Non-controlling interests		14 736	–	14 736	25 647	–	25 647
Earnings/(loss) per share (cents)							
– Basic earnings for the year attributable to ordinary equity holders of the parent	8	12.8	–	(114.9)	30.2	–	37.6
– Diluted earnings for the year attributable to ordinary equity holders of the parent		12.8	–	(114.9)	29.9	–	37.2

Consolidated Statement of Comprehensive Income

for the year ended 31 December 2016

	Notes	2016 US\$'000	2015 US\$'000
(Loss)/profit for the year		(144 074)	77 672
<i>Other comprehensive income that could be reclassified to the income statement in subsequent periods</i>			
Exchange differences on translation of foreign operations		24 398	(81 601)
Recycling of exchange differences on abandoned and discontinued operations	4	3 546	(988)
Other comprehensive income/(expense) for the year, net of tax		27 944	(82 589)
Total comprehensive income/(expense) for the year, net of tax		(116 130)	(4 917)
<i>Attributable to:</i>			
Equity holders of the parent		(140 793)	(15 586)
Non-controlling interests		24 663	10 669

Consolidated Statement of Financial Position

for the year ended 31 December 2016

	Notes	2016 US\$'000	2015 US\$'000
ASSETS			
Non-current assets			
Property, plant and equipment	9	257 199	339 367
Investment property	10	615	615
Intangible assets	11	14 014	13 510
Receivables and other assets	13	31	2 218
Other financial assets		–	4
		271 859	355 714
Current assets			
Inventories	14	30 911	30 288
Receivables and other assets	13	6 557	5 827
Other financial assets		–	6
Income tax receivable		4 636	269
Cash and short-term deposits	15	30 787	85 719
		72 891	122 109
Total assets		344 750	477 823
EQUITY AND LIABILITIES			
Equity attributable to equity holders of the parent			
Issued capital	16	1 384	1 383
Share premium		885 648	885 648
Treasury shares ¹		(1)	(1)
Other reserves	16	(143 498)	(163 420)
Accumulated losses		(610 329)	(439 764)
		133 204	283 846
Non-controlling interests		70 623	59 923
Total equity		203 827	343 769
Non-current liabilities			
Interest-bearing loans and borrowings	17	–	25 082
Trade and other payables	18	1 409	1 138
Provisions	19	16 630	12 473
Deferred tax liabilities	20	65 676	50 385
		83 715	89 078
Current liabilities			
Interest-bearing loans and borrowings	17	27 757	5 339
Trade and other payables	18	29 012	32 228
Income tax payable		439	7 409
		57 208	44 976
Total liabilities		140 923	134 054
Total equity and liabilities		344 750	477 823

¹ Shares held by the Gem Diamonds Limited Employee Share Trust.

Approved by the Board of Directors on 14 March 2017 and signed on their behalf by:

CT Elphick
Director

M Michael
Director

Consolidated Statement of Changes in Equity

for the year ended 31 December 2016

	Attributable to the equity holders of the parent					Total US\$'000	Non- controlling interests US\$'000	Total equity US\$'000
	Issued capital ¹ US\$'000	Share premium ¹ US\$'000	Own shares ² US\$'000	Other reserves ¹ US\$'000	Accumulated (losses)/ retained earnings US\$'000			
Balance at 1 January 2016	1 383	885 648	(1)	(163 420)	(439 764)	283 846	59 923	343 769
Total comprehensive income/ (expense)	–	–	–	18 017	(158 810)	(140 793)	24 663	(116 130)
(Loss)/profit for the year	–	–	–	–	(158 810)	(158 810)	14 736	(144 074)
Other comprehensive income	–	–	–	18 017	–	18 017	9 927	27 944
Share capital issued	1	–	–	–	–	1	–	1
Share-based payments (Note 25)	–	–	–	1 905	–	1 905	–	1 905
Dividends paid	–	–	–	–	(11 755)	(11 755)	(13 963)	(25 718)
Balance at 31 December 2016	1 384	885 648	(1)	(143 498)	(610 329)	133 204	70 623	203 827
Balance at 1 January 2015	1 383	885 648	(1)	(97 753)	(484 874)	304 403	61 014	365 417
Total comprehensive income/ (expense)	–	–	–	(67 611)	52 025	(15 586)	10 669	(4 917)
Profit for the year	–	–	–	–	52 025	52 025	25 647	77 672
Other comprehensive expense	–	–	–	(67 611)	–	(67 611)	(14 978)	(82 589)
Share-based payments (Note 25)	–	–	–	1 944	–	1 944	–	1 944
Dividends paid	–	–	–	–	(6 915)	(6 915)	(11 760)	(18 675)
Balance at 31 December 2015	1 383	885 648	(1)	(163 420)	(439 764)	283 846	59 923	343 769

¹ Refer to Note 16, Issued capital and reserves, for further detail.

² Being shares held by the Gem Diamonds Limited Employee Share Trust.

Consolidated Statement of Cash Flows

for the year ended 31 December 2016

	Notes	2016 US\$'000	2015 US\$'000
Cash flows from operating activities		70 675	119 103
Cash generated by operations	21.1	93 518	155 257
Working capital adjustments	21.2	446	(3 769)
		93 964	151 488
Interest received		1 253	1 762
Interest paid		(2 671)	(417)
Income tax paid		(21 871)	(33 730)
Cash flows used in investing activities		(98 988)	(109 605)
Purchase of property, plant and equipment		(10 624)	(22 892)
Ghaghoo development costs capitalised		(3 642)	(9 040)
Ghaghoo commissioning costs capitalised (net of revenue)		(14 374)	(16 630)
Waste cost capitalised		(70 378)	(61 416)
Proceeds from sale of property, plant and equipment		30	407
Cash used in disposal of subsidiary	21.3	-	(34)
Cash flows used in financing activities		(29 624)	(23 057)
Financial liabilities repaid		(3 906)	(4 384)
Dividends paid to holders of the parent		(11 755)	(6 913)
Dividends paid to non-controlling interests		(13 963)	(11 760)
Net decrease in cash and cash equivalents		(57 937)	(13 559)
Cash and cash equivalents at beginning of the year – continuing operations		85 719	110 704
Cash and cash equivalents at beginning of the year – discontinuing operation		-	34
Foreign exchange differences		3 005	(11 460)
Cash and cash equivalents at end of year held at banks		27 730	83 165
Restricted cash at end of year		3 057	2 554
Cash and cash equivalents at end of year	15	30 787	85 719

Notes to the Annual Financial Statements

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS

1.1 Corporate information

1.1.1 Incorporation

The holding company, Gem Diamonds Limited (the Company), was incorporated on 29 July 2005 in the British Virgin Islands (BVI). The Company's registration number is 669758.

These financial statements were authorised for issue by the Board on 14 March 2017.

The Group is principally engaged in the exploration and development of diamond mines.

1.1.2 Operational information

The Company has the following investments directly in subsidiaries at 31 December 2016:

Name of company	Share-holding	Cost of investment ¹	Country of incorporation	Nature of business
Subsidiaries				
Gem Diamond Technical Services (Proprietary) Limited ²	100%	US\$17	RSA	Technical, financial and management consulting services.
Gem Equity Group Limited ²	100%	US\$52 277	BVI	Dormant investment company holding 1% in Gem Diamonds Botswana (Proprietary) Limited, 2% in Gem Diamonds Marketing Services BVBA, 1% in Baobab Technologies BVBA and 0.1% in Gem Diamonds Marketing Botswana (Proprietary) Limited.
Letšeng Diamonds (Proprietary) Limited ²	70%	US\$126 000 303	Lesotho	Diamond mining and holder of mining rights.
Gem Diamonds Botswana (Proprietary) Limited ²	100%	US\$27 752 144	Botswana	Diamond mining; evaluation and development; and holder of mining licences and concessions.
BDI Mining Corp ²	100%	US\$82 064 783	BVI	Dormant investment company.
Gem Diamonds Australia Holdings ²	100%	US\$293 960 521	Australia	Dormant investment company.
Gem Diamonds Investments Limited ²	100%	US\$17 531 316	UK	Investment holding company holding 100% in each of Gem Diamonds Technology DMCC and Calibrated Diamonds Investment Holdings (Proprietary) Limited ³ ; 99.9% in Gem Diamonds Marketing Botswana (Proprietary) Limited; 99% in Baobab Technologies BVBA; and 98% in Gem Diamonds Marketing Services BVBA, a marketing company that sells the Group's diamonds on tender in Antwerp.

¹ The cost of investment represents original cost of investments at acquisition dates.

² No change in the shareholding since the prior year.

³ On 31 December 2016, the Group abandoned the CDIH group which was involved in the development and use of laser diamond shaping and cutting technology and machinery. As the operations are being closed and not sold the closure has been classified as an abandonment (refer to Note 4, Exceptional items).

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.1 Corporate information (continued)

1.1.3 Segment information

For management purposes, the Group is organised into geographical units as its risks and required rates of return are affected predominantly by differences in the geographical regions of the mines and areas in which the Group operates or areas in which operations are managed. The main geographical regions and the type of products and services from which each reporting segment derives its revenue from are:

- ▶ Lesotho (diamond mining activities);
- ▶ Botswana (diamond mining activities through Ghaghoo and sales and marketing of diamonds through Gem Diamonds Marketing Botswana (Proprietary) Limited);
- ▶ Belgium (sales, marketing and manufacturing of diamonds); and
- ▶ BVI, RSA and UK (technical and administrative services).

Management monitors the operating results of the geographical units separately for the purpose of making decisions about resource allocation and performance assessment.

Segment performance is evaluated based on operating profit or loss. Intersegment transactions are entered into under normal arm's-length terms in a manner similar to transactions with third parties. Segment revenue, segment expenses and segment results include transactions between segments. Those transactions are eliminated on consolidation.

Segment revenue is derived from mining activities, polished manufacturing margins, and Group services.

During the period, an immaterial operation, CDIH, operating out of South Africa and part of the Belgium segment, which developed and maintained laser diamond shaping and cutting technology and machinery, was abandoned due to its inability to generate profits during current market conditions and therefore its results have been excluded.

The following table presents revenue and profit, and asset and liability information from operations regarding the Group's geographical segments:

Year ended 31 December 2016	Lesotho US\$'000	Botswana US\$'000	Belgium US\$'000	BVI, RSA and UK US\$'000	Total US\$'000
Revenue					
Total revenue	184 864	–	194 387	9 719	388 970
Intersegment	(182 258)	–	(7 404)	(9 493)	(199 155)
External customers	2 606	–	186 983	226 ¹	189 815
Recycling of foreign currency translation reserve on abandonment of operation	–	–	3 546	–	3 546
Depreciation and amortisation	44 416	–	752	304	45 472
Depreciation and mining asset amortisation	9 704	–	752	304	10 760
Waste stripping cost amortisation	34 712	–	–	–	34 712
Share-based equity transactions	461	–	2	1 327	1 790
Impairment	–	170 778	2 154	–	172 932
Segment operating profit/(loss)	64 409	(169 685)	(6 529)	(12 094)	(123 899)
Net finance costs	702	7	–	(918)	(209)
Profit/(loss) before tax	65 111	(169 678)	(6 529)	(13 012)	(124 108)
Income tax expense					(19 966)
Loss for the year					(144 074)
Segment assets	309 469	6 001	6 185	23 095	344 750
Segment liabilities	39 677	33 164	609	1 797	75 247
Other segment information					
Capital expenditure					
– Property, plant and equipment ²	7 612	7 602	408	152	15 774
– Waste cost capitalised	70 378	–	–	–	70 378
– Operating and development costs capitalised	–	18 016	–	–	18 016
Total capital expenditure	77 990	25 618	408	152	104 168

¹ No revenue was generated in BVI.

² Capital expenditure includes non-cash movements in rehabilitation assets relating to changes in rehabilitation estimates for the Lesotho and Botswana segments and capitalisation of share-based payments for the Botswana segment.

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.1 Corporate information (continued)

1.1.3 Corporate information (continued)

Included in annual revenue for the current year is revenue from a single customer which amounted to US\$31.3 million arising from sales reported in the Lesotho and Belgium segment.

Segment liabilities do not include net deferred tax liabilities of US\$65.6 million.

Total sales for the current year are lower than that of the prior year mainly as a result of the lower frequency of exceptional large diamonds being recovered at the Lesotho segment, resulting in lower diamond prices achieved.

Year ended 31 December 2015	Lesotho US\$'000	Botswana US\$'000	Belgium US\$'000	BVI, RSA and UK US\$'000	Total conti- nuing opera- tions	Discon- tinued opera- tions	Total US\$'000
Revenue							
Total revenue	236 357	–	263 490	9 788	509 635	85	509 720
Intersegment	(235 183)	–	(15 696)	(9 281)	(260 160)	–	(260 160)
External customers	1 174	–	247 794	507 ¹	249 475	85	249 560
Depreciation and amortisation	56 497	–	615	362	57 474	117	57 591
Depreciation and mining asset amortisation	9 275	–	615	362	10 252	117	10 369
Waste stripping cost amortisation	47 222	–	–	–	47 222	–	47 222
Share-based equity transactions	489	–	–	1 249	1 738	–	1 738
Segment operating profit/(loss)	113 998	(1 864)	(1 281)	(2 416)	108 437	(1 002)	107 435
Net finance income					120	–	120
Profit/(loss) before tax					108 557	(1 002)	107 555
Income tax expense					(31 553)	–	(31 553)
Gain on disposal of subsidiary					–	1 670	1 670
Profit for the year					77 004	668	77 672
Segment assets	278 570	158 399	7 938	32 916	477 823	426	478 249
Segment liabilities	44 426	35 105	1 123	3 015	83 669	758	84 427
Other segment information							
Capital expenditure						–	–
– Property, plant and equipment ²	10 206	19 871	374	2 337	32 788	–	32 788
– Waste cost capitalised	61 416	–	–	–	61 416	–	61 416
– Operating and development expenses capitalised	–	14 260	–	–	14 260	–	14 260
Total capital expenditure	71 622	34 131	374	2 337	108 464	–	108 464

¹ No revenue was generated in BVI.

² Capital expenditure includes non-cash movements in rehabilitation assets relating to changes in rehabilitation estimates for the Lesotho and Botswana segments and capitalisation of share-based payments for the Botswana segment.

Included in annual revenue for the 2015 year was revenue from a single customer which amounted to US\$46.7 million arising from sales reported in the Lesotho and Belgium segment.

Segment liabilities do not include net deferred tax liabilities of US\$50.4 million.

Total sales for 2015 were lower than that of 2014 mainly as a result of market conditions and lower diamond prices achieved at the Lesotho segment, together with lower number of carats sold due to production cut-off periods.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies

1.2.1 Basis of presentation

The financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS). These financial statements have been prepared under the historical cost basis. The accounting policies have been consistently applied except for the adoption of the new standards and interpretations detailed below.

The functional currency of the Company and certain of its subsidiaries is US dollar, which is the currency of the primary economic environment in which the entities operate. All amounts are expressed in US dollar. The financial statements of subsidiaries whose functional and reporting currency is in currencies other than US dollar have been converted into US dollar on the basis as set out in Note 1.2.16, Foreign currency translations.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 1.2.26, Critical accounting estimates and judgements.

The Group has also adopted the following standards and interpretations from 1 January 2016:

Standards issued but not yet effective

Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning after 1 January 2017 or in later periods, which the Group has decided not to adopt early.

Standard, amendment or interpretation		Effective period commencing on or after
IFRS 16	<i>Leases</i>	1 January 2019
IFRS 2	<i>Classification and Measurement of Share-based Payment Transactions</i>	1 January 2018
IFRS 9	<i>Financial Instruments</i>	1 January 2018
IFRS 15	<i>Revenue from Contracts with Customer</i>	1 January 2018
IAS 7	<i>Disclosure Initiative</i>	1 January 2017
IAS 12	<i>Recognition of Deferred Tax Assets for Unrealised Losses</i>	1 January 2017

The Group is in the process of assessing the impact of these standards on the financial statements.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 will replace IAS 18 *Revenue* and IAS 11 *Construction Contracts* and establishes a unified framework for determining the timing, measurement and recognition of revenue. The principle of the new standard is to recognise revenue as performance obligations are met rather than based on the transfer of risks and rewards. The effective date of the standard is 1 January 2018.

The Group is currently reviewing the potential impact of IFRS 15 with the primary focus being understanding those sales contracts where the timing and amount of revenue recognised could differ under IFRS 15. As the Group's revenue is predominantly derived from rough diamond sales in which the transfer of risks and rewards coincides with the fulfilment of performance obligations, the timing and amount of revenue recognised is unlikely to be affected for these sales. It is currently anticipated that IFRS 15 will have an impact on the timing and amount of revenue recognised relating to uplift on partnership derived on the sale of polished diamonds. As these revenue streams have represented between 1.4% – 2.6% of total revenue generated in the past five years, it is not anticipated to have a significant impact on the results.

IFRS 15 also includes disclosure requirements including qualitative and quantitative information about contracts with customers to help users of the financial statements understand the nature, amount, timing and uncertainty of revenue. The Group will start developing a transition plan to identify and implement the required changes during 2017. The Group expects to adopt this standard retrospectively.

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.1 Basis of presentation (continued)

IFRS 16 Leases

Under the new standard, a lessee is in essence required to:

- ▶ recognise all right of use assets and lease liabilities, with the exception of short term (under 12 months) and low value leases, on the balance sheet. The liability is initially measured at the present value of future lease payments for the lease term. This includes variable lease payments that depend on an index or rate but excludes other variable lease payments. The right of use asset reflects the lease liability, initial direct costs, any lease payments made before the commencement date of the lease, less any lease incentives and, where applicable, provision for dismantling and restoration;
- ▶ recognise depreciation of right of use assets and interest on lease liabilities in the income statement over the lease term; and
- ▶ separate the total amount of cash paid into a principal portion (presented within financing activities) and interest portion (which the Group presents in operating activities) in the cash flow statement.

This standard will have an impact on the Group's earnings and it must be implemented retrospectively, either with the restatement of comparatives or with the cumulative impact of application recognised as at 1 January 2019 under the modified retrospective approach.

Under IFRS 16 the present value of the Group's operating lease commitments as defined under the new standard, excluding low value leases and short-term leases, will be shown as right of use assets and as lease liabilities on the balance sheet. Information on the undiscounted amount of the Group's operating lease commitments under IAS 17, the current leasing standard, is disclosed in Note 22. The Group is considering the available options for transition.

Over the next two years, the Group will focus on the identification of the provisions of the standard which will most impact the Group.

Business environment and country risk

The Group's operations are subject to country risk being the economic, political and social risks inherent in doing business in certain areas of Africa and Europe. These risks include matters arising out of the policies of the government, economic conditions, imposition of or changes to taxes and regulations, foreign exchange rate fluctuations and the enforceability of contract rights.

The consolidated financial information reflects management's assessment of the impact of these business environments on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

1.2.2 Going concern

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Review on pages 40 to 45 and pages 50 to 52. The financial position of the Company, its cash flows and liquidity position are described in the Strategic Review on pages 34 to 39. In addition, Note 24, Financial risk management, includes the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments; and its exposures to credit risk and liquidity risk.

After making enquiries which include reviews of forecasts and budgets, timing of cash flows, borrowing facilities and sensitivity analyses and considering the uncertainties described in this report either directly or by cross-reference, the Directors have a reasonable expectation that the Group and the Company have adequate financial resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going-concern basis in preparing the Annual Report and Accounts of the Company.

These financial statements have been prepared on a going-concern basis which assumes that the Group will be able to meet its liabilities as they fall due for the foreseeable future.

1.2.3 Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.3 Basis of consolidation (continued)

Subsidiaries

Subsidiaries are consolidated from the date of their acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. To meet the definition of control in IFRS 10, all three of the following criteria must be met:

- (a) an investor has power over an investee;
- (b) the investor has exposure, or rights, to variable returns from its involvement with the investee; and
- (c) the investor has the ability to use its power over the investee to affect the amount of the investor's returns.

The financial statements of subsidiaries used in the preparation of the consolidated financial statements are prepared for the same reporting year as the parent company and are based on consistent accounting policies. All intragroup balances and transactions, including unrealised profits arising from them, are eliminated in full.

Non-controlling interests

Non-controlling interests represent the equity in a subsidiary not attributable, directly or indirectly, to the parent company and is presented separately within equity in the consolidated statement of financial position, separately from equity attributable to owners of the parent. Losses within a subsidiary are attributed to the non-controlling interest even if that results in a deficit balance.

1.2.4 Exploration and evaluation expenditure

Exploration and evaluation activity involves the search for mineral resources, the determination of technical feasibility and the assessment of commercial viability of an identified resource. Exploration and evaluation activity includes:

- ▶ acquisition of rights to explore;
- ▶ researching and analysing historical exploration data;
- ▶ gathering exploration data through topographical, geochemical and geophysical studies;
- ▶ exploratory drilling, trenching and sampling;
- ▶ determining and examining the volume and grade of the resource;
- ▶ surveying transportation and infrastructure requirements; and
- ▶ conducting market and finance studies.

Administration costs that are not directly attributable to a specific exploration area are charged to the income statement. Licence costs paid in connection with a right to explore in an existing exploration area are capitalised and amortised over the term of the permit.

Exploration and evaluation expenditure is capitalised as incurred. Capitalised exploration expenditure is recorded as a component of property, plant and equipment at cost less accumulated impairment charges. As the asset is not available for use, it is not depreciated.

All capitalised exploration and evaluation expenditure is monitored for indications of impairment. Where a potential impairment is indicated, assessments are performed for each area of interest in conjunction with the group of operating assets (representing a cash-generating unit (CGU)) to which the exploration is attributed. To the extent that exploration expenditure is not expected to be recovered, it is charged to the income statement. Exploration areas where reserves have been discovered, but require major capital expenditure before production can begin, are continually evaluated to ensure that commercial quantities of reserves exist or to ensure that additional exploration work is under way as planned.

1.2.5 Development expenditure

When proved reserves are determined and development is sanctioned, capitalised exploration and evaluation expenditure is reclassified within property, plant and equipment to development expenditure. As the asset is not available for use, during the development phase, it is not depreciated. On completion of the development, any capitalised exploration and evaluation expenditure already capitalised to development asset, together with the subsequent development expenditure, is reclassified within property, plant and equipment to mining assets and depreciated on the basis as laid out in Note 1.2.6, Property, plant and equipment.

All development expenditure is monitored for indicators of impairment annually.

1. NOTES TO THE FINANCIAL STATEMENTS (continued)**1.2 Summary of significant accounting policies (continued)****1.2.6 Property, plant and equipment**

Property, plant and equipment are recorded at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributable to the acquisition and construction of the items, among others, professional fees, and for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policies.

Subsequent costs to replace a component of an item of property, plant and equipment that is accounted for separately, is capitalised when the cost of the item can be measured reliably, with the carrying amount of the original component being written off. All repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation commences when an asset is available for use. Depreciation is charged so as to write off the depreciable amount of the asset to its residual value over its estimated useful life, using a method that reflects the pattern in which the asset's future economic benefits are expected to be consumed by the Group.

Item	Method	Useful life
Mining assets	Straight line	Lesser of life of mine or period of lease
Decommissioning assets	Straight line	Lesser of life of mine or period of lease
Leasehold improvements	Straight line	Lesser of three years or period of lease
Plant and equipment	Straight line	Three to 10 years
Other assets	Straight line	Two to five years

Pre-production stripping costs

Costs associated with removal of waste overburden are classified as stripping costs.

The capitalisation of pre-production stripping costs as part of exploration and development assets ceases when the mine is commissioned and ready for production. Subsequent stripping activities that are undertaken during the production phase of a surface mine may create two benefits, being either the production of inventory or improved access to the ore to be mined in the future. Where the benefits are realised in the form of inventory produced in the period, the production stripping costs are accounted for as part of the cost of producing those inventories. Where production stripping costs are incurred and where the benefit is the creation of mining flexibility and improved access to ore to be mined in the future, the costs are recognised as a non-current asset, referred to as a 'stripping activity asset', if:

- future economic benefits (being improved access to the orebody) are probable;
- the component of the orebody for which access will be improved can be accurately identified; and
- the costs associated with the improved access can be reliably measured.

The stripping activity asset is separately disclosed in Note 9, Property, plant and equipment. If all the criteria are not met, the production stripping costs are charged to the income statement as operating costs. The stripping activity asset is initially measured at cost, which is the accumulation of costs directly incurred to perform the stripping activity that improves access to the identified component of ore, plus an allocation of directly attributable overhead costs. If incidental operations are occurring at the same time as the production stripping activity, but are not necessary for the production stripping activity to continue as planned, these costs are not included in the cost of the stripping activity asset. If the costs of the stripping activity asset and the inventory produced are not separately identifiable, a relevant production measure is used to allocate the production stripping costs between the inventory produced and the stripping activity asset. The stripping activity asset is subsequently amortised over the expected useful life of the identified component of the orebody that became more accessible as a result of the stripping activity. Based on proven and probable reserves, the expected average stripping ratio over the average life of the area being mined is used to amortise the stripping activity. As a result, the stripping activity asset is carried at cost less amortisation and any impairment losses.

The average life of area cost per tonne is calculated as the total expected costs to be incurred to mine the orebody divided by the number of tonnes expected to be mined. The average life of area stripping ratio and the average life of area cost per tonne are recalculated annually in light of additional knowledge and changes in estimates. Changes in the stripping ratio are accounted for prospectively as a change in estimate.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.7 Investment property

Investment property is initially recognised using the cost model. Subsequent recognition is at cost less accumulated depreciation, and less any accumulated impairment losses. Rental income from investment property is recognised on a straight-line basis over the term of the lease. Initial direct costs incurred in negotiating and arranging the lease are capitalised to investment property and depreciated over the lease term. Depreciation is calculated as follows:

Item	Method	Useful life
Investment property amount being zero	No depreciation is provided due to depreciable amount being zero	
Initial direct costs capitalised to investment property	Straight line	Five years

1.2.8 Business combinations, goodwill and other intangible assets

Business combinations and goodwill

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. The choice of measurement of non-controlling interest, either at fair value or at the proportionate share of the acquiree's identifiable net assets, is determined on a transaction-by-transaction basis. Acquisition costs incurred are expensed and included in administrative expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability will be recognised in accordance with IFRS 13 in the income statement. If the contingent consideration is classified as equity, it will not be remeasured until it is finally settled within equity.

Goodwill is initially measured at cost, being the excess of the aggregate of the acquisition date fair value of the consideration transferred and the amount recognised for the non-controlling interest (and where the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree) over the net identifiable amounts of the assets acquired and the liabilities assumed in exchange for the business combination. Assets acquired and liabilities assumed in transactions separate to the business combinations, such as the settlement of pre-existing relationships or post-acquisition remuneration arrangements are accounted for separately from the business combination in accordance with their nature and applicable IFRS. Identifiable intangible assets, meeting either the contractual legal or separability criterion are recognised separately from goodwill. Contingent liabilities representing a present obligation are recognised if the acquisition date fair value can be measured reliably.

If the aggregate of the acquisition date fair value of the consideration transferred and the amount recognised for the non-controlling interest (and where the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree) is lower than the fair value of the assets, liabilities and contingent liabilities, and the fair value of any pre-existing interest held in the business acquired, the difference is recognised in profit and loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's CGUs (or groups of CGUs) that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units. Each unit or group of units to which goodwill is allocated shall represent the lowest level within the entity at which the goodwill is monitored for internal management purposes, and shall not be larger than an operating segment before aggregation.

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

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.8 *Business combinations, goodwill and other intangible assets (continued)*

Concessions and licences

Concessions and licences are shown at cost. Concessions and licences have a finite useful life and are carried at cost less accumulated amortisation and accumulated impairment losses. Amortisation is calculated using the straight-line method to allocate the cost of concessions and licences over the shorter of the life of mine or term of the licence once production commences.

1.2.9 *Other financial assets*

Management determines the classification of its investments at initial recognition and re-evaluates this designation at every reporting date. Currently the Group only has financial assets at fair value through profit or loss, and loans and receivables.

When financial assets are recognised initially, they are measured at fair value plus (in the case of investments not at fair value through profit or loss) directly attributable costs.

Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss. Upon initial recognition, a financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorised as held for trading unless they are designated as hedges. Gains and losses on investments held for trading are recognised in profit or loss. Assets in this category are classified as current assets if they are either held for trading or are expected to be realised within 12 months of the reporting date.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except those with maturities greater than 12 months after the reporting date. These are classified as non-current assets. Such assets are carried at amortised cost using the effective interest rate method, less any allowance for impairment, if the time value of money is significant. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at an appropriate interest rate. The amount of the provision is recognised in the income statement.

1.2.10 *Financial liabilities*

Interest-bearing borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds (net of transaction costs) and the redemption value is recognised in the income statement, unless capitalised in accordance with Note 1.2.24, Finance costs, over the period of the borrowings, using the effective interest rate method.

Bank overdrafts are recognised at amortised cost.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.11 Fair value measurement

The Group measures financial instruments at fair value at each reporting date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- ▶ in the principal market for the asset or liability; or
- ▶ in the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible by the Group.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest-level input that is significant to the fair value measurement as a whole:

Level 1 – Quoted (unadjusted) market prices in active markets for identical assets or liabilities.

Level 2 – Valuation techniques for which the lowest-level input that is significant to the fair value measurement is directly or indirectly observable.

Level 3 – Valuation techniques for which the lowest-level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest-level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

1.2.12 Impairments

Non-financial assets

Assets that are subject to amortisation or depreciation are reviewed for impairment if it is determined that there is an indication of impairment in accordance with IAS 36. Goodwill is assessed for impairment on an annual basis. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Non-financial assets that were previously impaired are reviewed for possible reversal of the impairment at each reporting date.

A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such a reversal is recognised in the income statement. After such a reversal the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

1. NOTES TO THE FINANCIAL STATEMENTS (continued)**1.2 Summary of significant accounting policies (continued)****1.2.12 Impairments (continued)****Financial assets**

The Group assesses at each reporting date whether a financial asset or group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (ie the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through the use of an allowance account. The amount of the loss is recognised in the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date, any subsequent reversal of an impairment loss is recognised in the income statement.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Group will not be able to collect all of the amounts due under the original terms of the invoice. The carrying amount of the receivable is reduced through the use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible.

1.2.13 Inventories

Inventories, which include rough diamonds, ore stockpiles and consumables, are measured at the lower of cost and net realisable value. The amount of any write-down of inventories to net realisable value and all losses, is recognised in the period the write-down or loss occurs. Cost is determined as the average cost of production, using the weighted average method. Cost includes directly attributable mining overheads, but excludes borrowing costs.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs to be incurred in marketing, selling and distribution.

1.2.14 Cash and cash equivalents

Cash and cash equivalents are carried in the statement of financial position at amortised cost. Cash and cash equivalents comprise cash on hand, deposits held at call with banks, and other short-term, highly liquid investments with original maturities of three months or less.

For the purpose of the cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

1.2.15 Issued share capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction from the proceeds.

1.2.16 Foreign currency translations**Presentation currency**

The results and financial position of the Group's subsidiaries which have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- ▶ statement of financial position items are translated at the closing rate at the reporting date;
- ▶ income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- ▶ resulting exchange differences are recognised as a separate component of equity.

Details of the rates applied at the respective reporting dates and for the income statement transactions are detailed in Note 16, Issued capital and reserves.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.16 Foreign currency translations (continued)

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains or losses resulting from the settlement of such transactions and from the translation at the period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Non-monetary items that are measured in terms of cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Monetary items for each statement of financial position presented are translated at the closing rate at the reporting date.

1.2.17 Share-based payments

Employees (including Senior Executives) of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments (equity-settled transactions). In situations where some or all of the goods or services received by the entity as consideration for equity instruments cannot be specifically identified, they are measured as the difference between the fair value of the share-based payment and the fair value of any identifiable goods or services received at the grant date. For cash-settled transactions, the liability is remeasured at each reporting date until settlement, with the changes in fair value recognised in the income statement.

Equity-settled transactions

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted, and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined using an appropriate pricing model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions).

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

At each reporting date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions and of the number of equity instruments that will ultimately vest or, in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous reporting date is recognised in the income statement, with a corresponding entry in equity.

Where the terms of an equity-settled award are modified or a new award is designated as replacing a cancelled or settled award, the cost based on the original award terms continues to be recognised over the original vesting period. In addition, an expense is recognised over the remainder of the new vesting period for the incremental fair value of any modification, based on the difference between the fair value of the original award and the fair value of the modified award, both as measured on the date of the modification. No reduction is recognised if this difference is negative.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any cost not yet recognised in the income statement for the award is expensed immediately.

Where an equity-settled award is forfeited, it is treated as if vesting conditions had not been met and all costs previously recognised in the income statement for the award are reversed and recognised in income immediately.

Management applies judgement when determining whether share options relating to employees who resigned before the end of the service condition period are cancelled or forfeited as referred under policy 1.2.26, Critical accounting estimates and judgements.

1.2.18 Provisions

Provisions are recognised when:

- ▶ the Group has a present legal or constructive obligation as a result of a past event; and
- ▶ a reliable estimate can be made of the obligation.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation, using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as a finance cost.

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.19 Restoration and rehabilitation

The mining, extraction and processing activities of the Group normally give rise to obligations for site restoration and rehabilitation. Rehabilitation works can include facility decommissioning and dismantling, removal and treatment of waste materials, land rehabilitation, and site restoration. The extent of the work required and the estimated cost of final rehabilitation, comprising liabilities for decommissioning and restoration, are based on current legal requirements, existing technology and the Group's environmental policies, and is reassessed annually. Cost estimates are not reduced by the potential proceeds from the sale of property, plant and equipment.

Provisions for the cost of each restoration and rehabilitation programme are recognised at the time the environmental disturbance occurs. When the extent of the disturbance increases over the life of the operation, the provision and associated asset is increased accordingly. Costs included in the provision encompass all restoration and rehabilitation activity expected to occur. The restoration and rehabilitation provisions are measured at the expected value of future cash flows, discounted to their present value. Discount rates used are specific to the country in which the operation is located. The value of the provision is progressively increased over time as the effect of the discounting unwinds, which is recognised in finance charges. Restoration and rehabilitation provisions are also adjusted for changes in estimates.

When provisions for restoration and rehabilitation are initially recognised, the corresponding cost is capitalised as an asset where it gives rise to a future benefit and depreciated over future production from the operation to which it relates.

1.2.20 Taxation

Income tax for the period comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items charged or credited directly to equity, in which case it is recognised in equity. Current tax expense is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the statement of financial position liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled based on the tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

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

In respect of taxable temporary differences associated with investments in subsidiaries, associates and jointly controlled entities, deferred tax is provided except where the timing of the reversal of the temporary differences can be controlled by the Group and it is probable that the temporary differences will not reverse in the foreseeable future.

In respect of deductible temporary differences associated with investments in subsidiaries, associates and jointly controlled entities, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

Withholding tax is recognised in the income statement when dividends or other services which give rise to that withholding tax are declared or accrued respectively. Withholding tax is disclosed as part of current tax.

Royalties

Royalties incurred by the Group comprise mineral extraction costs based on a percentage of sales paid to the local revenue authorities. These obligations arising from royalty arrangements are recognised as current payables and disclosed as part of royalty and selling costs in the income statement.

Royalties and revenue-based taxes are accounted for under IAS 12 when they have the characteristics of an income tax. This is considered to be the case when they are imposed under government authority and the amount payable is based on taxable income – rather than based on quantity produced or as a percentage of revenue. For such arrangements, current and deferred tax is provided on the same basis as described above for other forms of taxation. The royalties incurred by the Group are considered not to meet the criteria to be treated as part of income tax.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.21 Employee benefits

Provision is made in the financial statements for all short-term employee benefits. Liabilities for wages and salaries, including non-monetary benefits, benefits required by legislation, annual leave, retirement benefits and accumulating sick leave obliged to be settled within 12 months of the reporting date, are recognised in trade and other payables and are measured at the amounts expected to be paid when the liabilities are settled. Benefits falling due more than 12 months after the reporting date are discounted to present value. The Group recognises an expense for contributions to the defined contribution pension fund in the period in which the employees render the related service.

Bonus plans

The Group recognises a liability and an expense for bonuses. The Group recognises a liability where contractually obliged or where there is a past practice that has created a constructive obligation. These liabilities are recognised in trade and other payables and are measured at the amounts expected to be paid when the liabilities are settled.

1.2.22 Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset. A reassessment is made after inception of the lease only if one of the following applies:

- (a) there is a change in contractual terms, other than a renewal or extension of the arrangement;
- (b) a renewal option is exercised or extension granted, unless the term of the renewal or extension was initially included in the lease term;
- (c) there is a change in the determination of whether fulfilment is dependent on a specific asset; or
- (d) there is a substantial change to the asset.

Where a reassessment is made, lease accounting shall commence or cease from the date when the change in circumstances gave rise to the reassessment for scenarios (a), (c) or (d) and at the date of renewal or extension period for scenario (b).

Group as a lessee

Leases of property, plant and equipment where the Group has, substantially, all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding lease obligations, net of finance charges, are included in financial liabilities.

The interest element of the finance cost is charged to the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each year. The property, plant and equipment acquired under finance leases are depreciated over the shorter of the asset's useful life and the lease term.

Leases where the lessor retains substantially all the risks and rewards of ownership are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease. When the Group is a party to a lease where there is a contingent rental element associated within the agreement, a cost is recognised as and when the contingency materialises.

Group as a lessor

Assets leased out under operating leases are included in investment property. Rental income is recognised on a straight-line basis over the lease term. Refer to Note 1.2.7, Investment property, for further information on the treatment of investment property.

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.23 Revenue

Revenue is measured at fair value of the consideration received or receivable and comprises the fair value for the sale of goods, net of value added tax, rebates and discounts and after eliminated sales within the Group. Revenue is recognised as follows:

Sale of goods

Revenue is recognised when the significant risks and rewards of ownership have been transferred to the customer and can be measured reliably and receipt of future economic benefits is probable.

The following revenue streams are recognised:

- ▶ rough diamonds which are made through competitive tender processes, partnership agreements and joint operation arrangements;
- ▶ polished diamonds and other products which are made through direct sale transactions;
- ▶ additional uplift on partnership arrangements; and
- ▶ additional uplift on joint operation arrangements.

Revenue through joint operation arrangements is recognised for the sale of the rough diamond according to the percentage interest in the joint operation arrangement, as only that percentage of significant risks and rewards pass at the time of sale. Contractual agreements are entered into between the Group and the joint operation partner (partner) whereby both parties control jointly the cutting and polishing activities relating to the diamond. All decisions pertaining to the cutting and polishing of the diamonds require unanimous consent from both parties. Once these activities are complete, the polished diamond is sold, after which the revenue on the remaining percentage of the rough diamond is recognised, together with additional uplift on the joint operation arrangement. For more detail on how these arrangements have been included in the financial statements refer to Note 2, Revenue. The Group portion of inventories related to these transactions is included in the total inventories balance refer to Note 14, Inventories.

Revenue through partnership arrangements is recognised for the sale of the rough diamond, with an additional uplift based on the polished margin achieved. Management recognises the revenue on the sale of the rough diamond when it is sold to a third party, as there is no continuing involvement by management in the cutting and polishing process and the significant risks and rewards have passed to the third party. For additional uplift on partnership arrangements, certain estimates and judgements are made by management as referred to under policy 1.2.26, Critical accounting estimates and judgements.

Rendering of service

Revenue from services relating to third-party diamond manufacturing is recognised in the accounting period in which the services are rendered, and it is probable that the economic benefits associated with the transaction will flow to the entity, by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Interest income

Interest income is recognised on a time-proportion basis using the effective interest rate method.

Dividends

Dividends are recognised when the amount of the dividend can be reliably measured and the Group's right to receive payment is established.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.24 Finance costs

Finance costs are generally expensed as incurred, except where they relate to the financing of construction or development of qualifying assets requiring a substantial period of time to prepare for their intended future use. Finance costs are capitalised up to the date when the asset is ready for its intended use.

1.2.25 Dividend distribution

Dividend distributions to the Group's shareholders are recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Group's shareholders.

1.2.26 Critical accounting estimates and judgements

The preparation of the consolidated financial statements requires management to make estimates and judgements and form assumptions that affect the reported amounts of the assets and liabilities, the reported revenue and costs during the periods presented therein, and the disclosure of contingent liabilities at the date of the financial statements. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future and the resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the financial results or the financial position reported in future periods are discussed below.

Estimates

Life of mine (LoM)

There are numerous uncertainties inherent in estimating ore reserves and the associated LoM. Therefore the Group must make a number of assumptions in making those estimations, including assumptions as to the prices of commodities, exchange rates, production costs and recovery rates. Assumptions that are valid at the time of estimation may change significantly when new information becomes available. Changes in the forecast prices of commodities, exchange rates, production costs or recovery rates may change the economic status of ore reserves and may, ultimately, result in the ore reserves being restated. Where assumptions change the LoM estimates, the associated depreciation rates, residual values, waste stripping and amortisation ratios, and environmental provisions are reassessed to take into account the revised LoM estimate. Refer to Note 9, Property, plant and equipment.

Exploration and evaluation expenditure

This policy requires management to make certain estimates and assumptions as to future events and circumstances, in particular whether economically viable extraction operations are viable where reserves have been discovered and whether indications of impairment exist. Any such estimates and assumptions may change as new information becomes available. Refer to Note 9, Property, plant and equipment.

Provision for restoration and rehabilitation

Significant estimates and assumptions are made in determining the amount of the restoration and rehabilitation provisions. These deal with uncertainties such as changes to the legal and regulatory framework, magnitude of possible contamination, and the timing, extent and costs of required restoration and rehabilitation activity. Refer to Note 19, Provisions, for further detail.

Judgements

Development expenditure

Judgement is applied by management in determining when a project has reached a stage at which economically recoverable reserves exist and that development may be sanctioned. Management is required to make certain estimates and assumptions similar to those described above for capitalised exploration and evaluation expenditure. Refer to Note 9, Property, plant and equipment.

Revenue – partnership arrangements

Management has entered into partnership arrangements to increase the revenue earned on the sale of rough diamonds. Under these arrangements, revenue is earned for the sale of the rough diamond, with an additional uplift based on the polished margin achieved. Management recognises the revenue on the sale of the rough diamond at the point at which it is sold to the third party, as there is no continuing involvement by management in the cutting and polishing process and the significant risks and rewards have passed to the third party. Judgement is applied by management in determining when additional uplift is recognised and measured with regard to rough diamonds sold into partnership arrangements. Management is required to make certain estimates and assumptions based on when the uplift can be reliably measured. This occurs when the third party sells these goods, at which point the value of the final polished goods are determined.

1. NOTES TO THE FINANCIAL STATEMENTS (continued)**1.2 Summary of significant accounting policies (continued)****1.2.26 Critical accounting estimates and judgements (continued)*****Impairment reviews***

The Group determines if goodwill is impaired at least on an annual basis, while all other significant operations are tested for impairment when there are potential indicators which may require impairment review. This requires an estimation of the recoverable amount of the relevant cash-generating unit under review. Recoverable amount is the higher of fair value less costs to sell and value in use.

While conducting an impairment review of its assets using value-in-use impairment models, the Group exercises judgement in making assumptions about future rough diamond prices, exchange rates, volumes of production, ore reserves and resources included in the current LoM plans, production costs and macro-economic factors such as inflation and discount rates. Changes in estimates used can result in significant changes to the consolidated income statement and consolidated statement of financial position.

The results of the impairment testing performed indicated an impairment on the Ghaghoo mining operation as disclosed in Note 12, Impairment testing.

The key assumptions used in the recoverable amount calculations, determined on a value-in-use basis, are listed in the table below:

Valuation basis

Discounted present value of future cash flows.

LoM and recoverable value of reserves and resources

Economically recoverable reserves and resources, carats recoverable and grades achievable are based on management's expectations of the availability of reserves and resources at mine sites and technical studies undertaken by in-house and third-party specialists. Reserves remaining after the current LoM plans and current lease periods have not been included in determining the value in use of the operations.

Capital expenditure

Management has estimated the timing and quantum of the capital expenditure based on the Group's current LoM plans for each operation.

Diamond prices

The diamond prices used in the impairment test have been set with reference to recent prices achieved, the Group's medium-term forecast and market trends. Long-term diamond price escalation reflects the Group's assessment of market supply/demand fundamentals.

Discount rate

The discount rate of 12.6% (2015: 12.0%) used for Letšeng and 12.0% (2015: 13.1%) for Ghaghoo, in both instances represents the before-tax risk-free rate adjusted for market risk, volatility and risks specific to the asset and its operating jurisdiction.

Cost and inflation rate

These costs for Letšeng are determined on management's experience and the use of contractors over a period of time whose costs are fairly reasonably determinable. Mining costs have been based on the negotiated eight-year mining contract, which came into effect from 1 January 2014. Costs of extracting and processing which are reasonably determinable are based on management's experience. Long-term inflation rates of 4% to 6% above the long-term US dollar inflation rate were used for operating costs and capital cost escalators.

Exchange rates

Exchange rates are estimated based on an assessment at current market fundamentals and long-term expectations. The US\$/Lesotho Loti (LSL) and US\$/Botswana Pula (BWP) exchange rate used was determined with reference to the closing rate at 31 December 2016 of LSL13.68 and BWP10.68, respectively.

Sensitivity

The value in use for Letšeng indicated sufficient headroom, and no reasonable change in the key assumptions will result in an impairment.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.26 Critical accounting estimates and judgements (continued)

Market capitalisation

The Group has made a judgement in determining if, in the instance where the Group's asset carrying values exceed market capitalisation, this results in an indicator of impairment. All significant operations were assessed for impairment during the year and impairments were recognised where relevant.

Refer to Note 12, Impairment testing, for further detail.

Capitalised stripping costs (deferred waste)

Waste removal costs (stripping costs) are incurred during the development and production phases at surface mining operations. Furthermore, during the production phase, stripping costs are incurred in the production of inventory as well as in the creation of future benefits by improving access and mining flexibility in respect of the ore to be mined, the latter being referred to as a 'stripping activity asset'. Judgement is required to distinguish between these two activities at Letšeng. The orebody needs to be identified in its various separately identifiable components. An identifiable component is a specific volume of the orebody that is made more accessible by the stripping activity. Judgement is required to identify and define these components (referred to as 'cuts'), and also to determine the expected volumes (tonnes) of waste to be stripped and ore to be mined in each of these components. These assessments are based on a combination of information available in the mine plans, specific characteristics of the orebody and the milestones relating to major capital investment decisions.

Judgement is also required to identify a suitable production measure that can be applied in the calculation and allocation of production stripping costs between inventory and the stripping activity asset. The ratio of expected volume (tonnes) of waste to be stripped for an expected volume (tonnes) of ore to be mined for a specific component of the orebody, compared to the current period ratio of actual volume (tonnes) of waste to the volume (tonnes) of ore is considered to determine the most suitable production measure.

These judgements and estimates are used to calculate and allocate the production stripping costs to inventory and/or the stripping activity asset(s). Furthermore, judgements and estimates are also used to apply the stripping ratio calculation in determining the amortisation of the stripping activity asset. Refer to Note 9, Property, plant and equipment, for further detail.

Stripping ratio

Estimated recoverable reserves are used in determining the amortisation of mine-specific assets. Amortisation is calculated by using the expected average stripping ratio over the average life of the area being mined. The average stripping ratio is calculated as the number of tonnes of waste material expected to be removed during the life of area, per tonne of ore mined. The average life of area cost per tonne is calculated as the total expected costs to be incurred to mine the orebody divided by the number of tonnes expected to be mined. The average life of area stripping ratio and the average life of area cost per tonne are recalculated annually in light of additional knowledge and changes in estimates. Changes in the stripping ratio are accounted for prospectively as a change in estimate. Refer to Note 9, Property, plant and equipment, for further detail.

Production start date

The phase of each mine construction project is assessed to determine when a mine moves into the production phase. The criteria used to assess the start date are determined by the unique nature of each mine's construction project and include factors such as the complexity of a plant and its location. Various relevant criteria are considered to assess when the mine is substantially complete and ready for its intended use and moves into the production phase. At this point, all related amounts are reclassified from 'exploration and development assets' to 'mining assets', 'stripping activity asset' and/or 'property, plant and equipment'. Some of the criteria would include but are not limited to the following:

- ▶ the level of capital expenditure compared to the construction costs estimates;
- ▶ completion of a reasonable period of testing of the mine plant and equipment;
- ▶ ability to produce inventory in saleable form; and
- ▶ ability to sustain ongoing production of inventory.

Refer to Note 9, Property, plant and equipment, for further detail.

1. NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Summary of significant accounting policies (continued)

1.2.26 Critical accounting estimates and judgements (continued)

Production start date (continued)

When a mine construction project moves into the production phase, the capitalisation of certain mine construction costs ceases and costs are either regarded as inventory or expensed, except for capitalisable costs related to mining asset additions or improvements, production phase stripping costs capitalisable as stripping activity asset(s), and exploration expenditure that meets the criteria for capitalisation. It is also at this point that depreciation/ amortisation commences.

Management made the key judgement that the Ghaghoo mine had not reached production start date during the year based on the following:

- ▶ Continued operational and technical challenges as a result of difficult ground conditions resulted in Ghaghoo not achieving its planned ramp-up profile and production targets.
- ▶ Inconsistent plant throughput rates impacting ability to sustain ongoing production of inventory.

As a result, the mine was not in the condition necessary for it to be capable of operating in the manner intended by management on a sustainable basis and therefore the mine remained in its construction phase with all costs incurred during the year being capitalised to the exploration and development asset. Subsequent to period end, the Ghaghoo mine was placed on care and maintenance and all costs previously capitalised to the exploration and development asset were impaired in full as disclosed in Note 9, Property, plant and equipment.

Share-based payments

Judgement is applied by management in determining whether the share options relating to employees who resigned before the end of the service condition period have been cancelled or forfeited in light of their leaving status. Where employees do not meet the requirements of a good leaver as per the rules of the long-term incentive plan (LTIP), no award will vest and this will be treated as cancellation by forfeiture. The expenses relating to these charges previously recognised are then reversed. Where employees do meet the requirements of a good leaver as per the rules of the LTIP, some or all of an award will vest and this will be treated as a modification to the original award. The future expenses relating to these awards are accelerated and recognised as an expense immediately. Refer to Note 25, Share-based payments, for further detail.

1.2.27 Exceptional items

The Group presents as exceptional items on the face of the income statement, those material items of income and expenses which, because of the nature and expected infrequency of the events giving rise to them, merit separate presentation to allow shareholders to understand better the elements of financial performance in the year, so as to facilitate comparison with prior periods and to assess better trends in financial performance. Refer to Note 4, Exceptional items, for further detail.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

2. REVENUE

	2016 US\$'000	2015 US\$'000
Sale of goods	189 355	248 969
Rendering of services	460	506
	189 815	249 475

Included in revenue are sales of diamonds which are sold through joint operation arrangements totalling US\$0.2 million (2015: US\$2.4 million).

Finance income is reflected in Note 5, Net finance (costs)/income.

3. OPERATING PROFIT/(LOSS) BEFORE EXCEPTIONAL ITEMS

Operating profit includes the following:

Other operating income

Profit on disposal of property, plant and equipment	16	251
Depreciation and amortisation		
Depreciation and mining asset amortisation – continuing operations	(14 899)	(13 057)
Depreciation – discontinued operation	–	(117)
Waste stripping costs amortised	(34 712)	(47 222)
	(49 611)	(60 396)
<i>Less:</i> Depreciation capitalised to development asset	4 545	2 738
<i>(Add)/less:</i> Depreciation and mining asset amortisation capitalised to inventory	(249)	224
	(45 315)	(57 434)
Amortisation of intangible assets	(157)	(157)
	(45 472)	(57 591)

Inventories

Cost of inventories recognised as an expense	(98 896)	(111 969)
Write-down of inventory to net realisable value	(466)	–
	(99 362)	(111 969)

Foreign exchange gain

Foreign exchange gain	1 715	7 314
Mark-to-market revaluations on forward exchange contracts	–	1 155
	1 715	8 469

Operating lease expenses as a lessee

Mine site property	(126)	(112)
Equipment and service leases	(54 279)	(51 147)
Contingent rental – Alluvial Ventures	(10 716)	(11 360)
Leased premises	(2 197)	(2 509)
	(67 318)	(65 128)

Auditor's remuneration – EY

Group financial statements	(441)	(555)
Statutory	(146)	(154)
	(587)	(709)

Auditor's remuneration – other

Statutory	(20)	(34)
	(20)	(34)

3. OPERATING PROFIT/(LOSS) BEFORE EXCEPTIONAL ITEMS (continued)

	2016 US\$'000	2015 US\$'000
Other non-audit fees – EY		
Tax services advisory and consultancy	(63)	(32)
Tax compliance services	(18)	(17)
Other services	(10)	(17)
Other assurance services ¹	(149)	(155)
	(240)	(221)
Other non-audit fees – other		
Internal audit	(1)	(29)
Tax services advisory and consultancy	(6)	(16)
	(7)	(45)
Employee benefits expense		
Salaries and wages ²	(16 673)	(21 784)
Underlying earnings before interest, tax, depreciation and mining asset amortisation (underlying EBITDA) before exceptional items		
Underlying EBITDA is shown, as the Directors consider this measure to be a relevant guide to the operational performance of the Group and excludes such non-operating costs as listed below. The reconciliation from operating profit to underlying EBITDA is as follows:		
Operating profit	52 579	98 839
Other operating income	(306)	(458)
Foreign exchange gain	(1 715)	(6 997)
Share-based payments	1 790	1 738
Depreciation and mining asset amortisation (excluding waste stripping cost amortised)	10 469	10 424
Underlying EBITDA before exceptional items	62 817	103 546
4. EXCEPTIONAL ITEMS		
Other operating income ³	–	8 126
Foreign exchange gain ³	–	1 472
Impairment of assets ⁴	(172 932)	–
Recycling of foreign currency translation reserve on abandonment of operation ⁴	(3 546)	–
	(176 478)	9 598

¹ Other assurance services by EY relate to the interim review on the half-year results for the six months ended 30 June.

² Includes contributions to defined contribution plan of US\$0.6 million (31 December 2015: US\$0.6 million).

³ The prior year exceptional items relate to the settlement of an interest-bearing tax liability for an amount less than that previously provided for which resulted in the reversal of accrued expenses of US\$8.1 million. In addition, the interest-bearing tax liability was payable in Australian dollar, resulting in a foreign exchange gain of US\$1.5 million.

⁴ Relates to the impairment of the abandoned operation resulting in an impairment charge of US\$2.2 million and recycling of foreign currency translation reserve of US\$3.5 million. In addition, the impairment of the carrying value of the Ghaghoo asset was US\$170.8 million. Refer to Note 12, Impairment testing, for further information.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

5. NET FINANCE (COSTS)/INCOME

	2016 US\$'000	2015 US\$'000
Finance income		
Bank deposits	1 232	1 098
Other	1 179	407
Total finance income	2 411	1 505
Finance costs		
Bank overdraft	(815)	(82)
Finance costs on borrowings	(1 064)	(335)
Finance costs on unwinding of rehabilitation provision	(741)	(968)
Total finance costs	(2 620)	(1 385)
	(209)	120
6. INCOME TAX		
Income tax expense		
Income statement		
Current		
– Overseas	(7 138)	(22 209)
Withholding tax		
– Overseas	(3 379)	(2 858)
Deferred		
– Overseas	(9 449)	(6 486)
	(19 966)	(31 553)
(Loss)/profit before taxation	(124 108)	108 557
	%	%
Reconciliation of tax rate		
Applicable income tax rate	20.0	20.3
Permanent differences	(27.0)	(1.9)
Unrecognised deferred tax assets	(6.9)	3.6
Effect of overseas tax at different rates	0.5	4.5
Withholding tax	(2.7)	2.6
Effective income tax rate	(16.1)	29.1

Included in permanent differences is the impairment of the abandoned operation and the impairment of the carrying value of the Ghaghoo asset. For more information, refer to Note 4, Exceptional items. During the year, the effective statutory UK Corporate Tax Rate changed to 20.0% (2015: 20.3%).

7. DISPOSAL OF SUBSIDIARY

There are no disposals of subsidiaries or discontinued operations for the current year.

During the prior year, the Group sold its small manufacturing business facility in Mauritius, through Gem Diamonds Technology Mauritius (Proprietary) Limited. The sale was finalised for the agreed purchase price of US\$0.4 million, to be paid in quarterly instalments of a minimum of US\$50 000 which was due to commence in January 2016. Based on current market conditions, the consideration has not been received to date and therefore a provision for bad debt of the full purchase price of US\$0.4 million has been raised. Refer to Note 13, Receivables and other assets.

The results of the Mauritius operation for the year ended 31 December 2015 is as follows:

	31 December 2015 US\$'000
Revenue	85
Cost of sales and other operating costs	(443)
Gross loss	(358)
Foreign exchange loss	(644)
Operating loss	(1 002)
Gain on disposal of subsidiary	1 670
Profit before tax from discontinued operation	668
Income tax expense	–
Profit after tax from discontinued operation	668
Earnings per share from discontinued operation (cents)	
Basic	0.48
Diluted	0.48
The net cash flows attributable to the discontinued operation are as follows:	
Operating	(293)
Investing	444
Financing	(151)
Foreign exchange loss on translation of cash balance	(4)
Net cash outflow	(4)
The net assets disposed of are as follows:	
Assets	
Property, plant and equipment	269
Inventories	4
Trade and other receivables	119
Cash and cash equivalents	34
Liabilities	
Trade and other payables	(732)
Provisions	(26)
Net identifiable assets disposed of	(332)
Recycling of foreign currency translation reserve	(988)
Consideration not received ¹	(350)
Gain on disposal of subsidiary	(1 670)

¹ Consideration was not received and a provision for bad debt has been raised during 2016.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

8. EARNINGS PER SHARE

The following reflects the income and share data used in the basic and diluted earnings per share computations:

	2016 US\$'000	2015 US\$'000
(Loss)/profit for the year from continuing operations after exceptional items	(144 074)	77 004
Profit for the year from discontinued operation	–	668
Less: Non-controlling interests	(14 736)	(25 647)
Net profit attributable to equity holders of the parent for basic and diluted earnings	(158 810)	52 025
The weighted average number of shares takes into account the treasury shares at year end.		
Weighted average number of ordinary shares outstanding during the year ('000)	138 266	138 227

Earnings per share is calculated by dividing the net profit attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share is calculated by dividing the net profit attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year after taking into account future potential conversion and issue rights associated with the ordinary shares.

	2016 Number of shares	2015 Number of shares
Weighted average number of ordinary shares outstanding during the year	138 266	138 227
Effect of dilution:		
– Future share awards under the Employee Share Option Plan	1 729	1 476
Weighted average number of ordinary shares outstanding during the year adjusted for the effect of dilution	139 995	139 703

There have been no other transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of completion of these financial statements.

9. PROPERTY, PLANT AND EQUIPMENT

As at 31 December 2016	Exploration and development assets ¹							Total US\$'000
	Stripping activity asset US\$'000	Mining asset US\$'000	Exploration and development assets ¹ US\$'000	Decommissioning assets US\$'000	Leasehold improvement US\$'000	Plant and equipment US\$'000	Other assets ² US\$'000	
Cost								
Balance at 1 January 2016	232 779	111 879	129 493	3 941	28 205	61 743	19 401	587 441
Additions	70 378	–	23 611	–	261	7 623	2 295	104 168
Net movement in rehabilitation provision	–	–	511	1 403	–	–	–	1 914
Disposals	–	–	–	–	–	–	(567)	(567)
Reclassifications	–	1 458	(12 721)	–	3 415	7 534	314	–
Foreign exchange differences	36 247	5 809	7 140	665	3 523	9 249	1 690	64 323
Balance at 31 December 2016	339 404	119 146	148 034	6 009	35 404	86 149	23 133	757 279
Accumulated depreciation/amortisation								
Balance at 1 January 2016	144 495	44 624	–	3 017	8 815	37 942	9 181	248 074
Charge for the year	34 712	1 786	–	111	3 622	5 617	3 763	49 611
Disposals	–	–	–	–	–	–	(548)	(548)
Reclassifications	–	809	–	–	(28)	(2)	(779)	–
Impairment	–	–	147 251	–	5 790	13 100	6 340	172 481
Foreign exchange differences	20 182	870	783	445	1 415	5 860	907	30 462
Balance at 31 December 2016	199 389	48 089	148 034	3 573	19 614	62 517	18 864	500 080
Net book value at 31 December 2016	140 015	71 057	–	2 436	15 790	23 632	4 269	257 199

¹ Borrowing costs of US\$1.6 million (31 December 2015: US\$1.6 million) incurred in respect of the US\$25.0 million facility at Ghaghoo (refer to Note 17, Interest-bearing loans and borrowings) were capitalised to the development asset. The weighted average capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation was 6.5%.

² Other assets comprise motor vehicles, computer equipment, furniture and fittings, and office equipment.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

9. PROPERTY, PLANT AND EQUIPMENT (continued)

As at	Stripping activity asset	Mining asset	Exploration and develop- ment assets ¹	Decommis- sioning assets	Leasehold improve- ment	Plant and equip- ment ²	Other assets ³	Total
31 December 2015	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000
Cost								
Balance at								
1 January 2015	243 952	125 361	124 081	8 408	22 348	88 554	14 579	627 283
Additions	61 416	–	27 402	–	390	13 183	8 824	111 215
Net movement in rehabilitation provision	–	–	–	(2 751)	–	–	–	(2 751)
Disposals	–	–	–	–	(96)	(1 450)	(209)	(1 755)
Reclassifications	–	2 126	–	–	13 115	(15 408)	167	–
Foreign exchange differences	(72 589)	(15 608)	(21 990)	(1 716)	(7 552)	(23 136)	(3 960)	(146 551)
Balance at 31 December 2015	232 779	111 879	129 493	3 941	28 205	61 743	19 401	587 441
Accumulated depreciation/ amortisation								
Balance at								
1 January 2015	138 079	44 434	–	3 646	9 944	48 135	8 118	252 356
Charge for the year	47 222	2 098	–	439	1 945	5 355	3 337	60 396
Disposals	–	–	–	–	(96)	(842)	(157)	(1 095)
Foreign exchange differences	(40 806)	(1 908)	–	(1 068)	(2 978)	(14 706)	(2 117)	(63 583)
Balance at 31 December 2015	144 495	44 624	–	3 017	8 815	37 942	9 181	248 074
Net book value at 31 December 2015	88 284	67 255	129 493	924	19 390	23 801	10 220	339 367

¹ Borrowing costs of US\$1.6 million (31 December 2014: US\$0.6 million) incurred in respect of the US\$25.0 million facility at Ghaghoo development (refer to Note 17, Interest-bearing loans and borrowings) were capitalised to the development asset. The weighted average capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation was 6.5%.

² During 2015 the Coarse Recovery Plant was completed and reclassified out of plant and equipment, into leasehold improvements. Borrowing costs of US\$0.9 million incurred in respect of the associated LSL140.0 million bank loan facility were capitalised (refer to Note 17, Interest-bearing loans and borrowings). The weighted average capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation was 11.35%.

³ Other assets comprise motor vehicles, computer equipment, furniture and fittings, and office equipment.

10. INVESTMENT PROPERTY

The investment property consists of a commercial unit located in the Almas Towers in Dubai. The unit is being let out in terms of a rental agreement entered into for a further two-year period commencing 1 October 2016.

	2016 US\$'000	2015 US\$'000
Cost		
Balance at 1 January	617	617
Balance at 31 December	617	617
Accumulated depreciation		
Balance at 1 January	2	2
Depreciation	–	–
Balance at 31 December	2	2
Net book value at 31 December	615	615
Fair value¹	923	1 011
Amounts recognised in profit or loss		
Rental income	60	59
Direct operating expenses	(20)	(16)
The future minimum rental income under the rental agreement in aggregate and for each of the following periods are as follows:		
– Within one year	63	44
– After one year but not more than five years	47	–
– More than five years	–	–
	110	44

¹ An independent valuation was performed whereby the fair value was based on an overview of property sales (units within the same building as the investment property) during 2016, weighted towards the most recent sales activity and taking into account current and future trending market sentiment.

11. INTANGIBLE ASSETS

As at 31 December 2016	Intangibles US\$'000	Goodwill US\$'000	Total US\$'000
Cost			
Balance at 1 January 2016	783	13 305	14 088
Foreign exchange difference	–	665	665
Balance at 31 December 2016	783	13 970	14 753
Accumulated amortisation			
Balance at 1 January 2016	578	–	578
Amortisation	157	–	157
Impairment	4	–	4
Balance at 31 December 2016	739	–	739
Net book value at 31 December 2016	44	13 970	14 014
As at 31 December 2015			
Cost			
Balance at 1 January 2015	784	17 818	18 602
Foreign exchange difference	(1)	(4 513)	(4 514)
Balance at 31 December 2015	783	13 305	14 088
Accumulated amortisation			
Balance at 1 January 2015	421	–	421
Amortisation	157	–	157
Balance at 31 December 2015	578	–	578
Net book value at 31 December 2015	205	13 305	13 510

Impairment of goodwill within the Group was tested in accordance with the Group's policy. Refer to Note 12, Impairment testing, for further details.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

12. IMPAIRMENT TESTING

	2016 US\$'000	2015 US\$'000
Impairment		
Ghaghoo	170 778 ¹	–
CDIH	2 154 ²	–
Total impairment	172 932	–

¹ As a result of the continued market uncertainty, the ongoing difficult market conditions for Ghaghoo's production and the challenges in the operation reaching targeted production it was decided to place the mine on care and maintenance post-year end. Ghaghoo's recoverable amount was reassessed at 31 December 2016 and an impairment was considered appropriate. The Group recognised a consolidated income statement impairment charge of US\$170.8 million (post-tax), being the write-down of US\$0.2 million inventory and all non-current assets of Ghaghoo.

² During 2016, the Group abandoned the CDIH Group, which developed and maintained laser diamond shaping and cutting technology and machinery due to its inability to generate profits. The impairment on CDIH includes US\$0.3 million write-down of inventory and US\$1.9 million write-down of other assets.

	2016 US\$'000	2015 US\$'000
Goodwill		
Goodwill acquired through business combinations has been allocated to the individual cash-generating unit, as follows:		
– Letšeng Diamonds	13 970	13 305
Balance at end of year	13 970	13 305

Movement in goodwill relates mainly to foreign exchange translation from functional to presentation currency.

The discount rate is outlined below, and represents the nominal pre-tax rate. This rate is based on the weighted average cost of capital (WACC) of the Group and adjusted accordingly at a risk premium for the Letšeng Diamonds cash-generating unit, taking into account risks associated therein.

	2016 %	2015 %
Discount rate		
– Letšeng Diamonds	12.6	12.0

Goodwill impairment testing is undertaken annually and whenever there are indications of impairment. The most recent test was undertaken at 31 December 2016. In assessing whether goodwill has been impaired, the carrying amount of the Letšeng Diamonds cash-generating unit is compared with its recoverable amount. For the purpose of goodwill impairment testing in 2016, the recoverable amount for Letšeng Diamonds has been determined based on a value-in-use model, similar to that done in the past.

Value in use

Cash flows are projected for a period up to the date that mining is expected to cease, based on management's expectations at the time of completing the testing. The period used was eight years, representing the lesser of the current economic resource or the remaining eight-year mining lease period.

12. IMPAIRMENT TESTING (continued)**Sensitivity to changes in assumptions**

For the purpose of testing for impairment of goodwill using the value-in-use basis for the Letšeng mining cash-generating unit, it was assessed that no reasonably possible change in any of the key assumptions would cause its carrying amount to exceed its recoverable amount.

The Group will continue to test its assets for impairment where indications are identified and may, in future, record additional impairment charges or reverse any impairment charges to the extent that market conditions improve and to the extent permitted by accounting standards.

13. RECEIVABLES AND OTHER ASSETS

	2016 US\$'000	2015 US\$'000
Non-current		
Prepayments ¹	–	1 905
Other receivables	31	313
	31	2 218
Current		
Trade receivables ²	1 187	83
Prepayments	756	780
Deposits	135	457
Other receivables	334	58
VAT receivable	4 145	4 449
	6 557	5 827

¹ The waste tonnes that had to be recovered from the mining contractor, which were overpaid in previous periods and gave rise to the prepayment in the prior year, were fully recovered from the mining contractor during the current year.

² Trade receivables mainly relates to margin recognised on partnership arrangements for which proceeds were received post period end.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

13. RECEIVABLES AND OTHER ASSETS (continued)

The carrying amounts above approximate their fair value.

Terms and conditions of the receivables:

	2016 US\$'000	2015 US\$'000
Analysis of trade receivables		
Neither past due nor impaired	1 154	53
Past due but not impaired:		
Less than 30 days	33	20
30 to 60 days	–	4
60 to 90 days	–	4
90 to 120 days	–	2
	1 187	83
14. INVENTORIES		
Diamonds on hand	17 278	18 984
Ore stockpiles	1 909	1 658
Consumable stores	11 724	9 646
	30 911	30 288
Net realisable value write-down ¹	466	–

¹ The write-down relates to inventory written down. Refer to Note 4, Exceptional item and Note 12, Impairment testing.

15. CASH AND SHORT-TERM DEPOSITS

	2016 US\$'000	2015 US\$'000
Cash on hand	2	1
Bank balances	15 762	58 465
Short-term bank deposits	15 023	27 253
	30 787	85 719

The amounts reflected in the financial statements approximate fair value.

Cash at banks earn interest at floating rates based on daily bank deposit rates. Short-term deposits are generally call deposit accounts and earn interest at the respective short-term deposit rates.

At 31 December 2016, the Group had restricted cash of US\$3.1 million (31 December 2015: US\$2.6 million). This restricted cash mainly relates to funds reserved for the debt service of the US\$25.0 million secured bank loan facility at Ghaghoo.

The Group's cash surpluses are deposited with major financial institutions of high-quality credit standing predominantly within Lesotho and the United Kingdom.

At 31 December 2016, the Group had US\$53.3 million (31 December 2015: US\$16.1 million) of undrawn facilities representing the LSL250.0 million (US\$18.3 million) three-year unsecured revolving working capital facility at Letšeng and the US\$35.0 million three-year unsecured revolving credit facility at the Company.

For further details on these facilities, refer to Note 17, Interest-bearing loans and borrowings, and Note 29, Events after the reporting period.

16. ISSUED CAPITAL AND RESERVES

Issued capital

	31 December 2016		31 December 2015	
	Number of shares '000	US\$'000	Number of shares '000	US\$'000
Authorised – ordinary shares of US\$0.01 each				
As at year end	200 000	2 000	200 000	2 000
Issued and fully paid				
Balance at beginning of year	138 296	1 383	138 270	1 383
Allotments during the year	65	1	27	–
Balance at end of year	138 361	1 384	138 297	1 383

Share premium

Share premium comprises the excess value recognised from the issue of ordinary shares at par value.

Treasury shares

The Company established an Employee Share Option Plan (ESOP) on 5 February 2007. Under the terms of the ESOP, the Company granted options to employees of over 376 500 ordinary shares with a nil exercise price upon listing. At listing, the Gem Diamonds Limited Employee Share Trust acquired these ordinary shares by subscription from the Company at nominal value of US\$0.01.

During the current year, 5 000 shares were exercised (31 December 2015: 7 350) and no shares lapsed (31 December 2015: nil). At 31 December 2016, 53 200 shares were held by the trust (31 December 2015: 58 200).

Other reserves	Foreign currency translation reserve US\$'000	Share-based equity reserve US\$'000	Total US\$'000
Balance at 1 January 2016	(214 162)	50 742	(163 420)
Other comprehensive expense	18 017	–	18 017
Total comprehensive expense	18 017	–	18 017
Share-based payments	–	1 905	1 905
Balance at 31 December 2016	(196 145)	52 647	(143 498)
Balance at 1 January 2015	(146 551)	48 798	(97 753)
Other comprehensive expense	(67 611)	–	(67 611)
Total comprehensive expense	(67 611)	–	(67 611)
Share-based payments	–	1 944	1 944
Balance at 31 December 2015	(214 162)	50 742	(163 420)

Notes to the Annual Financial Statements continued

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16. ISSUED CAPITAL AND RESERVES (continued)

Foreign currency translation reserve

The foreign currency translation reserve comprises all foreign exchange differences arising from the translation of foreign entities. The South African, Lesotho, Botswana and United Arab Emirate subsidiaries' functional currencies are different to the Group's functional currency of US dollar. The rates used to convert the operating functional currency into US dollar are as follows:

	Currency	2016	2015
Average rate	ZAR/LSL to US\$1	14.70	12.78
Period end	ZAR/LSL to US\$1	13.68	15.50
Average rate	Pula to US\$1	10.89	10.14
Period end	Pula to US\$1	10.68	11.25
Average rate	Dirham to US\$1	3.68	3.67
Period end	Dirham to US\$1	3.68	3.67

Share-based equity reserves

For details on the share-based equity reserve, refer to Note 25, Share-based payments.

Capital management

For details on capital management, refer to Note 24, Financial risk management.

17. INTEREST-BEARING LOANS AND BORROWINGS

	Effective interest rate %	Maturity	2016 US\$'000	2015 US\$'000
Non-current				
LSL140.0 million bank loan facility	South African JIBAR + 4.95%	30 June 2017 ¹	–	1 807
US\$25.0 million bank loan facility	London US\$ three-month LIBOR + 5.5%	30 June 2021 ²	–	23 275
			–	25 082
Current				
LSL140.0 million bank loan facility	South African JIBAR + 4.95%	30 June 2017 ¹	2 047	3 614
US\$25.0 million bank loan facility	London US\$ three-month LIBOR + 5.5%	30 June 2021 ²	25 710	1 725
			27 757	5 339

¹ LSL140.0 million bank loan facility at Letšeng Diamonds

This loan is a three-year unsecured project debt facility signed jointly with Standard Lesotho Bank and Nedbank Limited on 26 June 2014 for the total funding of the Coarse Recovery Plant. The loan is repayable in 10 quarterly payments which commenced 31 March 2015 with a final payment due on 30 June 2017; however, full repayment was made on 10 February 2017. The interest rate for the facility at 31 December 2016 is 12.3% (31 December 2015: 11.6%).

² US\$25.0 million bank loan facility at Gem Diamonds Botswana (Ghaghoo)

Following the decision to place the Ghaghoo mine on care and maintenance, the US\$25.0 million facility was repaid through the utilisation of the existing Company US\$35.0 million facility. At 31 December 2016, the facility was reclassified into current liabilities.

Total interest for the year on the interest-bearing loans and borrowings was US\$1.9 million (2015: US\$2.5 million) of which US\$1.6 million related to the Ghaghoo facility and has been capitalised to the carrying value of the asset as borrowing costs.

Other facilities

In addition, at 31 December 2016, the Group has the following available facilities:

- ▶ At Gem Diamonds Limited, a US\$35.0 million three-year unsecured revolving credit facility with Nedbank Capital which was renewed on 29 January 2016. No amounts have been drawn down during the year. Following the repayment of the US\$25.0 million facility in early 2017, the available amount on this facility reduced to US\$10.0 million.
- ▶ Through its subsidiary Letšeng Diamonds, a LSL250.0 million (US\$18.3 million) three-year unsecured revolving working capital facility jointly with Standard Lesotho Bank and Nedbank Capital, which was renewed in July 2015.

18. TRADE AND OTHER PAYABLES

	2016 US\$'000	2015 US\$'000
Non-current		
Operating lease	–	82
Severance pay benefits ¹	1 409	1 056
	1 409	1 138
Current		
Trade payables ²	15 599	16 340
Accrued expenses ²	8 430	9 342
Leave benefits	1 011	730
Royalties ²	2 024	4 285
Operating lease	1 260	741
Other	688	790
	29 012	32 228
Total trade and other payables	30 421	33 366

The carrying amounts above approximate fair value.

Terms and conditions of the trade and other payables:

¹ The severance pay benefits arise due to legislation within the Lesotho jurisdiction, requiring that two weeks of severance pay be provided for every completed year of service, payable on retirement.

² These amounts are mainly non-interest-bearing and are settled in accordance with terms agreed between the parties.

19. PROVISIONS

	2016 US\$'000	2015 US\$'000
Rehabilitation provisions	16 630	12 473
Reconciliation of movement in rehabilitation provisions		
Balance at beginning of year	12 473	19 543
Increase/(decrease) during the year	1 631	(4 229)
Unwinding of discount rate	899	1 265
Foreign exchange differences	1 627	(4 106)
Balance at end of year	16 630	12 473

Rehabilitation provisions

The provisions have been recognised as the Group has an obligation for rehabilitation of the mining areas. The provisions have been calculated based on total estimated rehabilitation costs, discounted back to their present values over the life of mine at the mining operations. The pre-tax discount rates are adjusted annually and reflect current market assessments.

In determining the amounts attributable to the rehabilitation provisions, management used a discount rate range of 6.0% to 7.4% (31 December 2015: 6.5% to 7.5%), estimated rehabilitation timing of eight to 11 years (31 December 2015: nine to 12 years) and an inflation rate range of 4.0% to 6.7% (31 December 2015: 4.6% to 6.0%) respectively at the Botswana and Lesotho mining areas. In addition to the changes in the discount rates, inflation and rehabilitation timing, the increase in the provision is attributable to the annual reassessment of the estimated closure costs performed at the operations and the strengthening of the local currencies against the US dollar.

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20. DEFERRED TAXATION

	2016 US\$'000	2015 US\$'000
Deferred tax assets		
Accrued leave	56	34
Operating lease liability	5	2
Provisions	4 539	3 594
Tax loss not utilised	–	239
	4 600	3 869
Deferred tax liabilities		
Property, plant and equipment	(65 870)	(49 652)
Prepayments	(367)	(563)
Unremitted earnings	(4 039)	(4 039)
	(70 276)	(54 254)
Net deferred tax liability	(65 676)	(50 385)
Reconciliation of deferred tax liability		
Balance at beginning of year	(50 385)	(57 467)
Movement in current period:		
– Accelerated depreciation for tax purposes	(9 851)	(6 193)
– Accrued leave	(198)	(5)
– Operating lease liability	72	93
– Prepayments	208	(293)
– Provisions	537	(308)
– Tax losses utilised in the year	(217)	220
– Disposal of subsidiaries	–	50
– Foreign exchange differences	(5 842)	13 518
Balance at end of year	(65 676)	(50 385)

The Group has not recognised a deferred tax liability for all taxable temporary differences associated with investments in subsidiaries because it is able to control the timing of dividends and only part of the temporary difference is expected to reverse in the foreseeable future. The gross temporary difference in respect of the undistributable reserves of the Group's subsidiaries for which a deferred tax liability has not been recognised is US\$49.3 million (31 December 2015: US\$39.1 million).

The Group has estimated tax losses of US\$348.3 million (31 December 2015: US\$311.7 million). The deferred tax asset of US\$0.9 million recognised in the prior year has been fully utilised during the current year. All tax losses are generated in jurisdictions where tax losses do not expire.

21. CASH FLOW NOTES

	Notes	2016 US\$'000	2015 US\$'000
21.1 Cash generated by operations			
(Loss)/profit for the year before tax from continuing operations		(124 108)	108 557
Profit/(loss) before tax for the year from discontinued operation		–	668
Adjustments for:			
Depreciation and amortisation on property, plant and equipment	3	10 760	10 369
Waste stripping cost amortised	3	34 712	47 222
Impairment on assets	4	172 932	–
Finance income	5	(2 411)	(1 505)
Finance costs	5	2 620	1 385
Market to market revaluations		–	(249)
Unrealised foreign exchange differences		(4 718)	(6 369)
Profit on disposal of property, plant and equipment		(16)	(251)
Movement in prepayment		254	1 115
Other non-cash movements		1 703	(5 753)
Gain on disposal of subsidiary		–	(1 670)
Share-based equity transaction		1 790	1 738
		93 518	155 257
21.2 Working capital adjustment			
Decrease/(increase) in inventory		1 579	(8 216)
Decrease/(increase) in receivables		5 259	(4 586)
(Decrease)/increase in trade and other payables		(6 392)	9 033
		446	(3 769)
21.3 Cash flows used in investing activities			
Cash equivalents sold		–	(34)
Net cash proceeds divested		–	(34)

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

22. COMMITMENTS AND CONTINGENCIES

	2016 US\$'000	2015 US\$'000
Commitments		
Operating lease commitments – Group as lessee		
The Group has entered into commercial lease arrangements for rental of office premises. These leases have a period of between two and 12 years with an option of renewal at the end of the period. The terms will be negotiated during the extension option periods catered for in the agreements. There are no restrictions placed upon the lessee by entering into these leases. Future minimum rentals payable under non-cancellable operating leases:		
– Within one year	1 753	1 443
– After one year but not more than five years	5 087	3 759
– More than five years	5 797	5 900
	12 637	11 102
Mining leases		
Mining lease commitments represent the Group's future obligation arising from agreements entered into with local authorities in the mining areas that the Group operates.		
The period of these commitments is determined as the lesser of the term of the agreement, including renewable periods, or the life of the mine. The estimated lease obligation regarding the future lease period, accepting stable inflation and exchange rates, is as follows:		
– Within one year	112	107
– After one year but not more than five years	593	492
– More than five years	1 283	1 271
	1 988	1 870
Moveable equipment lease		
The Group has entered into commercial lease arrangements which include the provision of loading, hauling and other transportation services payable at a fixed rate per tonne of ore and waste mined; power generator equipment payable based on a consumption basis; and rental agreements for various mining equipment based on a fixed monthly fee.		
– Within one year	41 749	25 428
– After one year but not more than five years	175 704	157 883
– More than five years	–	33 138
	217 453	216 449
Capital expenditure		
Approved but not contracted for	19 927	127
Approved and contracted for	3 315	5 229

The main capital expenditure approved but not contracted for relates to the construction of the Letšeng mining workshop of LSL215.0 million (US\$15.7 million). The capital expenditure will be funded from a new project facility which is being finalised in 2017.

Contingent rentals – Alluvial Ventures

The contingent rentals represent the Group's obligation to a third party (Alluvial Ventures) for operating a third plant on the Group's mining property at Letšeng Diamonds. The rental is determined when the actual diamonds mined by Alluvial Ventures are sold. The rental agreement is based on 50% to 70% of the value (after costs) of the diamonds recovered by Alluvial Ventures and is limited to US\$1.2 million per individual diamond. As at the reporting date, such future sales cannot be determined.

Letšeng Diamonds Educational Fund

In terms of the mining agreement entered into between the Group and the government of the Kingdom of Lesotho, the Group has an obligation to provide funding for education and training scholarships. The quantum of such funding is at the discretion of the Letšeng Diamonds Education Fund Committee. The amount of the funding provided for the current year was US\$0.1 million (31 December 2015: US\$0.1 million).

22. COMMITMENTS AND CONTINGENCIES (continued)**Contingencies**

The Group has conducted its operations in the ordinary course of business in accordance with its understanding and interpretation of commercial arrangements and applicable legislation in the countries where the Group has operations. In certain specific transactions, however, the relevant third party or authorities could have a different interpretation of those laws and regulations that could lead to contingencies or additional liabilities for the Group. Having consulted professional advisers, the Group has identified possible disputes approximating US\$0.5 million (December 2015: US\$0.6 million) and tax claims within the various jurisdictions in which the Group operates approximating US\$1.0 million (December 2015: US\$1.3 million). There are no possible disputes relating to Ghaghoo's care and maintenance status included in these contingencies.

There remains a risk that further tax liabilities may potentially arise. While it is difficult to predict the ultimate outcome in some cases, the Group does not anticipate that there will be any material impact on the Group's results, financial position or liquidity.

23. RELATED PARTIES

Related party	Relationship
Jemax Management (Proprietary) Limited	Common director
Jemax Aviation (Proprietary) Limited	Common director
Gem Diamond Holdings Limited	Common director
Government of Lesotho	Non-controlling interest

Refer to Note 1.1.2, Operational information, for information regarding shareholding in subsidiaries.

Refer to the Directors' Report for information regarding the Directors.

	2016 US\$'000	2015 US\$'000
Compensation to key management personnel (including Directors)		
Share-based equity transactions	1 396	1 421
Short-term employee benefits	3 907	7 784
	5 303	9 205
Fees paid to related parties		
Jemax Aviation (Proprietary) Limited	(96)	(108)
Jemax Management (Proprietary) Limited	(75)	(165)
Royalties paid to related parties		
Government of Lesotho	(14 624)	(19 273)
Lease and licence payments to related parties		
Government of Lesotho	(126)	(112)
Purchases from related parties		
Jemax Aviation (Proprietary) Limited	(97)	(75)
Jemax Management (Proprietary) Limited	(82)	(89)
Amount included in trade receivables owing by/(to) related parties		
Jemax Aviation (Proprietary) Limited	4	(42)
Jemax Management (Proprietary) Limited	(8)	(7)
Amounts owing to related party		
Government of Lesotho	(1 966)	(3 513)
Dividends paid		
Government of Lesotho	(13 963)	(11 760)

Jemax Management (Proprietary) Limited and Jemax Aviation (Proprietary) Limited provided administrative and aviation services with regard to the mining activities undertaken by the Group. The above transactions were made on terms agreed between the parties and were made on terms that prevail in arm's-length transactions.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

24. FINANCIAL RISK MANAGEMENT

Financial risk factors

The Group's activities expose it to a variety of financial risks:

- ▶ market risk (including commodity price risk and foreign exchange risk);
- ▶ credit risk; and
- ▶ liquidity risk.

The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

Risk management is carried out under policies approved by the Board of Directors. The Board provides principles for overall risk management, as well as policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments, and investing excess liquidity.

There have been no changes to the financial risk management policy since the prior year.

Capital management

The capital of the Company is the issued share capital, share premium and treasury shares on the Group's statement of financial position. The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximise shareholder value. The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may issue new shares. The management of the Group's capital is performed by the Board.

At 31 December 2016, the Group has US\$53.3 million (31 December 2015: US\$16.1 million) debt facilities available and continues to have the flexibility to manage the capital structure more efficiently by the use of these debt facilities, thus ensuring that an appropriate gearing ratio is achieved.

The debt facilities in the Group are as follows:

Unsecured – Standard Lesotho Bank and Nedbank Capital (a division of Nedbank Limited) – three-year unsecured revolving credit facility – LSL250.0 million (US\$18.3 million)

The Group, through its subsidiary, Letšeng Diamonds, has an LSL250.0 million (US\$18.3 million), three-year unsecured revolving working capital facility. The facility bears interest at the Lesotho prime rate.

At year end, there is no drawdown on this facility.

Secured – Nedbank Capital (a division of Nedbank Limited) – six-and-a-half-year project debt facility – US\$25.0 million

The Group, through its subsidiary, Gem Diamonds Botswana (Ghaghoo), has a secured debt loan facility held with Nedbank Capital. In November 2016 this loan was restructured in order to postpone further capital repayments from June 2016 to June 2019, with final repayment due on 31 December 2021. The loan is repayable in staggered bi-annual payments. The first capital repayment of US\$0.1 million was paid in June 2016 with the next capital repayment due in June 2019. The facility bears interest at London USD Interbank three-month LIBOR + 5.5%.

At year end, this facility was fully drawn down. Post-year end this facility was fully repaid in line with placing the Ghaghoo asset on care and maintenance. For further detail refer to Note 17, Interest-bearing borrowings and Note 29, Events after the reporting period.

Unsecured – Standard Lesotho Bank and Nedbank Limited – three-year unsecured project debt facility – LSL140.0 million (US\$10.2 million)

This loan is a three-year unsecured project debt facility signed jointly with Standard Lesotho Bank and Nedbank Limited on 26 June 2014 for LSL140.0 million, being the total funding of the Coarse Recovery Plant with a final payment due on 30 June 2017. This facility bears interest at South African JIBAR + 4.95%.

At year end, there was LSL28.0 million (US\$2.0 million) outstanding on this facility. Post-year end, this facility was fully repaid in advance of its final repayment date. For further detail refer to Note 17, Interest-bearing borrowings and Note 29, Events after the reporting period.

Unsecured – Nedbank Capital (a division of Nedbank Limited) – three-year unsecured revolving credit facility – US\$35.0 million

The Company has a US\$35.0 million three-year unsecured revolving credit facility with Nedbank Capital which was renewed on 29 January 2016. This facility bears interest at London USD Interbank three-month LIBOR + 5.5%.

At year end, there is no drawdown on this facility. Post-year end this facility was accessed in order to settle the Ghaghoo US\$25.0 million facility.

24. FINANCIAL RISK MANAGEMENT (continued)

Capital management (continued)

The Group is subject to diamond price risk. Diamonds are not homogeneous products and the price of rough diamonds is not monitored on a public index system. The fluctuation of prices is related to certain features of diamonds such as quality and size. Diamond prices are marketed in US dollar and long-term US\$ per carat prices are based on external market consensus forecasts and contracted sales arrangements adjusted for the Group's specific operations. The Group does not have any financial instruments that may fluctuate as a result of commodity price movements.

(a) Market risk

(i) Foreign exchange risk

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the Lesotho Loti, South African Rand and Botswana Pula. Foreign exchange risk arises when future commercial transactions, recognised assets and liabilities are denominated in a currency that is not the entity's functional currency.

The Group's sales are denominated in US dollar which is the functional currency of the Company, but not the functional currency of the operations.

The currency sensitivity analysis below is based on the following assumptions:

Differences resulting from the translation of the financial statements of the subsidiaries into the Group's presentation currency of US dollar, are not taken into consideration.

The major currency exposures for the Group relate to the US dollar and local currencies of subsidiaries. Foreign currency exposures between two currencies where one is not the US dollar are deemed insignificant to the Group and have therefore been excluded from the sensitivity analysis.

The analysis of the currency risk arises because of financial instruments denominated in a currency that is not the functional currency of the relevant Group entity. The sensitivity has been based on financial assets and liabilities at 31 December 2016. There has been no change in the assumptions or method applied from the prior year.

Sensitivity analysis

If the US dollar had appreciated/(depreciated) 10% against currencies significant to the Group at 31 December 2016, income before taxation would have been US\$2.6 million higher/(lower) (31 December 2015: US\$3.1 million). There would be no effect on equity reserves other than those directly related to income statement movements.

(ii) Forward exchange contracts

The Group enters into forward exchange contracts to hedge the exposure to changes in foreign currency of future sales of diamonds at Letšeng Diamonds. The Group performs no hedge accounting. At 31 December 2016, the Group had no forward exchange contracts outstanding (31 December 2015: US\$nil).

(iii) Cash flow interest rate risk

The Group's income and operating cash flows are substantially independent of changes in market interest rates. The Group's cash flow interest rate risk arises from borrowings. Borrowings issued at variable rates expose the Group to cash flow interest rate risk. At the time of taking new loans or borrowings, management uses its judgement to decide whether it believes that a fixed or variable rate borrowing would be more favourable to the Group over the expected period until maturity.

(b) Credit risk

The Group's potential concentration of credit risk consists mainly of cash deposits with banks and other receivables. The Group's short-term cash surpluses are placed with the banks that have investment grade ratings. The maximum credit risk exposure relating to financial assets is represented by the carrying value as at the reporting dates. The Group considers the credit standing of counterparties when making deposits to manage the credit risk.

Considering the nature of the Group's ultimate customers and the relevant terms and conditions entered into with such customers, the Group believes that credit risk is limited as customers pay on receipt of goods.

No other financial assets are impaired or past due and accordingly, no additional analysis has been provided.

No collateral is held in respect of any impaired receivables or receivables that are past due but not impaired.

Notes to the Annual Financial Statements continued

for the year ended 31 December 2016

24. FINANCIAL RISK MANAGEMENT (continued)

Capital management (continued)

(c) Liquidity risk

Liquidity risk arises from the Group's inability to obtain the funds it requires to comply with its commitments including the inability to sell a financial asset quickly at a price close to its fair value. Management manages the risk by maintaining sufficient cash, marketable securities and ensuring access to financial institutions and shareholding funding. This ensures flexibility in maintaining business operations and maximises opportunities. The Group has available debt facilities of US\$53.3 million at year end.

The table below summarises the maturity profile of the Group's financial liabilities at 31 December based on contractual undiscounted payments:

	2016 US\$'000	2015 US\$'000
Floating interest rates		
Interest-bearing loans and borrowings ¹		
– Within one year	28 689	7 438
– After one year but not more than five years	1 587	29 658
Total	30 276	37 096
Trade and other payables		
– Within one year	29 012	32 228
– After one year but not more than five years	1 409	1 138
Total	30 421	33 366

¹ Includes the Letšeng and Ghaghoo facilities which have been repaid subsequent to year end. For further detail refer to Note 29, Events after the reporting period.

25. SHARE-BASED PAYMENTS

The expense recognised for employee services received during the year is shown in the following table:

	2016 US\$'000	2015 US\$'000
Equity-settled share-based payment transactions charged to the income statement	1 790	1 738
Equity-settled share-based payment transactions capitalised	116	206
	1 906	1 944

The long-term incentive plans are described below:

Employee Share Option Plan (ESOP)

Certain key employees are entitled to a grant of options, under the ESOP of the Company. The vesting of the options is dependent on employees remaining in service for a prescribed period (normally three years) from the date of grant. The fair value of share options granted is estimated at the date of the grant using a Black Scholes simulation model, taking into account the terms and conditions upon which the options were granted. It takes into account projected dividends and share price fluctuation co-variances of the Company.

There is a nil or nominal exercise price for the options granted at admission of the Company. The contractual life of the options is 10 years and there are no cash settlement alternatives. The Company has no past practice of cash settlement.

Non-Executive share awards

In order to align the interests of the Chairman and independent Directors with those of the shareholders, the non-Executive Directors were invited to subscribe for shares at nominal value on terms set out in the prospectus. The non-Executive Directors shall not be eligible to participate in the short-term incentive bonus scheme (STIBS) or ESOP or any other performance-related incentive arrangements which may be introduced by the Company from time to time. There are currently no non-Executive share awards.

ESOP for September 2012 (LTIP)

On 11 September 2012, 936 000 nil-cost options were granted to certain key employees (excluding Executive Directors) under the LTIP of the Company. Of the total number of shares, 312 000 were nil value options and 624 000 were market value options. The exercise price of the market value options is £1.78 (US\$2.85), which was equal to the market price of the shares on the date of grant. The awards which vest over a three-year period in tranches of a third of the award each year, dependent on the performance targets for the 2013, 2014 and 2015 financial years being met, are exercisable between 1 January 2016 and 31 December 2023. This award became exercisable on 1 January 2016. Of the 936 000 options originally granted, only 217 100 are still outstanding following the resignation of a number of employees and the exercising of these options.

25. SHARE-BASED PAYMENTS (continued)

ESOP for March 2014 (LTIP)

In March 2014, 625 000 nil-cost options were granted to certain key employees under the LTIP of the Company. The vesting of the options will be subject to the satisfaction of certain performance as well as service conditions classified as non-market conditions. The options which vest over a three-year period in tranches of a third of the award each year are exercisable between 19 March 2017 and 18 March 2024. If the performance or service conditions are not met, the options lapse. As the performance conditions are non-market-based they are not reflected in the fair value of the award at grant date, and therefore the Company will assess the likelihood of these conditions being met with a relevant adjustment to the cumulative charge as required at each financial year end. The fair value of the nil-cost options is £1.74 (US\$2.87). Of the 625 000 options originally granted, only 297 271 are still outstanding following the resignation of a number of employees.

ESOP for June 2014 (LTIP)

In June 2014, 609 000 nil-cost options were granted to the Executive Directors under the LTIP of the Company. The vesting of the options will be subject to the satisfaction of certain market and non-market performance conditions over a three-year period. Of the 609 000 nil-cost options, 152 250 relates to market conditions with the remaining 456 750 relating to non-market conditions. The options which vest are exercisable between 10 June 2017 and 9 June 2024. If the performance or service conditions are not met, the options lapse. The performance conditions relating to the non-market conditions are not reflected in the fair value of the award at grant date. At each financial year end, the Company will assess the likelihood of these conditions being met with a relevant adjustment to the cumulative charge as required. The fair value of the nil-cost options relating to non-market conditions is £1.61 (US\$2.70). The fair value of the options granted, relating to the market conditions, is estimated at the date of the grant using a Monte Carlo simulation model, taking into account the terms and conditions upon which the options were granted, projected dividends, share price fluctuations, the expected volatility, the risk-free interest rate, expected life of the options in years and the weighted average share price of the Company. Of the 609 000 options originally granted, only 560 839 are still outstanding following the resignation of an Executive Director during the year.

ESOP for April 2015 (LTIP)

In April 2015, 660 000 nil-cost options were granted to certain key employees under the long-term incentive plan (LTIP) of the Company. The vesting of the options will be subject to the satisfaction of certain performance as well as service conditions classified as non-market conditions. The options which vest after a three-year period are exercisable between 1 April 2018 and 31 March 2025. If the performance or service conditions are not met, the options lapse. As the performance conditions are non-market-based they are not reflected in the fair value of the award at grant date, and therefore the Company will assess the likelihood of these conditions being met with a relevant adjustment to the cumulative charge as required at each financial year end. The fair value of the nil-cost options is £1.33 (US\$1.97). Of the 667 500 options originally granted, only 472 608 are still outstanding following the resignation of a number of employees.

In addition, 740 000 nil-cost options were granted to the Executive Directors under the LTIP of the Company. The vesting of the options will be subject to the satisfaction of certain market and non-market performance conditions over a three-year period. Of the 740 000 nil-cost options, 185 000 relate to market conditions with the remaining 555 000 relating to non-market conditions. The options which vest are exercisable between 1 April 2018 and 31 March 2025. If the performance or service conditions are not met, the options lapse. The performance conditions relating to the non-market conditions are not reflected in the fair value of the award at grant date. At each financial year end, the Company will assess the likelihood of these conditions being met with a relevant adjustment to the cumulative charge as required. The fair value of the nil-cost options relating to the market conditions is £1.33 (US\$1.97). The fair value of these options is estimated in a similar manner as the June 2014 LTIP. Of the 740 000 options originally granted, only 640 730 are still outstanding following the resignation of an Executive Director during the year.

ESOP for March 2016 (LTIP)

In March 2016, 1 400 000 nil-cost options were approved to be granted to certain key employees and Executive Directors under the LTIP of the Company. The vesting of the options will be subject to the satisfaction of certain market and non-market performance conditions over a three-year period. The satisfaction of certain performance as well as service conditions are classified as non-market conditions. A total of 185 000 of the options granted relate to market conditions. The options vest after a three-year period and are exercisable between 15 March 2019 and 14 March 2026. If the performance or service conditions are not met, the options lapse. The performance conditions relating to the non-market conditions are not reflected in the fair value of the award at grant date, and therefore the Company will assess the likelihood of these conditions being met with a relevant adjustment to the cumulative charge as required at each financial year end. The fair value of the nil-cost options is £0.99 (US\$1.40). The fair value of the options relating to market conditions is estimated in a similar manner as the June 2014 and April 2015 LTIP. Of the total options originally granted, 1 340 000 are still outstanding following the resignation of a number of employees.

Notes to the Annual Financial Statements continued

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25. SHARE-BASED PAYMENTS (continued)

Movements in the year

ESOP

The following table illustrates the number ('000) and movement in share options during the year:

	2016 '000	2015 '000
Outstanding at beginning of year	11	18
Exercised during the year	(5)	(7)
Balance at end of year	6	11
Exercisable at end of year	–	–

The following table lists the inputs to the model used for the plan for the awards granted under the ESOP:

Dividend yield (%)	–
Expected volatility (%)	22
Risk-free interest rate (%)	5
Expected life of option (years)	10
Weighted average share price	18.28
Model used	Black Scholes

The fair value of share options granted is estimated at the date of the grant using a Black Scholes simulation model, taking into account the terms and conditions upon which the options were granted, projected dividends, share price fluctuations, the expected volatility, the risk-free interest rate, expected life of the option in years and the weighted average share price of the Company.

The ESOP is an equity-settled plan and the fair value is measured at the grant date.

ESOP for March 2016, April 2015, June 2014, March 2014 and September 2012 (LTIP)

The following table illustrates the number ('000) and movement in the outstanding share options during the year:

	2016 '000	2015 '000
Outstanding at beginning of year	2 726	2 445
Granted during the year	1 400	1 408
Exercised during the year	(61)	–
Forfeited	(536)	(1 127)
Balance at end of year	3 529	2 726

The following table lists the inputs to the model used for the market conditions awards granted during the current and prior year:

	LTIP March 2016	LTIP April 2015	LTIP June 2014	LTIP September 2012
Dividend yield (%)	2.00	2.00	–	–
Expected volatility (%)	39.71	37.18	37.25	42.10
Risk-free interest rate (%)	0.97	1.16	1.94	0.33
Expected life of option (years)	3.00	3.00	3.00	3.00
Weighted average share price (US\$)	1.56	2.10	2.70	2.85
Fair value of nil value options (US\$)	1.40	1.97	1.83	2.85
Fair value of market value options (US\$)	–	–	–	1.66
Model used	Monte Carlo	Monte Carlo	Monte Carlo	Monte Carlo

The fair value of share options granted is estimated at the date of the grant using a Monte Carlo simulation model, taking into account the terms and conditions upon which the options were granted, projected dividends, share price fluctuations, the expected volatility, the risk-free interest rate, expected life of the option in years and the weighted average share price of the Company.

26. FINANCIAL INSTRUMENTS

Set out below is an overview of financial instruments, other than the non-current and current portions of the prepayment disclosed in Note 13, Receivables and other assets, which do not meet the criteria of a financial asset. These prepayments are carried at amortised cost.

	31 December 2016 US\$'000	31 December 2015 US\$'000
Financial assets		
Cash (net of overdraft)	30 787	85 719
Receivables and other assets	5 832	5 360
Other financial assets	–	10
Total	36 619	91 089
Total non-current	31	317
Total current	36 588	90 772
Financial liabilities		
Interest-bearing loans and borrowings	27 757	30 421
Trade and other payables	30 421	33 366
Total	58 178	63 787
Total non-current	1 409	26 220
Total current	56 769	37 567

The carrying amounts of the Group's financial instruments held approximate their fair value.

Fair value hierarchy

All financial instruments for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, based on the lowest level input that is significant to the fair value measurement as a whole, as follows:

Level 1 – Quoted (unadjusted) market prices in active markets for identical assets or liabilities.

Level 2 – Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable.

Level 3 – Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

There were no transfers between Level 1 and Level 2 fair value measurements or any transfers into or out of Level 3 fair value measurements during the period.

Other risk management activities

The Group is exposed to foreign currency risk on future sales of diamonds at Letšeng Diamonds. In order to reduce this risk, the Group enters into forward exchange contracts to hedge this exposure. The Group performs no hedge accounting. During the current period the Group did not enter into any new forward exchange contracts due to the strong US dollar being favourable to the Group's revenue.

27. DIVIDENDS PAID AND PROPOSED

	2016 US\$'000	2015 US\$'000
Proposed dividends on ordinary shares		
Final ordinary cash dividend for 2016: US\$nil (2015: 5 US cents per share)	–	6 915
Special dividend for 2016: US\$nil (2015: 3.5 US cents per share)	–	4 840
Total	–	11 755

There were no dividends proposed for the 2016 financial year.

The 2015 dividends were approved on 7 June 2016 and a final cash dividend of 8.5 US cents per share was paid to shareholders on 16 June 2016.

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28. MATERIAL PARTLY OWNED SUBSIDIARIES

Financial information of Letšeng Diamonds, a subsidiary which has a material non-controlling interest, is provided below.

Proportion of equity interest held by non-controlling interests

Name incorporation	Country of and operation	2016 US\$'000	2015 US\$'000
Letšeng Diamonds (Proprietary) Limited	Lesotho		
Accumulated balances of material non-controlling interest		63 522	57 494
Profit allocated to material non-controlling interest		14 739	24 397

The summarised financial information of this subsidiary is provided below. This information is based on amounts before intercompany eliminations.

Summarised income statement for the year ended 31 December

Revenue	184 864	236 357
Cost of sales	(105 398)	(118 385)
Gross profit	79 466	117 972
Royalties and selling costs	(14 827)	(19 475)
Other (costs)/income	(217)	8 401
Operating profit	64 422	106 898
Net finance income	702	279
Profit before tax	65 124	107 177
Income tax expense	(15 996)	(25 850)
Profit for the year	49 128	81 327
Total comprehensive income	49 128	81 327
Attributable to non-controlling interest	14 739	24 397
Dividends paid to non-controlling interest	13 963	11 760

Summarised statement of financial position as at 31 December

Assets

Non-current assets

Property, plant and equipment and intangible assets 267 433 204 350

Current assets

Inventories, receivables and other assets, and cash and short-term deposits 45 438 78 436

Total assets 312 871 282 786

Non-current liabilities

Trade and other payables, provisions and deferred tax liabilities 76 304 59 345

Current liabilities

Interest-bearing loans and borrowings and trade and other payables 24 827 31 794

Total liabilities 101 131 91 139

Total equity 211 740 191 647

Attributable to:

Equity holders of parent 148 218 134 153

Non-controlling interest 63 522 57 494

Summarised cash flow information for the year ended 31 December

Operating 55 582 4 701

Investing (77 967) –

Financing (11 915) 5 421

Net (decrease)/increase in cash and cash equivalents (34 300) 10 122

29. EVENTS AFTER THE REPORTING PERIOD

Post-year end the outstanding balance of LSL28.0 million (US\$2.0 million) on the three-year unsecured project debt facility at Letšeng, was fully repaid together with interest and net breakage costs.

Post-year end, following the decision to place the Ghaghoo mine on care and maintenance, the US\$25.0 million term loan facility at Ghaghoo was settled in advance of its final repayment date using the US\$35.0 million revolving credit facility held at the Company. The restricted cash of US\$3.0 million reserved for a portion of the future repayment of the term loan facility at Ghaghoo was released at the same time.

No other fact or circumstance has taken place between the end of the reporting period and the approval of the financial statements which, in our opinion, is of significance in assessing the state of the Group's affairs.

Abbreviations and definitions

AGM	Annual general meeting
AIFR	All injury frequency rate
Basotho	Lesotho nationals
BVI	British Virgin Islands
BWP	Botswana Pula
CAGR	Compound annual growth rate
CDIH	Calibrated Diamonds Investment Holdings (Proprietary) Limited Group
CEO	Chief Executive Officer
CGU	Cash-generating unit
CO₂e	Carbon dioxide equivalent
cpht	Carats per hundred tonnes
CSI	Corporate social investment
DPA	Diamond Producers Association
DTR	Disclosure Guidance and Transparency Rules
EBITDA	Earnings before interest, tax, depreciation and amortisation
EPS	Earnings per share
ESOP	Employee Share Option Plan
EU	European Union
EY	Ernst & Young
FCA	Financial Conduct Authority
GDP	Gross domestic product
GHG	Greenhouse gas
GIA	Gemological Institute of America
GJ	Gigajoules
GRI	Global Reporting Initiative
ha	Hectare
HSSE	Health, safety, social and environment
IAS	International Accounting Standards
ICAEW	Institute of Chartered Accountants in England and Wales
IFRS	International Financial Reporting Standards
IPO	Initial Public Offering

ISO	International Organisation for Standardisation
JIBAR	Johannesburg Interbank Agreed Rate
KPI	Key performance indicators
LIBOR	London Interbank Offered Rate
LoM	Life of mine
LSL	Lesotho Loti
LTI	Lost time injury
LTIFR	Lost time injury frequency rate
LTIP	Long-term incentive plan
MCF	Mine call factor
PAC	Project affected community
ROACE	Return on average capital employed
RSA	Republic of South Africa
SAMREC	South African Mineral Resource Committee
Scope 1 emissions	Direct greenhouse gas emissions
Scope 2 emissions	Energy-indirect greenhouse gas emissions from the generation of purchased energy
Scope 3 emissions	Energy-indirect greenhouse gas emissions (not included in Scope 2)
SID	Senior Independent Director
STIBS	Short-term incentive bonus scheme
The Board	The Gem Diamonds Board of Directors
The Group	The Gem Diamonds Company and its subsidiaries
TSR	Total shareholder return
UK	United Kingdom
US\$	United States Dollar
USA / US	United States of America
WACC	Weighted average cost of capital
WF	Water footprint

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