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sappi

2018 Southern Africa Annual Report

Our businesses

Sappi Southern Africa has a tradition of innovating and developing new products to meet the demand for dissolving wood pulp, specialities and packaging papers, printing and writing papers, as well as biomaterials and biochemicals to our direct and indirect customer base.

Our dissolving wood pulp (specialised cellulose) products are used worldwide by converters to create viscose fibre for fashionable clothing and textiles, pharmaceutical products as well as a wide range of consumer and household products. Quality specialities and packaging papers are used in the manufacture of such products as soup sachets, cosmetic and confectionery packaging, boxes for agricultural products for export, tissue wadding for

household tissue products and casting and release papers used by suppliers to the fashion, textile, automobile and household industries. Our range of printing and writing papers include paper products used by printers in the production of books, brochures, magazines, catalogues, direct mail, stationery and newspapers.

The wood and pulp needed for our products is either produced within Sappi or brought from accredited suppliers. Across the group, Sappi is close to 'pulp neutral', meaning that we sell almost as much pulp as we buy. All wood grown on Sappi-owned land and a large proportion grown on plantations managed by us, is Forest Stewardship Council® (FSC®) and ISO 9000 certified.

We have a strong focus on social responsibility in South Africa. This is an economic imperative in the region. Our plantations and most of our mills are located in rural areas and we therefore have an important influence on development in these areas. We continue to make progress on each of the elements of our Broad-based Black Economic Empowerment (BBBEE) scorecard.

Full details of our education, training, health and environmental initiatives can be found on our website www.sappi.com.

Southern Africa

Plantations*	Products produced	Capacity ⁽¹⁾ ('000)		
		Ha	Standing tons	m ³
KwaZulu-Natal	Plantations (pulpwood and sawlogs)**	253	11,336	
Mpumalanga	Plantations (pulpwood and sawlogs)**	263	16,252	
Lomati Sawmill	Sawn timber (m ³)			102
Total Sappi Forests		516	27,588	102

Mills	Products produced	Capacity ⁽¹⁾ ('000 tons)	
		Paper	Pulp
Ngodwana Mill	Unbleached chemical pulp for own consumption		
	Mechanical pulp for own consumption		210
	Kraft linerboard		110
	Newsprint	240	
		140	
Stanger Mill	Bleached bagasse pulp for own consumption		60
	Office paper and tissue paper	110	
Tugela Mill	Neutral sulfite semi-chemical pulp for own consumption		150
	Corrugating medium	200	
Sappi ReFibre***	Waste paper collection and recycling for own consumption		140
Total Sappi Paper and Paper Packaging		690	670
Ngodwana Mill	Dissolving wood pulp		250
Saiccor Mill	Dissolving wood pulp		800
Total Sappi Specialised Cellulose			1,050
Total Sappi Southern Africa		690	1,720

⁽¹⁾ Capacity at maximum continuous run rate.

* Approximately 138,000 ha of our land is set aside and maintained by Sappi Forests to conserve the natural habitat and biodiversity found there.

** Plantations include owned and leased areas as well as contracted supply.

*** Sappi ReFibre collects waste paper in the South African market which is used to produce packaging papers.

Sappi Southern Africa Limited

(Incorporated in the Republic of South Africa)

Registration number 1951/003180/06

**Group Annual Financial Statements
Audited**

September 2018

Sappi Southern Africa Limited

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year ended September 2018

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Supervisor of the preparation of the annual financial statements

J Shaw CA (SA)

Sappi Southern Africa Limited


Directors' approval year ended September 2018

The directors are responsible for the maintenance of adequate accounting records and the content, integrity and fair presentation of the group annual financial statements and the related financial information included in this report. These have been prepared in accordance with International Financial Reporting Standards, the SAICA Financial Reporting Guides as issued by the Accounting Practices Committee, the Financial Reporting Pronouncements as issued by Financial Reporting Standards Council, the JSE Limited Debt Listings Requirements and the requirements of the Companies Act of South Africa. In preparing the group financial statements, appropriate accounting policies supported by reasonable judgments and estimates were applied. The auditors are responsible for auditing the group financial statements in the course of executing their statutory duties.

The directors acknowledge that they are ultimately responsible for the system of internal financial control established and are committed to maintaining a strong control environment. The directors are of the opinion that the system of internal control provides reasonable assurance that the financial records may be relied on for the preparation of the group financial statements. However, any system of internal financial control can provide only reasonable, and not absolute assurance against material misstatement or loss.

The directors have reviewed the group's budget and cash flow forecasts. This review, together with the group's financial position, existing borrowing facilities and cash on hand, have satisfied the directors that the group will continue as a going concern for the foreseeable future. The group, therefore, continue to adopt the going concern basis in the preparation of the group financial statements.

The directors' report and group annual financial statements appear on pages 8 to 60 and were approved by the board of directors on 28 January 2019 and signed on its behalf by:



A Thiel
Chief Executive Officer



P Moodley
Chief Financial Officer

Company secretary's certificate

In terms of section 88(2)(e) of the Companies Act 71 of 2008 of South Africa, I hereby certify that, to the best of my knowledge and belief, the company has lodged with the Companies and Intellectual Property Commission of South Africa, for the financial year ended September 2018, all such returns as are required of a public company in terms of this Act and that such returns appear to be true, correct and up to date.

Sappi Limited
Secretaries
per A Mahendranath
Group Secretary

28 January 2019



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Independent auditor's report

To the shareholders of Sappi Southern Africa Limited

Report on the audit of the consolidated financial statements

Opinion

We have audited the consolidated financial statements of Sappi Southern Africa Limited ("the Group") set out on pages 10 to 60, which comprise the Group balance sheet as at September 2018, and the Group income statement and the Group statement of comprehensive income, the Group statement of changes in equity and the Group statement of cash flows for the year then ended, and notes to the Group financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Sappi Southern Africa Limited as at September 2018, and its consolidated financial performance and consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the Companies Act of South Africa.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the Independent Regulatory Board for Auditors' *Code of Professional Conduct for Registered Auditors (IRBA Code)* and other independence requirements applicable to performing audits of financial statements in South Africa. We have fulfilled our other ethical responsibilities in accordance with the IRBA Code and in accordance with other ethical requirements applicable to performing audits in South Africa. The IRBA Code is consistent with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants (Parts A and B)*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

KPMG Inc. is a company incorporated under the South African Companies Act and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.

KPMG Inc. is a Registered Auditor, in public practice, in terms of the Auditing Profession Act, 26 of 2005.

Registration number 1999/021543/21

Executive Chairman: Prof Wiseman Nkuhlu

Directors: Full list on website

The company's principal place of business is at KPMG Crescent,

85 Empire Road, Parktown, where a list of the directors' names is available for inspection.

The key audit matter	How the matter was addressed in our audit
Valuation of plantations	
<p>Refer to note 2.3.4 for the accounting policies applied and note 7 to the Group financial statements.</p> <p>Plantations are valued in terms of IAS 41, <i>Agriculture</i> and are stated at fair value less cost to sell at the harvesting stage, using the income approach, and is a level 3 measure in terms of IFRS 13, <i>Fair Value Measurement</i>.</p> <p>The valuation of plantations requires complex measurements and involves estimation uncertainty. The key measurement and assumptions having the most significant impact on the fair value of the plantations include:</p> <ul style="list-style-type: none"> • Estimated prices less cost of delivery; • Volume and growth estimates; • Cost assumptions; and • Discount rate. <p>Given the complexity and the significant amount of estimation and judgement involved in the determination of fair value of the plantations, this matter was considered a key audit matter.</p>	<p>Our audit procedures related to the valuation of plantations included, amongst others:</p> <ul style="list-style-type: none"> • Critically evaluating the fair value methodology against the criteria in IAS 41, <i>Agriculture</i> and IFRS 13, <i>Fair Value Measurement</i>, measurements and key assumptions applied by management in determining the fair value of the plantations. This was performed by our valuation specialists, that formed part of the audit team, by applying their knowledge of the industry to assess the appropriateness of the valuations; • Challenging the consistency and appropriateness of the underlying measurements and assumptions used by comparing to external observable data, where possible, and considering management's historical accuracy in determining these measurements and estimations; and • Assessing the reasonableness of the Group's fair value estimates, and the related sensitivity disclosures, by performing our own sensitivity analysis of the plantation valuations. <p>We considered the adequacy and appropriateness of the Group's disclosures on the valuation of plantations.</p>
Taxation	
<p>Refer to note 2.3.3 for the accounting policies applied and notes 5 and 21 to the Group financial statements.</p> <p>The Group has entities in a number of local geographical locations which transact with off-shore operations. The various Group entities are subject to examination by tax authorities, the outcome of which cannot be predicted with certainty, giving rise to complexity in the accounting for the Group's taxation.</p> <p>Given the complexity and judgement involved in the accounting for taxation, this matter was considered a key audit matter.</p>	<p>We involved our tax specialists, with local and international tax knowledge, who formed part of the audit team.</p> <p>Our audit procedures included an assessment of the Group's taxation assets and liabilities with particular consideration given to the judgements applied by management in accounting for uncertain tax positions. This more specifically included:</p> <ul style="list-style-type: none"> • Evaluating the Group's assessment of its exposure to tax risks and accounting for related uncertain tax positions. We also reviewed correspondence with tax authorities in this regard to support the Group's assessments made. <p>We considered the adequacy and appropriateness of the Group's taxation disclosures in the consolidated financial statements.</p>





Other information

The directors are responsible for the other information. The other information comprises the Company secretary's certificate, the Directors' report as required by the Companies Act of South Africa, the Directors' approval and Annexure A: Definitions. Other information does not include the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express an audit opinion or any form of assurance conclusion thereon.

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

Responsibilities of the directors for the consolidated financial statements

The directors are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards and the requirements of the Companies Act of South Africa, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the consolidated financial statements

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

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control;
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors;





- conclude on the appropriateness of the directors' use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation; and
- obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the directors, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and, therefore, are the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

In terms of the IRBA Rule published in Government Gazette Number 39475 dated 4 December 2015, we report that KPMG Inc. has been the auditor of Sappi Southern Africa Limited for two years.

KPMG Inc.

Per Safeera Loonat
Chartered Accountant (SA)
Registered Auditor
Director
29 January 2019

Sappi Southern Africa Limited

Director's report year ended September 2018

The directors submit their report for the year ended September 2018.

Sappi Southern Africa Limited's consolidated financial statements has been audited in compliance with the applicable requirements of the Companies Act of South Africa.

Business of Sappi Southern Africa Limited ("Sappi Southern Africa" or "the company") and its operating companies ("Group")

The company is based in South Africa and produces dissolving wood pulp (DWP), paper grade pulp, paper and wood products for use in the Southern Africa and export markets.

Sappi Southern Africa overview

The Sappi Group is one of the world's largest manufacturer of DWP and exports almost all of the 1050 000 tons produced by Sappi Southern Africa at the Saiccor and Ngodwana Mills. When converted to viscose staple fibre (VSF), DWP is a natural substitute in many applications for cotton and polyester and this is used in the manufacture of a wide range of consumer products, including in textiles for fashion clothing and household linen. DWP can also be processed into products used in food and beverages, health and hygiene products, wrapping and packaging, pharmaceuticals and many more applications that touch our daily lives.

The South African paper business produces 690 000 tons of kraft linerboard, corrugating medium, newsprint, office paper and tissue paper which are largely sold regionally, where we have strong market positions in most of these products.

We also produce 470 000 tons of paper pulp and collect 140 000 tons of recycled waste paper. On a net basis we are approximately self-sufficient for our pulp requirements.

Sappi Southern Africa owns or leases 378,000 hectares (ha) with approximately 27.5 million tons of standing timber and 138,000ha being used for other purposes such as conservation. Contracted supply covers almost 92,000ha. Of the 236,000ha planted at the end of FY2018, 59% was hardwood and 41% softwood, and of contracted supply, 93% is hardwood. These plantations provide approximately 57% of the wood requirements for the Southern Africa mills. Our aim is to produce low-cost wood with the required pulping characteristics and increase yield per hectare. We actively pursue this aim, particularly through genetic improvement of planting stock.

Markets and operations

Growing demand for DWP, constrained cotton supply, and good customer operating rates continue to support our dissolving wood pulp business. Demand for VSF, and therefore DWP, continued to be linked to the growth in the overall textile market. Sappi Southern Africa's sales volumes in 2018 were flat year on year following the late start up at Saiccor and Ngodwana Mill, after plant upgrades. The US Dollar spot prices for DWP increased year on year by approximately 1% to the current level of US\$922/ton.

The average rate of the ZAR strengthened by 2% to the US Dollar for the year, and had a significant negative impact on the company's results. Although there were higher selling prices and strong local market conditions, it was not sufficient to negate the effect of the stronger R/US\$.

The cost of imported variable cost items increased significantly in local currency terms and the usage savings generated on chemical and pulp could not help offset the impact of the increased cost. Fixed cost increased by 9% year-on-year mainly due to higher manpower and maintenance cost.

The net result of the above is a Rand annual operating profit of ZAR3 293 million.

Sappi Southern Africa's sales for 2018 in Rand terms remained flat year on year, R17 867 million compared to 2017 (R17 839 million).

Sappi Southern Africa's EBITDA reduced to R4 167 million in 2018 from R4 831 million in 2017, while the EBITDA margin declined to 23% from the prior year's 27% margin. Operating profit decreased to R3 293 million in 2018 (R4 048 million in 2017). In 2018 Sappi Southern Africa achieved a 15% "Return on Net Operating Assets", compared to the 21% it achieved in 2017.

We regard ownership of our plantations as a key strategic resource which gives us access to low cost fibre for our pulp production and ensures continuity of an important raw material input source. As we manage our plantations on a sustainable basis, the growth in plantations over the year was largely offset by fellings in the year. A positive fair value price adjustment of R352 million was recorded in fiscal 2018 due mainly to the rolling forward of the higher average fair value rates offset by higher fuel and contractor costs.

Regrettably the company reported the fatality of one contractor in our forestry business during the past financial year. Management and the Sappi Group board have placed even greater emphasis on safety, particularly in our plantation operations where most of our severe and fatal accidents have occurred. We will continue to focus on entrenching a strong safety culture, with the ultimate aim of zero accidents in the workplace.

We have a strong focus on social responsibility in South Africa, which is an economic imperative in the region. Our plantations and most of our mills are located in rural areas and we therefore have an important influence on development in these areas. We continue to make progress on each of the elements of our Black Economic Empowerment scorecard.

Going concern

The directors believe that the Group has sufficient resources and expected cash flows to continue as a going concern for the next financial year.

Subsequent events

In January 2019 Sappi Southern Africa Limited funded R1.36 billion to Sappi Limited as per a loan agreement. This was done to enable Sappi Limited to pay dividends that were declared.

Sappi Southern Africa Limited

Director's report year ended September 2018

Outlook

Market prices for DWP are determined by a number of factors. Approximately a quarter of current DWP capacity has the ability to switch between various fluff and paper pulp grades and DWP. The decision to switch is usually based on the pricing differential between the particular paper grade pulp and DWP. Textile prices also influence DWP prices as this determines the maximum affordable price our customers can bear. Lastly, the DWP supply and demand balance as well as the availability and pricing of alternative sources of cellulose to the VSF market, such as cotton linter pulp, can affect the market price for dissolving wood pulp.

Based on the growth rate in the overall textile market (driven by factors such as population growth and wealth effects) and the move towards more comfortable, environmentally friendly natural fibres, we expect long-term growth of 4-5% per annum for DWP. Forecast growth is largely driven by growth rates in the viscose staple fibre (VSF) segment

In the containerboard market in Southern Africa, a strong fruit and vegetable season boosted sales. Most of Sappi's containerboard sales are into the agricultural market, which is expected to grow by 3% per annum going forward.

Reporting period

The Group's financial period ends on the Sunday closest to the last day of September and results are reported as if at the last day of September

Share Capital

There were no changes in the authorised share capital during the financial year.

Authorised

6 052 500	Ordinary shares of R2 each
19 520	Class "A" cumulative non-convertible redeemable preference shares of R0.01 each with a variable coupon rate
221 107	Class "B" cumulative non-convertible redeemable preference shares of R0.01 each with a variable coupon rate
831	Class "C" cumulative non-convertible redeemable preference shares of R0.01 each with a variable coupon rate
123 321	Class "D" cumulative non-convertible redeemable preference shares of R0.01 each with a variable coupon rate

Issued

6 015 769	Ordinary shares of R2 each
19 520	Class "A" cumulative non-convertible redeemable preference shares of R0.01 each with a variable coupon rate
219 760	Class "B" cumulative non-convertible redeemable preference shares of R0.01 each with a variable coupon rate
831	Class "C" cumulative non-convertible redeemable preference shares of R0.01 each with a variable coupon rate
120 018	Class "D" cumulative non-convertible redeemable preference shares of R0.01 each with a variable coupon rate

Financing

At year end, the average tenure of the company's debt is 2.0 years .

Sappi Southern Africa Limited currently has the following credit ratings:

- Global Credit Rating (GCR): South African national rating A+(za)/A1+ (za)/Positive Outlook (May 2018).

Net borrowings

Sappi Southern Africa has sufficient cash to meet all its debt obligations . Details of the non-current term borrowings are set out in note 16 of the annual financial statements.

Insurance

Sappi Southern Africa has an active programme of risk management to address and reduce exposure to property damage and business interruption. All production and distribution units are subjected to regular risk assessments by external risk engineering consultants, the results of which receive the attention of senior management. The risk mitigation programmes are coordinated at Sappi Group level in order to achieve a standardisation of methods. Work on improved enterprise risk management is on-going and aims to lower the risk of incurring losses from uncontrolled incidents.

Asset insurance is renewed on a calendar year basis. The self-insured retention portion for any one property damage occurrence is EUR 2: million with the annual aggregate set at EUR 33 million. For property damage and business interruption insurance, cost-effective cover to full value is not readily available. A loss limit cover of EUR 730 million has been deemed to be adequate for the reasonable foreseeable loss for any single claim. In addition to the Property damage and business interruption policies there is a full program of policies to mitigate the losses stemming from events not covered by the main global policy.

During 2018, no incidents occurred that resulted in a successful claim against the Group's property damage or business interruption insurance policies.

Fixed assets

Capital expenditure of R3 262 million was incurred during the year as per the cash flow statement. Capital expenditure is expected to increase significantly in 2019 as we proceed with the 110kt capacity increase of Dissolving Wood Pulp and the woodyard upgrade at our Saiccor Mill.

Sappi Southern Africa Limited

Director's report year ended September 2018

Litigation

We become involved from time to time in various claims and lawsuits incidental to the ordinary course of our business. We are not currently involved in legal proceedings which, either individually or in the aggregate, are expected to have a material adverse effect on our business assets or properties.

Audit and Risk Committee

The Sappi Southern Africa Limited group of companies (Group) is a major subsidiary of Sappi Limited (Sappi), a company that maintains its listing on the JSE Limited. Sappi complies in all material respects with the JSE listings requirements, regulations and codes. The Sappi Southern Africa Limited Audit Committee operates as a function of the Sappi Limited Audit Committee. The committee, in terms of the Companies Act of South Africa, and King code has the responsibility for reviewing the effectiveness of the Group's system of internal controls and risk management system. An internal audit function is responsible for advising the Board of Directors on the effectiveness of the Group's risk management system. For further information on Sappi's application of the King Code please refer to the Sappi Ltd 2018 Integrated Annual Report

The committee oversees the relationship with the external auditors; is responsible for their appointment and remuneration; reviews the effectiveness of the external audit process; and ensures that the objectivity and independence of the external auditors is maintained. The committee has concluded that it is satisfied that the auditor independence and objectivity has been maintained. The comprehensive report of the committee is included in the Group annual report.

Company secretary

The company secretary does not fulfil executive management functions outside of the duties of company secretary and is not a director. During the year, the board has assessed the independence, competence, qualifications and experience of the company secretary and has concluded that she is sufficiently independent (i.e. maintained an arm's length relationship with the executive team, the board and individual directors), qualified, competent and experienced to hold this position. The company secretary is responsible for the duties set out in section 88 of the Companies Act 71 of 2008 (as amended) of South Africa. Specific responsibilities include providing guidance to directors on discharging their duties in the best interests of the group, informing directors of new laws affecting the group, as well as arranging for the induction of new directors.

Subsidiary companies

Details of the company's significant subsidiaries are given in note 30.

Directors	Appointed
Alex Thiel	1/12/2010
Pramy Moodley	1/1/2017
Steven Binnie	1/9/2012
Glen Pearce	1/7/2014

Registered office

108 Oxford Road
Houghton Estate
2198

Auditors

KPMG Inc

Holding company

Sappi Limited

Secretaries

Sappi Limited
108 Oxford Road
Houghton Estate 2198
South Africa
Telephone +27 (0) 11 407 8111
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e-Mail Ami.Mahendranath@sappi.com

Sappi Southern Africa Limited

Group income statement for the year ended September 2018

R'millions	Note	2018	2017
Sales		17,867	17,839
Cost of sales	3.1	14,040	13,156
Gross profit		3,827	4,683
Selling, general administrative and other expenses	3.1	578	723
Share of equity accounted investee, net of tax	9	(44)	(88)
Operating profit		3,293	4,048
Net finance income	4	(85)	(94)
Finance costs		128	134
Finance income		(180)	(152)
Net foreign exchange gains		(33)	(76)
Profit before taxation		3,378	4,142
Taxation charge	5	1,202	1,063
Profit for the year		2,176	3,079

Group statement of comprehensive income for the year ended September 2018

R'millions	Note	2018	2017
Profit for the year		2,176	3,079
Other comprehensive income (loss), net of tax	14	102	(98)
Item that will not be reclassified subsequently to profit or loss		14	(71)
Actuarial gains (losses) on post-employment benefit funds		19	(99)
Deferred tax on above item		(5)	28
Items that may be reclassified subsequently to profit or loss		88	(27)
Movement in hedging reserves		122	(36)
Tax on above items		(34)	9
Total comprehensive income for the year		2,278	2,981

Sappi Southern Africa Limited

Group balance sheet as at September 2018

R'millions	Note	2018	2017
ASSETS			
Non-current assets		24,660	17,336
Property, plant and equipment	6	13,080	10,634
Plantations	7	6,595	6,206
Equity accounted investee	9	161	194
Other non-current assets	10	393	302
Derivative financial instruments	25	54	-
Amounts owing by group companies	27	4,377	-
Current assets		5,913	10,098
Inventories	11	2,011	1,627
Trade and other receivables	12	610	347
Derivative financial instruments	25	123	21
Amounts owing by group companies	27	2,155	5,139
Prepaid taxes		-	41
Cash and cash equivalents		1,014	2,923
Total assets		30,573	27,434
EQUITY AND LIABILITIES			
Shareholders' equity		21,096	18,813
Ordinary share capital and share premium	13	221	221
Non-distributable reserves	15	157	152
Hedging reserves		93	5
Retained earnings		20,625	18,435
Non-current liabilities		5,395	5,036
Interest-bearing borrowings	16	1,145	1,145
Deferred tax liabilities	8	3,979	3,637
Other non-current liabilities	17	271	254
Current liabilities		4,082	3,585
Interest-bearing borrowings	16	-	500
Derivative financial instruments	25	80	20
Trade and other payables		3,675	2,842
Taxation payable		109	-
Amounts owing to group companies	27	218	223
Total equity and liabilities		30,573	27,434

Sappi Southern Africa Limited

Group statement of cash flows for the year ended September 2018

R'millions	Note	2018	2017
Cash retained from operating activities		2,745	3,515
Cash generated from operations	18.1	3,688	4,638
- Decrease (increase) in working capital	18.2	(293)	89
Cash generated from operating activities		3,395	4,727
- Finance costs paid	18.3	(79)	(70)
- Finance income received		179	161
- Taxation paid	18.4	(750)	(1,303)
Cash utilised in investing activities		(4,154)	(4,437)
Investment to maintain operations		(1,327)	(710)
Investment to expand operations		(1,935)	(622)
Proceeds on disposal of other non-current assets	18.5	144	16
Increase in amounts owing by group companies		(1,066)	(3,208)
Other decrease in non-current assets		30	87
Cash effects of financing activities		(500)	-
Repayment of interest-bearing borrowings		(500)	-
Net movement in cash and cash equivalents		(1,909)	(922)
Cash and cash equivalents at beginning of year		2,923	3,845
Cash and cash equivalents at end of year		1,014	2,923

Sappi Southern Africa Limited
Group Statement of Changes in Equity
for the year ended September 2018

R'millions	Ordinary share		Ordinary share	Non-distributable		Retained earnings	Total equity
	capital	Share premium	capital and share premium	reserves	Hedging reserves		
Balance - September 2016	12	209	221	151	32	15,427	15,831
Share-based payments	-	-	-	28	-	-	28
Sappi Limited Share Incentive Trust	-	-	-	(41)	-	-	(41)
Share-based payments	-	-	-	14	-	-	14
Other comprehensive income for the year	-	-	-	-	(27)	(71)	(98)
Profit for the year	-	-	-	-	-	3,079	3,079
Balance - September 2017	12	209	221	152	5	18,435	18,813
Share-based payments	-	-	-	37	-	-	37
Sappi Limited Share Incentive Trust	-	-	-	(45)	-	-	(45)
Share-based payments	-	-	-	13	-	-	13
Other comprehensive income for the year	-	-	-	-	88	14	102
Profit for the year	-	-	-	-	-	2,176	2,176
Balance - September 2018	12	209	221	157	93	20,625	21,096
<i>Note</i>			<i>13</i>	<i>15</i>			

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements for the year ended September 2018

1.1 Basis of preparation

The consolidated financial statements of Sappi Southern Africa (the 'Company') as at and for the year ended September 2018 comprise the Company and its subsidiaries (together referred to as the 'Group' and individually as 'Group entities' or 'Group entity') as well as the group's interests in associates and joint ventures.

The group annual financial statements were approved by the board of directors on 28 January 2019

The consolidated financial statements (the Group Annual Financial Statements) have been prepared in accordance with:

- International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB),
- the SAICA Financial Reporting Guides as issued by the Accounting Practices Committee,
- Financial Reporting Pronouncements as issued by Financial Reporting Standards Council,
- the Debt Listings Requirements of the JSE Limited, and
- the requirements of the Companies Act 2008 of South Africa.

The Group Annual Financial Statements are prepared on the historical cost basis, except as set out in the accounting policies which follow. Certain items, including derivatives, are stated at their fair value while plantations are stated at fair value less costs to sell.

Fair value is determined in accordance with IFRS 13 *Fair Value Measurement* and is categorised as follows:

- Level 1: Quoted prices in active markets for identical assets or liabilities,
- Level 2: Inputs other than quoted prices that are observable, either directly or indirectly, and
- Level 3: Inputs for the asset or liability that are unobservable.

Transfers between fair value hierarchies are recorded when that change occurs.

The Group Annual Financial Statements are presented in South African Rands (ZAR), which is the functional currency of the Sappi Southern Africa Ltd and is rounded to the nearest million except as otherwise indicated.

The preparation of the Group Annual Financial Statements was supervised by J Shaw CA(SA)

The group's financial year-end is on the Sunday closest to the last day of September. Accordingly, the last two financial years were as follows:

- 02 October 2017 to 30 September 2018 (52 weeks)
- 26 September 2016 to 01 October 2017 (53 weeks)
- 28 September 2015 to 25 September 2016 (52 weeks)

The Group Annual Financial Statements are prepared on the going concern basis.

Assets and liabilities and, income and expenses are not offset in the income statement or balance sheet unless specifically permitted by IFRS.

2. Accounting policies

The following principal accounting policies have been consistently applied in dealing with items that are considered material in relation to the group annual financial statements. Adoption of new accounting standards and changes to accounting standards are dealt with in sections 2.4 and 2.5.

Changes in accounting estimates are recognised prospectively in profit or loss, except to the extent that they give rise to changes in the carrying amount of recognised assets and liabilities where the change in estimate is recognised immediately.

2.1 Significant accounting policy elections

The group has made the following significant accounting policy elections in terms of IFRS:

- regular way purchases or sales of financial assets are recognised and derecognised using trade date accounting,
- cumulative gains or losses recognised in other comprehensive income (OCI) for cash flow hedge relationships are transferred from equity and included in the initial measurement of the non-financial asset or liability when the hedged item is recognised,
- the net interest on post-employment benefits is included in finance costs, and
- property, plant and equipment is accounted for using the cost model

The elections are explained further in each specific policy in sections 2.2 and 2.3.

2.2 Summary of accounting policies

2.2.1 Foreign currencies

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the date of each transaction. Subsequent to initial recognition, monetary assets and liabilities denominated in foreign currencies are translated at the earlier of reporting or settlement date and the resulting foreign currency exchange gains or losses are recognised in profit or loss for the period. Translation differences on available-for-sale financial instruments are included in OCI.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting policies

2.2 Summary of accounting policies (continued)

2.2.2 Group accounting

(i) Subsidiaries

An entity is consolidated when the group can demonstrate power over the investee, is exposed or has rights to variable returns from its involvement with an investee and has the ability to affect those returns through its power over the investee. The financial results of subsidiaries are consolidated into the group's results from acquisition date until disposal date.

Intra-group balances and transactions and, profits or losses arising from intra-group transactions are eliminated in the preparation of the group annual financial statements.

(ii) Equity accounted investees

The financial results of associates and joint ventures are incorporated in the group's results using the equity method of accounting from acquisition date until disposal date. Under the equity method, associates and joint ventures are carried at cost and adjusted for the post-acquisition changes in the group's share of the associates' and joint ventures' net assets. The share of the associates' or joint ventures' profit after tax is determined from their latest financial statements or, if their year-ends are different to those of the group, from their unaudited management accounts that correspond to the group's financial year-end.

Where there are indicators of impairment, the entire carrying amount of the investment (including goodwill) is tested for impairment as a single asset by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount. Any impairment loss recognised, which the group records in other operating expenses in profit or loss, is deducted from the carrying amount of the investment. Any reversal of an impairment loss increases the carrying amount of the investment to the extent recoverable, but not higher than the historical amount.

2.2.3 Financial instruments

(i) Initial recognition

Financial instruments are recognised on the balance sheet when the group becomes a party to the contractual provisions of a financial instrument. All purchases of financial assets that require delivery within the time frame established by regulation or market convention ('regular way' purchases) are recognised at trade date.

(ii) Initial measurement

All financial instruments are initially recognised at fair value, including transaction costs that are incremental to the group and directly attributable to the acquisition or issue of the financial asset or financial liability, except for those classified as fair value through profit or loss where the transaction costs are recognised immediately in profit or loss.

(iii) Subsequent measurement

- Financial assets and financial liabilities at fair value through profit or loss

Financial instruments at fair value through profit or loss consist of items classified as held for trading or where they have been designated as fair value through profit or loss. All derivative instruments are classified as held for trading other than those which are designated and effective hedging instruments.

- Financial liabilities at amortised cost

All financial liabilities, other than those at fair value through profit or loss, are classified as financial liabilities at amortised cost.

- Loans and receivables

Loans and receivables are carried at amortised cost.

- Available-for-sale financial assets

Available-for-sale financial assets are measured at fair value with any gains or losses recognised directly in equity along with the associated deferred taxation. Any foreign currency translation gains or losses or interest revenue, measured on an effective-yield basis, are recognised in profit or loss.

(iv) Embedded derivatives

Certain derivatives embedded in financial and host contracts are treated as separate derivatives and recognised on a standalone basis when their risks and characteristics are not closely related to those of the host contract and the host contract is not carried at fair value. Gains or losses on these embedded derivatives are reported in profit or loss.

(v) Derecognition

The group derecognises a financial asset when the rights to receive cash flows from the asset have expired or have been transferred and the group has transferred substantially all risks and rewards of ownership.

A financial liability is derecognised when and only when the liability is extinguished, ie when the obligation specified in the contract is discharged, cancelled or has expired. The difference in the respective carrying amounts is recognised in profit or loss for the period.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting policies

2.2 Summary of accounting policies

2.2.3 Financial Instruments (continued)

(vi) Impairment of financial assets

- Loans and receivables

An impairment loss is recognised in profit or loss when there is evidence that the group will not be able to collect an amount in accordance with the original terms of each receivable.

- Available-for-sale financial assets

When there is objective evidence that an available-for-sale financial asset is impaired, the cumulative unrealised gains or losses recognised in equity (to the extent of any remeasurements) are reclassified to profit or loss even though the financial asset has not been derecognised.

Impairment losses are only reversed in a subsequent period if the fair value increases due to an objective event occurring since the loss was recognised. Impairment reversals other than available-for-sale debt securities are not reversed through profit or loss but through OCI.

(vii) Finance income and finance costs

Finance income and finance costs are recognised in profit or loss using the effective interest rate method. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial asset or financial liability to that asset's or liability's net carrying amount on initial recognition.

2.2.4 Government grants

Government grants related to income are recognised in sundry income under selling, general and administrative expenses. Government grants related to assets are recognised by deducting the grant from the carrying amount of the related asset.

2.2.5 Intangible assets

(i) Research activities

Expenditures on research activities and internally generated goodwill are recognised in profit or loss as an expense as incurred.

(ii) Development activities

Intangible assets are stated at cost less accumulated amortisation and impairment losses. Amortisation of engineering projects, computer software and development costs is charged to profit or loss on a straight-line basis over the estimated useful lives of these assets, not exceeding five years.

(iii) Brands and patents

Brands, customer relationships and customer technology acquired are capitalised and amortised on a straight-line basis over their estimated useful lives which, on average, is ten years.

(iv) Other intangible assets

Other intangible assets comprise license fees, trademarks and carbon certificates which are amortised on a straight-line basis over their useful lives between 3 and 20 years.

2.2.6 Inventories

Inventories are stated at the lower of cost or net realisable value. Cost includes all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Cost is determined on the following basis:

Classification	Cost formula
Finished goods	First in first out (FIFO)
Raw materials, work in progress and consumable stores	Weighted average
Cost of items that are not interchangeable	Specific identification inventory valuation basis

Net realisable value is the estimated selling price in the ordinary course of business less necessary costs to make the sale.

2.2.7 Leases

Finance leases are capitalised at the inception of the lease at the lower of the fair value of the leased asset or the present value of the minimum lease payments with the related lease obligation recognised at the same value. Lease payments are allocated between capital repayments and finance charges using the effective interest rate method.

Capitalised leased assets are depreciated on a basis consistent with those of owned assets except, where the transfer of ownership at the end of the lease period is uncertain, they are depreciated on a straight-line basis over the shorter of the lease period and the expected useful life of the asset.

Lease payments made under operating leases are charged to profit or loss on a straight-line basis over the term of the lease unless another systematic basis is more representative of the time pattern of the group's benefit.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting policies

2.2 Summary of accounting policies (continued)

2.2.8 Assets held for sale

Non-current assets (or disposal groups) are classified as held for sale when their carrying values will be recovered principally through a sale rather than through continuing use. Non-current assets classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell and are not depreciated.

2.2.9 Borrowing costs

Borrowing costs directly attributable to the acquisition, construction and production of qualifying assets are capitalised as part of the costs of those assets.

Borrowing costs capitalised are calculated at the group's average funding cost other than to the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset. Where this occurs, actual borrowing costs incurred less any investment income on the temporary investment of those borrowings are capitalised.

2.2.10 Revenue

Revenue arising from the sale of goods is recognised when the significant risks and rewards of ownership have been transferred, delivery has been made and title has passed, the amount of the revenue and the related costs can be reliably measured and it is probable that the debtor will pay for the goods. For the majority of local and regional sales, transfer occurs at the point of offloading the shipment into the customer warehouse whereas for the majority of export sales, transfer occurs when the goods have been loaded into the relevant carrier unless the contract of sale specifies different terms.

Revenue is measured at the fair value of the amount received or receivable and after the deduction of trade and settlement discounts, rebates and customer returns.

Shipping and handling costs, such as freight to the group's customers' destinations, are included in cost of sales.

2.2.11 Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, deposits and money market instruments with a maturity of three months or less and other short-term highly liquid investments that are readily convertible into cash.

2.2.12 Goodwill

The acquisition of subsidiaries is accounted for using the acquisition method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the group in exchange for control of the acquiree. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition are recognised at their fair value at the acquisition date.

Goodwill arising at acquisition is subsequently held at cost less any accumulated impairment losses. Goodwill is tested for impairment annually or more frequently where there is an indication of impairment within one or more cash-generating units (CGUs) to which goodwill has been allocated.

Goodwill is tested for impairment using a cash flow valuation model based on an allocation of the goodwill to one or more CGUs. The group takes into account its ability to produce products across different operating units in determining CGUs and in allocating goodwill to those CGUs.

2.2.13 Share-based payments

(i) Equity-settled share-based payment transactions

The services or goods received in an equity-settled share-based payment transaction with counterparties are measured at the fair value of the equity instruments at grant date.

If the equity instruments granted vest immediately and the beneficiary is not required to complete a specified period of service before becoming unconditionally entitled to those instruments, the benefit received is recognised in profit or loss for the period in full on grant date with a corresponding increase in equity.

Where the equity instruments do not vest until the beneficiary has completed a specified period of service, it is assumed that the benefit received by the group as consideration for those equity instruments will be received over the vesting period. These benefits are accounted for in profit or loss as they are received with a corresponding increase in equity. Share-based payment expenses are adjusted to reflect the number of awards for which the related service and non-market performance conditions are expected to be met.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting Policies

2.2 Summary of accounting policies

2.2.13 Share-based payments (continued)

(ii) Measurement of fair value of equity instruments granted

The equity instruments granted by the group are measured at fair value at the measurement date using either the modified binomial option pricing and the Monte-Carlo simulation model. The valuation technique is consistent with generally acceptable valuation methodologies for pricing financial instruments and incorporates all factors and assumptions that knowledgeable, willing market participants would consider in setting the price of the equity instruments.

(iii) Broad-based Black Economic Empowerment transaction

The group accounts for the transaction in accordance with IFRS 2 *Share-based payment* and the South African Institute of Chartered Accountants Financial Reporting Guide 2 as issued by the Accounting Practices Committee and the fair value of the services rendered by employees are recorded in profit or loss as they are rendered during the service period.

In accounting for the group's share-based payment transactions, management uses estimates and assumptions to determine share-based payment expenses. Key inputs, which are necessary in determining the grant date fair value, include the volatility of the group's share price, employee turnover rate, and dividend payout rates.

Note 25 provides further detail on key estimates, assumptions and other information on share-based payments applicable as at the end of the year.

2.2.14 Derivatives and hedge accounting

For the purpose of hedge accounting, hedges are classified as follows:

(i) Fair value hedges

Fair value hedges are designated when hedging the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment. Changes in the fair value of derivatives that are designated as hedging instruments are recognised in profit or loss immediately together with any changes in the fair value of the hedged item that are attributable to the hedged risk. The change in the fair value of the hedging instrument is recognised in the same line of profit or loss as the change in the hedged item.

(ii) Cash flow hedges

Cash flow hedges are designated when hedging the exposure to variability in cash flows that are either attributable to a particular risk associated with a recognised asset or liability, a highly probable forecast transaction, or the foreign currency risk in an unrecognised firm commitment. In relation to cash flow hedges which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised in OCI and the ineffective portion is recognised in profit or loss.

The gains or losses recognised in OCI are transferred to profit or loss in the same period in which the hedged transaction affects profit or loss.

If the forecasted transaction results in the recognition of a non-financial asset or non-financial liability, the associated cumulative gain or loss is transferred from OCI to the underlying asset or liability on the transaction date.

(iii) Discontinuance of hedge accounting

Hedge accounting is discontinued on a prospective basis when the hedge no longer meets the hedge accounting criteria (including when it becomes ineffective), when the hedge instrument is sold, terminated or exercised and when, for cash flow hedges, the designation is revoked and the forecast transaction is no longer expected to occur. Where a forecasted transaction is no longer expected to occur, the cumulative gain or loss deferred in OCI is transferred to profit or loss.

The financial instruments that are used in hedging transactions are assessed both at inception and quarterly thereafter to ensure they are effective in offsetting changes in either the fair value or cash flows of the related underlying exposures. Hedge ineffectiveness is recognised immediately in profit or loss.

Refer to notes 26 and 27 for details of the fair value hedging relationships as well as the impact of the hedge on the pre-tax profit or loss for the period.

2.2.15 Provisions

A provision is recognised when the group has a legal or constructive obligation arising from a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and which can be reliably measured. Where the effect of discounting (time value) is material, provisions are discounted and the discount rate used is a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

The establishment and review of the provisions requires significant judgement by management as to whether or not there is a probable obligation and as to whether or not a reliable estimate of the amount of the obligation can be made.

Restructuring provisions are recognised when the group has developed a detailed formal plan for restructuring and has raised a valid expectation that it will carry out the restructuring by starting to implement the plan or announcing its main features to those affected by it.

The measurement of a restructuring provision includes only the direct expenditures arising from the restructuring and is recorded in other operating expenses in profit or loss.

2.2.16 Environmental restoration and decommissioning obligations

The group initially recognises a liability for management's best present value estimate of costs expected to be incurred in the dismantling and removal of non-current assets where a legal or constructive obligation exists. The liability changes over time and actual costs incurred in future periods could differ materially from estimates. Additionally, future changes to environmental laws and regulations, life-of-operation estimates and discount rates could affect the carrying amount of this liability.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting Policies

2.2 Summary of accounting policies

2.2.16 Environmental restoration and decommissioning obligations (continued)

Due to the uncertainty in the timing of the closure of the group's facilities, some of these obligations have an indeterminate settlement date, and the group believes that adequate information does not exist to apply an expected present value technique to estimate any such potential obligations. Accordingly, the group does not record a liability for such remediation until a decision is made that allows reasonable estimation of the timing of such remediation.

2.2.17 Short-term employee benefits

Short-term employee benefits are expensed as the related service is provided. A liability is recognised for the amount expected to be paid if the group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

2.3 Critical accounting policies and key sources of estimation uncertainty

2.3.1 Impairment of assets other than goodwill and financial instruments

The group assesses all assets other than goodwill and financial instruments at each balance sheet date for indications of impairment or whether an impairment reversal is required.

In assessing assets for impairment, the group estimates the asset's useful life, discounted future cash flows, including appropriate bases for future product pricing in the appropriate markets, raw material and energy costs, volumes of product sold, the planned use of machinery or equipment or closing of facilities. The pre-tax discount rate (impairment discount factor) is another sensitive input to the calculation. For an asset whose cash flows are largely dependent on those of other assets, the recoverable amount is determined for the CGU to which the asset belongs. Additionally, assets are also assessed against their fair value less costs to sell.

Where impairment exists, the losses are recognised in other operating expenses in profit or loss for the period.

A previously recognised impairment loss will be reversed through profit or loss if the recoverable amount increases as a result of a change in the estimates that were previously used to determine the recoverable amount, but not to an amount higher than the carrying amount that would have been determined, net of depreciation or amortisation, had no impairment loss been recognised in prior periods.

2.3.2 Property, plant and equipment

Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Cost includes, where specifically required in terms of legislative requirements or where a constructive obligation exists, the estimated cost of dismantling and removing the assets, professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the group's accounting policy. In addition, spare parts whose expected useful lives are anticipated to be more than 12 months are treated as property, plant and equipment.

Expenditure incurred to replace a component of property, plant and equipment is capitalised to the cost of related property, plant and equipment and the part replaced is derecognised.

Depreciation, which commences when the assets are ready for their intended use, is recognised in profit or loss over their estimated useful lives to estimated residual values using a method that reflects the pattern in which the asset's future economic benefits are expected to be consumed by the entity. Land is not depreciated.

Management judgement and assumptions are necessary in estimating the methods of depreciation, useful lives and residual values. The residual value for the majority of items of property, plant and equipment has been deemed to be zero by management due to the underlying nature of the property, plant and equipment.

The following methods and rates are used to depreciate property, plant and equipment to estimated residual values:

Buildings	straight-line	10 to 40 years
Plant and equipment	straight-line	3 to 30 years

The group reassesses the estimated useful lives and residual values of components of property, plant and equipment on an ongoing basis. As a result, depending on economic and other circumstances, a component of property, plant and equipment could exceed the estimated useful life as indicated in the categories above.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting policies

2.3 Critical accounting policies (continued)

2.3.3 Taxation

Taxation on the profit or loss for the year comprises current and deferred taxation. Taxation is recognised in profit or loss except to the extent that it relates to items recognised directly in OCI, in which case it is also recognised in OCI.

(i) Current taxation

Current taxation is the expected taxation payable on the taxable income, which is based on the results for the period after taking into account necessary adjustments, using taxation rates enacted or substantively enacted at the balance sheet date, and any adjustment to taxation payable in respect of previous years.

The group estimates its income taxes in each of the jurisdictions in which it operates. This process involves estimating its current tax liability together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes.

The various group entities are subject to examination by tax authorities. The outcome of tax audits cannot be predicted with certainty. If any matters addressed in these tax audits are resolved in a manner not consistent with management's expectations or tax positions taken in previously filed tax returns, then the provision for income tax could be required to be adjusted in the period that such resolution occurs.

(ii) Deferred taxation

Deferred taxation is provided using the balance sheet liability method, based on temporary differences. The amount of deferred taxation provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities using taxation rates enacted or substantively enacted at the balance sheet date. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

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

Before recognising a deferred tax asset, the group assesses the likelihood that the deferred tax assets will be recovered from future taxable income and, to the extent recovery is not probable, a deferred tax asset is not recognised. In recognising deferred tax assets, the group considers profit forecasts, including the effect of exchange rate fluctuations on sales, external market conditions and restructuring plans.

(iii) Dividend withholding tax

Dividend withholding tax is payable on dividends distributed to certain shareholders. This tax is not attributable to the company paying the dividend but is collected by the company and paid to the tax authorities on behalf of the shareholder. On receipt of a dividend, the dividend withholding tax is recognised as part of the current tax charge in the income statement in the period in which the dividend is received.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting policies

2.3 Critical accounting policies (continued)

2.3.4 Plantations

Plantations are stated at fair value less costs to sell at the harvesting stage and is a Level 3 measure in terms of the fair value measurement hierarchy as established by IFRS 13 Fair Value Measurement. The group uses the income approach in determining fair value as it believes that this method yields the most appropriate valuation.

In arriving at plantation fair values, the key assumptions are estimated prices less cost of delivery, discount rates, and volume and growth estimations. All changes in fair value are recognised in the period in which they arise.

The impact of changes in estimated prices, discount rates, and volume and growth assumptions may have on the calculated fair value and other key financial information on plantations is disclosed in note 7.

- *Estimated prices less cost of delivery*

The group uses a 12 quarter rolling historical average price to estimate the fair value of all immature timber and mature timber that is to be felled in more than 12 months from the reporting date. Twelve quarters is considered a reasonable period of time after taking the length of the growth cycle of the plantations into account. Expected future price trends and recent market transactions involving comparable plantations are also considered in estimating fair value.

Mature timber that is expected to be felled within 12 months from the end of the reporting period are valued using unadjusted current market prices. Such timber is expected to be used in the short term and consequently, current market prices are considered an appropriate reflection of fair value.

The fair value is derived by using the prices as explained above and reduced by the estimated cost of delivery. Cost of delivery includes all costs associated with getting the harvested agricultural produce to the market, including harvesting, loading, transport and allocated fixed overheads.

- *Discount rate*

The discount rate used is the applicable pre-tax discount rate.

- *Volume and growth estimations and cost assumptions*

The group focuses on good husbandry techniques which include ensuring that the rotation of plantations is met with adequate planting activities for future harvesting. The age threshold used for quantifying immature timber is dependent on the rotation period of the specific timber genus which varies between 5 and 18 years. In the Southern African region, softwood less than eight years and hardwood less than five years are classified as immature timber.

Trees are generally felled at the optimum age when ready for intended use. At the time the tree is felled, it is taken out of plantations and accounted for under inventory and reported as a depletion cost (fellings).

Depletion costs include the fair value of timber felled which is determined on the average method, plus amounts written off against standing timber to cover loss or damage caused by fire, disease and stunted growth. These costs are accounted for on a cost per metric tonne allocation method multiplied by unadjusted current market prices. Tonnes are calculated using the projected growth to rotation age and are extrapolated to current age on a straight-line basis.

The group has projected growth estimation over a period of 5 to 18 years per rotation. In deriving this estimate, the group established a long-term sample plot network which is representative of the species and sites on which trees are grown and the measured data from these permanent sample plots were used as input into the group's growth estimation. Periodic adjustments are made to existing models for new genetic material.

The group directly manages plantations established on land that is either owned or leased from third parties. Indirectly managed plantations represent plantations established on land held by independent commercial farmers where Sappi provides technical advice on the growing and tendering of trees.

The associated costs for managing plantations are recognised as silviculture costs in cost of sales (see note 3).

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting policies

2.3 Critical accounting policies (continued)

2.3.5 Post-employment benefits

Defined benefit and defined contribution plans have been established for eligible employees of the group, with the assets held in separate trustee-administered funds.

The present value of the defined benefit obligations and related current service costs are calculated annually by independent actuaries using the projected unit credit method.

These actuarial models use an attribution approach that generally spread individual events over the service lives of the employees in the plan.

Estimates and assumptions used in the actuarial models include the discount rate, return on assets, salary increases, healthcare cost trends, longevity and service lives of employees.

The group's policy is to recognise actuarial gains or losses, which can arise from differences between expected and actual outcomes or changes in actuarial assumptions, in OCI. Any increase in the present value of plan liabilities expected to arise due to current service costs is charged to profit or loss.

Gains or losses on the curtailment or settlement of a defined benefit plan are recognised in profit or loss when the group is demonstrably committed to the curtailment or settlement. Past service costs or credits are recognised immediately.

Net interest for the period is determined by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period, adjusted for any changes as a result of contributions and benefit payments, to the net defined benefit liability and recorded in finance costs in profit or loss.

The net liability recognised in the balance sheet represents the present value of the defined benefit obligation reduced by the fair value of the plan assets. Where the calculation results in a benefit to the group, the recognised asset is limited to the present value of any future refunds from the plan or reductions in future contributions to the plan.

Refer to note 22 for the key estimates, assumptions and other information on post-employment benefits.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

2. Accounting policies (continued)

2.4 Adoption of accounting standards in the current year

The group adopted the following standards, interpretations, amendments and improvements to standards in the current fiscal year, all of which had no material impact on the group's reported results or financial position:

- IAS 12 - Income Taxes - Recognition of Deferred Tax Assets for Unrealised Losses
- IAS 7 Statement of Cash Flows – Disclosure Initiative – clarifies that entities shall provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities
- Annual Improvements 2014-2016 Cycle

2.5 Accounting standards, interpretations and amendments to existing standards that are not yet effective

Certain new standards, amendments and interpretations to existing standards have been published but which are not yet effective and which have not yet been adopted by the group. The impact of these standards is still being evaluated by the group.

- IFRS 9 Financial Instruments – IFRS 9 introduces new requirements for classifying and measuring financial assets and liabilities - October 2018. Management has implemented and concluded a project to assess the revised classification and measurement impact of this standard. IFRS 9 has set out a new classification and measurement approach for financial assets that reflect the business model in which the assets are managed and their cash flow characteristics. The three principal classification categories for financial assets are: measured at amortised cost, fair value through profit and loss and fair value through other comprehensive income (FVOCI). Based on management's assessment, the new classification will not have a significant impact compared to the current accounting for financial assets in terms of IAS 39. IFRS 9 replaces the 'incurred loss' model in IAS 39 with the forward looking 'expected credit loss' (ECL) model. The group will apply the practical expedient in IFRS 9 to calculate the ECL on trade receivables using a provision matrix. Based on management's assessment, application of the ECL model will not result in a material impact compared to the current accounting in terms of IAS 39. With respect to hedging, on transition a new class of non-distributable equity reserve will be created called Cost of hedging reserve. This reserve will be used to separate all time value of money and forward point valuations on hedged instruments, as required per IFRS 9, which is not material at transition.

The overall impact on retained earnings on transition to IFRS 9. is expected to be immaterial. Additional disclosures will be required for financial instruments in terms of IFRS 9.

- IFRS 15 Revenue from Contracts with Customers – provides a single, principles based five-step model to be applied to all contracts with customers - October 2018. Management has reviewed the significant customer contracts to determine recognition, measurement and disclosure effects of the new standard. Adoption of IFRS 15 is not expected to have a material impact on the recognition and measurement of revenue when compared to the current application of IAS 18.

Under IAS 18, Sappi derives revenue from contracts with customers from one revenue stream being the sale of goods. For the majority of local and regional sales, transfer occurs at the point of offboarding the shipment into the relevant carrier unless the contract of sale specifies different terms. Revenue is measured at the fair value of the amount received or receivable and after the deduction on trade and settlement discounts, rebates and customer returns. Shipping and handling costs, such as freight to the group's customers' destinations, are included in the cost of sales.

Under IFRS 15, revenue will be recognised when a customer obtains control of the goods. Management's assessment indicates that this will not result in a material change in timing of revenue recognition with revenue being recognised at a point in time, with no deferral of revenue. As a result, the impact on retained earnings on transition to IFRS 15 is expected to be immaterial. Additional disclosures will be required for revenue in terms of IFRS 15.

The group plans to adopt IFRS 15 using the cumulative effect method, with the effect of initially applying this standard recognised at the date of initial application (ie October 2018). As a result, the group will not apply the requirements of IFRS 15 to comparative periods presented.

- IFRS 16 Leases – Provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance substantially unchanged from its replacement standard IAS 17 Leases - October 2019. Management is currently reviewing the operating lease contracts in place to determine the impact of this standard.

The following standards are not expected to have a material impact:

- IFRS 2 - Classification and Measurement of Share-based Payment Transactions - October 2018
- IFRIC 22 - Foreign Currency Transactions and Advance Consideration- October 2018
- IFRIC 23 - Uncertainty over Income Tax Treatments - October 2019
- IAS 19 - Plan Amendment, Curtailment or Settlement - October 2019
- IAS 28 - Long-term Interests in Associates and Joint Ventures October 2019
- Annual Improvements 2015-2017 Cycle - Amendments to IFRS 1 and IAS 28 - October 2019

* Effective date refers to annual period beginning on or after said date

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued)
for the year ended September 2018

3. Operating profit

3.1 Cost of sales and selling, general and administrative and other expenses

Operating profit has been arrived at after charging (crediting):

R'millions	2018		2017	
	Cost of sales	Selling, general and administrative expenses	Cost of sales	Selling, general and administrative expenses
Raw materials, energy and other direct input costs	8,593	-	7,934	-
Fair value adjustment on plantations	(386)	-	(225)	-
Employment costs	2,000	466	1,749	577
Depreciation	839	35	759	25
Delivery charges	1,062	-	1,027	-
Maintenance	924	-	839	-
Other overheads	1,008	-	1,073	-
Marketing and selling expenses	-	22	-	26
Administrative and general expenses (income)	-	55	-	95
	14,040	578	13,156	723
			2018	2017
Fair value gains on plantations (note 7)				
Changes in volumes				
- Fellings			861	836
- Growth			(895)	(774)
			(34)	62
Plantation price fair value adjustment			(352)	(287)
			(386)	(225)
Silviculture costs (included within cost of sales)			856	788
Leasing charges for premises			58	44
Leasing charges for plant and equipment			5	12
Leasing charges for vehicles			31	35
Leasing charges for office equipment			25	25
Cost on derecognition of loans and receivables			94	83
Remuneration paid other than to <i>bona fide</i> employees of the company in respect of:			18	18
- Technical services			16	14
- Administration services			2	4
Audit and related services			12	12
Research and development costs			144	126

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

3. Operating profit (continued)

3.2 Employee Costs

R'millions	2018	2017
Employment costs consist of	2,466	2,326
Wages and salaries	1,723	1,709
Defined contribution plan expense (refer to note 23)	140	125
Defined benefit pension plan expense (refer to note 23)	68	76
Other defined benefit plan expense	8	4
Other company contributions	201	128
Overtime	138	129
Share-based payment expense	36	28
Other	152	127

3.3 Other expenses (income) include

(Profit) loss on disposal of assets	(53)	31
Insurance recoveries	(7)	-
Impairment of property, plant and equipment	2	-
Broad-based Black Economic Empowerment (BBBEE) charge	13	14
Reversal/Write-off of other assets	(38)	43

4. Net finance costs

Gross interest and other finance costs on liabilities carried at amortised cost	123	138
- Interest on bank overdrafts	3	2
- Interest on redeemable bonds and other loans	120	136
Net interest on employee benefit liabilities	5	(4)
Finance revenue received on assets carried at amortised cost	(180)	(152)
- Interest on bank accounts	(178)	(150)
- Interest revenue on other loans and investments	(2)	(2)
Net foreign exchange gains	(33)	(76)
	(85)	(94)

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

5. Taxation charge

R'million	2018	2017
Current taxation		
Current year	606	998
Prior year under/overprovision	287	(84)
Deferred taxation		
Current year	309	110
Prior year underprovision	-	39
	1,202	1,063

In addition to income taxation charges to profit and loss, current taxation charge of R6.7 million (2017: R7.6 million charge) and deferred taxation charge of R32.8 million (2017: R30.4 million relief) has been recognised directly in other comprehensive income (refer note 8).

Reconciliation of the tax rate	%	%
Statutory tax rate	28.0	28.0
Non-taxable income ⁽¹⁾	(0.9)	(1.2)
Prior year adjustments	8.5	(1.1)
Effective taxation rate for the year	35.6	25.7

(1) This mainly includes dividends, special allowances and items of a capital nature.

6. Property, plant and equipment

	2018	2017
Land and buildings ⁽¹⁾		
At cost	3,160	3,233
Accumulated depreciation and impairments	(1,168)	(1,234)
	1,992	1,999
Plant and equipment ⁽²⁾		
At cost	21,709	18,585
Accumulated depreciation and impairments	(10,621)	(9,950)
	11,088	8,635
Aggregate cost	24,869	21,818
Aggregate accumulated depreciation and impairments	(11,789)	(11,184)
Aggregate book value ⁽³⁾	13,080	10,634

⁽¹⁾ Details of land and buildings are available at the registered offices of the respective companies who own the assets.

⁽²⁾ Plant and equipment includes vehicles and furniture, the book value of which does not warrant disclosure as a separate class of assets.

⁽³⁾ An amount of R1,823.7 million (2017: R775.3 million) relates to assets under construction.

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

6. Property, plant and equipment (continued)

The movement of property, plant and equipment is reconciled as follows:

R'millions	Land and buildings	Plant and equipment	Total
Net book value at September 2016	1,929	8,134	10,063
Additions	163	1,239	1,402
Disposals	(1)	(46)	(47)
Depreciation	(92)	(692)	(784)
Net book value at September 2017	1,999	8,635	10,634
Additions	123	3,309	3,432
Disposals	(24)	(86)	(110)
Depreciation	(104)	(770)	(874)
Impairments (administration building)	(2)	-	(2)
Net book value at September 2018	1,992	11,088	13,080

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

7. Plantations

R'million	2018	2017
Fair value of plantations at the beginning of the year	6,206	6,043
Disposals	(1)	-
Fire, hazardous weather and other damages	(6)	(71)
In-field inventory	10	9
Gains arising from growth	895	774
Gain arising from fair value price changes	352	287
Harvesting - agriculture produce (fellings)	(861)	(836)
Fair value of plantations at the end of the year	6,595	6,206

Sappi manages the establishment, maintenance and harvesting of its plantations on a compartmentalised basis. These plantations are comprised of pulpwood and sawlogs and are managed to ensure that the optimum fibre balance is supplied to its paper and pulping operations in Southern Africa.

The group manages its plantations on a rotational basis. As such, increases by means of growth are negated by fellings, for the group's own use or for external sales, over the rotation period.

The group manages plantations on land that the group owns, as well as on land that the group leases. The group discloses both of these as directly managed plantations. With regard to indirectly managed plantations, the group has several different types of agreements with many independent farmers. The terms of the agreements depend on the type and specific needs of the farmer as well as the areas planted and range in duration from one to more than twenty years. In certain circumstances, the group provides loans to farmers (note 10) that are disclosed as other non-current assets on the group balance sheet (these loans are considered, individually and in aggregate, immaterial to the group). If the group provides seedlings, silviculture and/or technical assistance, the costs are expensed when incurred by the group.

The group is exposed to financial risks arising from climatic changes, disease and other natural risks such as fire, flooding and storms as well as human-induced losses arising from strikes, civil commotion and malicious damage. These risks are covered by an appropriate level of insurance as determined by management. The plantations have an integrated management system that complies with Forest Stewardship Council™ standards.

Plantations are stated at fair value less estimated cost to sell at the harvesting stage and is a Level 3 measure in terms of the fair value measurement hierarchy as established by IFRS 13 Fair Value Measurement which is consistent with the prior year.

The fair value of plantations has been calculated using a real pre-tax discount rate of 11.04%. The group currently values approximately 28 million tons of timber using selling prices and delivery costs that are benchmarked against industry norms. The average annual growth is measured at approximately 16 tons of timber per hectare while immature timber comprise approximately 107,000 hectares of plantations. As changes to estimated prices, the discount rate, costs to sell, and volume and growth assumptions applied in the valuation of immature timber may impact the calculated fair value, the group has calculated the sensitivity of a change in each of these assumptions as tabled

	2018	2017
Market price changes		
1% increase in market prices	29	26
1% decrease in market prices	(29)	(26)
Discount rate (for immature timber)		
1% increase in rate	(37)	(36)
1% decrease in rate	37	36
Volume assumption		
1% increase in estimate of volume	63	59
1% decrease in estimate of volume	(63)	(59)
Costs to sell		
1% increase in costs to sell	(24)	(23)
1% decrease in costs to sell	24	23
Growth assumptions		
1% increase in rate of growth	16	15
1% decrease in rate of growth	(16)	(15)

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

8. Deferred tax

R'millions	2018		2017	
	Assets	Liabilities	Assets	Liabilities
Other non-current liabilities	-	46	-	16
Accrued and other liabilities	-	(139)	-	(142)
Property, plant and equipment	-	2,214	-	2,010
Plantations	-	1,858	-	1,753
	-	3,979	-	3,637

	2018	2017
Reconciliation of deferred tax		
Deferred tax balances at beginning of year		
- Deferred tax assets	-	-
- Deferred tax liabilities	3,637	3,518
	3,637	3,518
Deferred tax benefit (charge) for the year (refer to note 5)	309	149
- Other non-current assets	(3)	(1)
- Accrued and other liabilities	3	11
- Property, plant and equipment	204	94
- Plantations	105	45
Amounts recorded directly in other comprehensive income	33	(30)
Deferred tax balances at end of year	3,979	3,637
- Deferred tax assets	-	-
- Deferred tax liabilities	3,979	3,637

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

9. Equity accounted investee

A 50% joint venture agreement with Borregaard AS for the construction and operation of a lignin plant at Umkomaas, South Africa and development, production and sale of products based on lignosulphonate in order to build a sustainable lignin business. The financial statements of the Umkomaas Lignin Proprietary Limited are to 31 December of each year which is the year-end of Borregaard AS. The unaudited management accounts which are prepared in accordance with International Financial Reporting Standards are used to account for joint venture's income to Sappi's year-end.

Summarised financial information of Umkomaas Lignin Proprietary Limited:

R'millions	2018	2017
Initial cost of investment in joint venture	2	2
Share of post-acquisition profits	89	122
- Opening balance	122	125
- Current year profit	44	88
- Additions equity	-	-
- Dividend received	(77)	(91)
Historic loan - converted to share capital	70	70
Investment in joint venture	161	194

Dividends received from joint ventures for the 2018 financial year were R77.5 million (2017: R90.8 million).

Balance Sheet summary

Current assets	272	341
Non-current assets	254	262
Current liabilities	(100)	(95)
Non-current liabilities	(104)	(120)

The above assets and liabilities include the following:

Cash and cash equivalents	72	141
Current financial liabilities (excluding trade and other payables, and provisions)	(100)	(95)
Non-current financial liabilities (excluding trade and other payables, and provisions)	(104)	(120)

Income Statement summary

Sales	645	653
Depreciation and amortisation	27	22
Finance costs	7	1
Finance revenue	4	1
Taxation charge	30	49
Profit from continuing operations	89	175
Other comprehensive income	-	-
Total comprehensive income	89	175

Reconciliation of the financial information to the carrying amount of the joint venture:

Net assets of the joint venture	322	388
Proportion of the group's ownership interest	50%	50%
Carrying amount of the group's interest in the joint venture	161	194

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

10. Other non-current assets

R'millions	2018	2017
Advances to tree growers	45	42
Licence fee	1	1
Defined benefit pension plan assets (refer to note 23)	256	236
Unlisted investment	15	15
Investment in Ngodwana energy	23	-
Shareholder loan to Ngodwana energy	45	-
Other	8	8
	393	302

11. Inventories

R'millions	2018	2017
Raw materials	451	405
Work in progress	65	59
Finished goods	1,102	786
Consumable stores and spares	393	377
	2,011	1,627

The charge to the income statement relating to the write-down of inventories to net realisable value amounted to R22.2 million (2017: R41.1 million).

The cost of inventories recognised as an expense and included in cost of sales amounted to R13,356.2 million (2017: R12,406.7 million).

12. Trade and other receivables

R'millions	2018	2017
Trade accounts receivable	120	117
Allowance for credit losses	(4)	-
Trade accounts receivable, net	116	117
Receiver of revenue	281	50
Prepaid insurance	23	22
Prepayments and other receivables	190	158
	610	347

Management rates the quality of trade and other receivables periodically against its internal credit rating parameters. The quality of these trade receivables is such that management believes no additional allowance for credit losses, other than as provided, is necessary. No significant risk has been identified within the trade accounts receivables not past due but not impaired. Due to the short maturities of trade and other receivables, the carrying amount of these trade and other receivables approximate their fair values.

Trade receivables (including securitised trade receivables) represent 6.3% (2017: 6.2%) of turnover.

12.1 Reconciliation of the allowance for credit losses

Balance at beginning of year	-	-
Raised during the year	4	-
Balance at end of year	4	-

The allowance for credit losses has been determined by reference to specific customer delinquencies.

12.2 Analysis of amounts past due

September 2018

The following provides an analysis of the amounts that are past the contractual maturity dates:

R' million	Not impaired	Impaired	Total
Less than 7 days overdue	-	-	-
Between 7 and 30 days overdue	-	-	-
Between 30 and 60 days overdue	-	-	-
More than 60 days overdue	1	4	5
	1	4	5

September 2017

The following provides an analysis of the amounts that are past the contractual maturity dates:

R' million	Not impaired	Impaired	Total
Less than 7 days overdue	6	-	6
Between 7 and 30 days overdue	-	-	-
Between 30 and 60 days overdue	-	-	-
More than 60 days overdue	-	-	-
	6	-	6

All amounts which are due but beyond their contractual repayment terms are reported to divisional management on a regular basis. Any provision for impairment is required to be approved in line with Sappi's limits of authority framework.

The group holds collateral of R72.6 million (2017: R70.5 million) against trade receivables past contractual repayment terms. The group holds collateral of R1.4 million (2017: R0 million) against past due trade receivables.

12.3 Fair value

Due to the short maturities of trade and other receivables, the carrying amount of these trade and other receivables approximates their fair value.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

12. Trade and other receivables (continued)

12.4 Off-balance sheet structures

Sappi sells the majority of its ZAR receivables to Rand Merchant Bank Limited, a division of FirstRand Bank Limited. In terms of the agreement, Sappi is required to maintain a credit insurance policy with a reputable insurance provider and, while the company does not guarantee the recoverability of any amounts, it carries 15% of the credit risk (and Rand Merchant Bank Limited the remainder) of each underlying receivable, after all recoveries, including insurance recoveries. As a result, no additional liability has been recognised as this would be insignificant to the financial statements.

Sappi administers the collection of all amounts processed on behalf of the bank that are due from the customer. The purchase price of these receivables is dependent on the timing of the payment received from the client. The rate of discounting that is charged on the receivables is the Johannesburg Inter-bank Agreed Rate (JIBAR) plus a spread. This structure is treated as an off-balance sheet arrangement.

If this securitisation facility were to be terminated, we would discontinue further sales of trade receivables and would not incur any losses in respect of receivables previously sold in excess of the 15% mentioned above. There are a number of events which may trigger termination of the facility, among others, an amount of defaults above a specified level, terms and conditions of the agreement not being met, or breaches of various credit insurance ratios. The impact on liquidity varies according to the terms of the agreement; generally, however, future trade receivables would be recorded on-balance sheet until a replacement agreement is entered into.

Details of the securitisation programme at the end of the 2018 and 2017 financial years are disclosed in the table below:

Bank	Value	Facility	Discount charges
2018			
Rand Merchant Bank Limited	ZAR1,004 million	Unlimited ⁽¹⁾	Linked to 3-month JIBAR
2017			
Rand Merchant Bank Limited	ZAR980 million	Unlimited ⁽¹⁾	Linked to 3-month JIBAR

⁽¹⁾ The facility in respect of the securitisation facility is unlimited, but subject to the sale of qualifying receivables to the bank.

Refer to note 27 for further details on credit risks.

12.5 Concentration of credit risk

A significant portion of the group's sales and accounts receivable are from a small number of customers. None of the group's significant customers represented more than 10% of our sales and trade receivables during the years ended September 2018 and September 2017.

Where appropriate, credit insurance has been taken out over the group's trade receivables.

None of the group's other receivables represent a high concentration of credit risk because the group has dealings with a variety of major banks and customers worldwide.

At balance sheet date, the carrying amount of R610.4 million (2017: R347.2 million) represents the group's maximum credit risk exposure from trade and other receivables.

The group has the following trade receivable amounts due from single customers:

Threshold	2018		2017	
	Number of customers	R'Million	Number of customers	R'Million
Less than US\$5 million	79	110	82	117
	79	110	82	117

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

13. Ordinary share capital and share premium

R'millions	Consolidated	
	2018	2017
Authorised share capital:		
6,052,500 Ordinary shares of R2 each	12	12
19,520 Class A cumulative preference shares of R0.01 each ⁽¹⁾⁽²⁾	-	-
221,107 Class B cumulative preference shares of R0.01 each ⁽¹⁾⁽²⁾	-	-
831 Class C cumulative preference shares of R0.01 each ⁽¹⁾⁽²⁾	-	-
123,321 Class D cumulative preference shares of R0.01 each ⁽¹⁾⁽²⁾	-	-
	12	12
Issued share capital:		
6,015,769 (2017: 6,015,769) Ordinary shares of R2 each	12	12
19,520 (2017: 19,520) Class A cumulative preference shares of R0.01 each ⁽¹⁾⁽²⁾⁽³⁾	-	-
219,760 (2017: 219,760) Class B cumulative preference shares of R0.01 each ⁽¹⁾⁽²⁾⁽³⁾	-	-
831 (2017: 831) Class C cumulative preference shares of R0.01 each ⁽¹⁾⁽²⁾⁽³⁾	-	-
120,018 (2017: 118,602) Class D cumulative preference shares of R0.01 each ⁽¹⁾⁽²⁾⁽³⁾	-	-
Sappi Property Company (Pty) Limited ⁽²⁾⁽³⁾	-	-
	12	12
Share premium on ordinary shares	209	209
Share premium on preference shares	-	-
362,820 Investment in Sappi Property Company Proprietary Limited preference shares ⁽¹⁾⁽²⁾	-	-
Closing balance	221	221

⁽¹⁾ The variable coupon rate based upon Sappi Southern Africa Limited's (SSA) long-term borrowing rate.

⁽²⁾ The Class "A", "B", "C" and "D" preference share were issued to Sappi Property Company Proprietary Limited (SPC) for no cash consideration on 30 June 2008. SSA subsequently acquired all the ordinary shares of SPC on 11 June 2010 Sappi Southern Africa Limited holds 362,820 (2017: 362,532) preference shares in SPC. A legal right to off-set these preference shares exists.

⁽³⁾ Issued at nominal value

Capital risk management

The capital structure of the group consists of:

- issued share capital and share premium and accumulated profits disclosed above and in the statement of changes in equity respectively
- debt, which includes interest-bearing borrowings as disclosed in note 16, and
- cash and cash equivalents.

The objectives of the group in managing capital are:

- to safeguard the group's ability to continue as a going concern, to be flexible and to take advantage of opportunities that are expected to provide an adequate return to shareholders,
- to ensure sufficient resilience against economic turmoil,
- to maximise returns to stakeholders by optimising the weighted average cost of capital, given inherent constraints, and
- to ensure appropriate access to equity and debt.

The group monitors its gearing through a ratio of net debt (interest-bearing borrowings and overdrafts less cash and cash equivalents) to total capitalisation (shareholders' equity plus net debt).

The group has entered into a number of debt facilities which contain certain terms and conditions in respect of capital management.

The group was in compliance with the financial covenants relating to the loans payable during both the current and prior fiscal years.

The group's strategy with regard to capital risk management remains unchanged from the prior year.

The group manages its capital and makes adjustments to it in light of changes in economic conditions. No changes were made in the objectives, policies or processes during the current period.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

14. Other comprehensive income

R'millions	2018	2017
Item that will not be reclassified subsequently to profit or loss		
Actuarial (losses) gains on post-employment benefit funds	14	(71)
Gross amount	19	(99)
Tax	(5)	28
Item that may be reclassified subsequently to profit or loss		
Hedging reserves	88	(27)
Movements during the year	102	214
Reclassified to profit or loss	23	(252)
Reclassified to property, plant and equipment	(3)	2
Tax	(34)	9
Other comprehensive income recorded directly in equity	102	(98)
Profit for the year	2,176	3,079
Total comprehensive income for the year	2,278	2,981
15. Non-distributable reserves		
Share-based payment reserve (refer to note 24)	(57)	(49)
Share-based payment reserve - BBEE (refer to note 24)	214	201
	157	152

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

16. Interest-bearing borrowings

R'millions	2018	2017
Unsecured borrowings	1,145	1,645
Less: Current portion included in current liabilities	-	(500)
Total non-current interest-bearing borrowings	1,145	1,145

The repayment profile of the interest-bearing borrowings is as follows:

Payable in the year ended September:

2018		500
2019	-	-
2020	1,145	1,145
2021	-	-
2022	-	-
2023 (September 2017: Thereafter)	-	-
Thereafter	-	-
	1,145	1,645

Capitalised lease liabilities

As at financial year-end, the group had no material capitalised finance lease liabilities.

Set out below are details of the more significant interest-bearing borrowings in the group as at September 2018:

	Currency	Interest rate	Principal amount outstanding	Balance sheet value	Security / cession	Expiry
Redeemable bonds						
Public bond	ZAR	Fixed ⁽¹⁾	ZAR745 million	ZAR744 million	Unsecured	April 2020
Unsecured bank term loans						
GroCapital Financial Services	ZAR	Fixed ⁽¹⁾	ZAR400 million	ZAR400 million	Unsecured	May 2020

⁽¹⁾ The principal value of the loans / bonds corresponds to the amount of the facility; however, the balance sheet value has been adjusted by the discounts paid upfront.

A detailed analysis of total interest-bearing borrowings has been disclosed in note 27.

Other restrictions

In addition to the above borrowings, the group operates an of-balance sheet securitisation facility. Please refer to note 12 for further detail on this facility and related restrictions.

During the 2018 and 2017 financial years, the group was in compliance with the financial covenants relating to all loans payable. Compliance with applicable covenants are monitored on an ongoing basis. If a possible breach of a financial covenant were to be expected, negotiations would commence with the applicable institutions before such breach occurs.

Unutilised facilities

The group monitors its availability of funds on a daily basis. The group treasury committee monitors the amount of unutilised facilities to assess the headroom available. The net cash balances included in current assets and current liabilities are included in the determination of the headroom available.

	Currency	Interest rate	2018	2017
Unutilised committed facilities				
Syndicate loan/revolving credit facility ⁽¹⁾	ZAR	Variable (JIBAR)	1,000	1,000
Unutilised uncommitted facilities				
Cash management overdraft facility/short-term banking facilities	ZAR	Variable (ZAR bank prime)	275	275
Total unutilised facilities (committed and uncommitted) excluding cash			1,275	1,275

⁽¹⁾ Syndicated loans with a consortium of banks with revolving facilities available of R1 billion. The R1 billion facility is an evergreen facility with a 15 month notice period and is subject to financial covenants relating to the financial position of Sappi Southern Africa Limited. During the year, the group paid an amount of R4.4 million (2017: R4.5 million) in respect of this facility.

Fair value

The fair values of all interest-bearing borrowings are disclosed in note 27.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

17. Other non-current liabilities

R'millions	2018	2017
Post-employment benefits (refer to note 22)	271	250
Other	-	4
	<u>271</u>	<u>254</u>

18. Notes to the group statement of cash flows

18.1 Cash generated from operations

Profit for the year	2,176	3,079
Adjustment for:		
- Depreciation	874	784
- Fellingings	861	836
- Taxation charge	1,202	1,063
- Net finance (income) costs	(85)	(94)
- Equity accounted profits	(45)	(88)
- Loss (profit) on disposal of assets and businesses	(53)	31
- Plantation fire, drought and other damages	6	71
- Fair value adjustment gains and growth on plantations	(1,247)	(1,061)
- Other non-cash items	(1)	17
	<u>3,688</u>	<u>4,638</u>

18.2 Increase in working capital

(Increase) decrease in inventories	(395)	11
(Increase) decrease in receivables	(409)	147
(Increase) decrease in amounts owed by group companies	(364)	37
Increase (decrease) in payables	843	(39)
Increase (decrease) in amounts owed to group companies	32	(67)
	<u>(293)</u>	<u>89</u>

18.3 Finance costs paid

Interest and other finance costs on liabilities carried at amortised cost	(128)	(134)
Net foreign exchange gains (losses)	33	76
Transfers to financing activities and non-cash items	16	(12)
	<u>(79)</u>	<u>(70)</u>

18.4 Taxation paid

Net amounts receivable (payable) at beginning of year	41	(356)
Taxation charge to profit or loss	(893)	(914)
Taxation (charge) benefit per OCI	(7)	8
Net amounts payable at end of year	109	(41)
	<u>(750)</u>	<u>(1,303)</u>

18.5 Proceeds on disposal of other non-current assets

Book value of non-current assets disposed of	91	48
Profit (loss) on disposal	53	(32)
	<u>144</u>	<u>16</u>

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

19. Encumbered assets

At financial year-end, none of the group's assets were encumbered.

20. Commitments

R'millions	2018	2017
<i>Capital commitments</i>		
Contracted but not provided	2,227	722
Approved but not contracted	3,425	1,492
	<u>5,652</u>	<u>2,214</u>

Future forecasted cash flows of capital commitments at September:

2018		1,935
2019	3,230	279
2020	2,263	-
Thereafter	159	
	<u>5,652</u>	<u>2,214</u>

These projects are expected to be financed by funds generated by the business, existing cash resources and borrowing facilities available to the group.

Lease commitments

Future undiscounted minimum operating lease obligations payable in the year ended September:

2018		96
2019	101	50
2020	46	38
2021	32	26
2022	25	24
2023 (2017: Thereafter)	22	132
Thereafter	99	-
	<u>325</u>	<u>366</u>

The group enters into a number of leases, mainly relating to property, plant and equipment and vehicles. Lease terms range between 3 to 10 years and may be renegotiated on expiry.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

21. Contingent liabilities

Contingent liabilities mainly relate to environmental and taxation queries in respect of certain group companies.

The group is involved in various lawsuits and administrative proceedings. The relief sought in such lawsuits and proceedings includes injunctions, damages and penalties. Although the final results in these lawsuits and proceedings cannot be predicted with certainty, it is the present opinion of management, after consulting with legal counsel, that the possibility of a material outflow of resources in connection with these lawsuits and administrative proceedings is considered to be remote.

The company has been audited by the South African Revenue Service (SARS) in respect of transfer pricing relating to the 2011-2014 years of assessment. On 14 September 2017, a letter of findings was issued to the company notifying it of a potential upward adjustment to taxable income of R883 million which would result in an additional tax liability of approximately R316 million, excluding any potential interest and penalties, should the company eventually be assessed on this basis. The company did not agree with SARS's analysis and had responded to the letter of findings objecting to the basis for the proposed adjustments and including representations on why interest and penalties should not be raised. The SARS assessments were received on 26 February 2018. The company made a payment without prejudice of R268 million. The company formally objected against the assessments received and are awaiting a response from SARS.

22. Post-employment benefits - pensions

Summary of results

	2018	2017
Post-employment plan costs (credits) recognised in profit or loss	49	52
Employer contributions paid during the financial year	61	63

Defined contribution plans

The group operates a defined contribution plan for all qualifying employees throughout the group. The assets of the plans are held, separately from those of the group, in funds under the control of trustees or administered by insurance companies. The group also participates in various local industry (multi-employer) plans, open to eligible employees often as a voluntary alternative to company sponsored plans. There are no obligations on the group other than to pay contributions according to the rules of each plan.

The total cost charged to the income statement of R140 million (2017: R125 million) represents contributions payable to these plans by the group based on rates specified in the rules of these plans. Expected contributions (total cost charged) to be paid in the next financial year is R147 million.

Defined benefit pension plans

The group operates a defined benefit pension and a defined benefit disability plan. These plans are closed to new entrants. All plans have been established in accordance with applicable legal requirements, customs and existing circumstances in South Africa.

The assets of our funded plans are held in separate trustee-administered funds and are subject to statutory requirements. Generally, the trusts are required by law and their articles of associations to act in the interests of the fund and its stakeholders, ie members and the various local sponsoring companies across the group. The plans comprise of management and member-appointed trustees, including an independent trustee, who collectively are responsible for the administration and governance of the trusts.

Benefits are formula-driven, based on final average salary

Exposure to risks

The major risks faced by the group as a result of the defined benefit obligation can be summarised as follows:

Inflation: The risk that future inflation indices is higher than expected and uncontrolled,

Future changes in legislation: The risk that changes to legislation with respect to the post-employment liability may increase the liability for the group,

Future changes in the tax environment: The risk that changes in the tax legislation governing employee benefits may increase the liability for the group,

Longevity: The risk that pensioners live longer than expected and thus their pension benefit is payable for longer than expected, and

Administration: Administration of this liability poses a burden to the group.

The main strategic choices that are formulated in the actuarial and technical policies of our plans across the group are as follows:

- Strategic asset mix based on
 - 40% equity instruments,
 - 55% debt instruments, and
 - 5% cash.

Local regulations impose minimum funding targets and maximum foreign holdings significantly influencing the strategic asset allocation of individual plans.

Since the pension liabilities are adjusted to respective local consumer price indices, the plans are exposed to local inflation, interest rate risks and changes in life expectancies of members. As the plan assets include significant investments in quoted equity shares, property and high yield bonds in various markets around the globe, the group is exposed to equity, property, high yield bond market risk and for non-domestic holdings, currency risk. Debt instruments typically comprise investment grade corporate and government debt in markets around the globe, primarily held to match counter-movements in plan liabilities of the same value. The group is also exposed to losses from the effects of credit grade re-ratings on debt instruments in bond markets across the globe.

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

22. Post-employment benefits - pensions (continued)

Investment management and strategic asset allocation

Plan fiduciaries are responsible for investment policies and strategies for local trusts. Long-term strategic investment objectives include preserving the funded status of the trust and balancing risk and return while keeping in mind the regulatory environment. Plan fiduciaries oversee the investment allocation process, which includes selecting investment managers, setting long-term strategic targets and rebalancing assets periodically. Plan fiduciaries also make use of fiduciary managers, multi-asset manager mandates and 'flight path' assessment tools to assist with strategic asset allocation. Such reviews include asset-liability modelling studies to analyse risk-and-return profiles. Investment and contribution policies are integrated within this study.

Funding Policy

Members contribute a fixed percentage of pensionable salary to the pension plan and the group's subsidiaries fund the balance of the cost of the entitlements expected to be earned on an annual basis, and cover the entire cost of the disability plan. The funding requirements are based on local actuarial measurement frameworks. For prefunded plans, contributions are determined on a current salary base. Additional liabilities stemming from past service due to salary increases are paid immediately to the plans as part of the overall agreed contribution rate to restore individual plan deficits where these occur.

Expected company contributions across group subsidiaries over the next financial year are R60 million.

An actuarial review is performed annually, with an actuarial valuation being performed on a tri-annual basis.

	2018	2017
Components of defined benefit cost recognised in profit or loss		
Current service cost	61	71
Past service cost	2	1
Net interest credit on defined benefits	(19)	(24)
Fund administration costs	5	4
Net amount recognised in profit or loss	<u>49</u>	<u>52</u>
Net amount attributed to Operating Cost	68	76
Net amount attributed to Finance Cost	(19)	(24)
Net amount recognised in profit or loss	<u>49</u>	<u>52</u>
Components of defined benefit cost recognised in other comprehensive income		
Actuarial loss arising from membership experience	(33)	(3)
Actuarial gain (loss) arising from changes in demographic assumptions	2	(146)
Actuarial gain arising from changes in financial assumptions	181	300
Actuarial loss arising on assets	(142)	(239)
Net gain (loss) recognised in other comprehensive income	<u>8</u>	<u>(88)</u>

	Consolidated	
	2018	2017
Movement in the present value of the defined benefit obligation in the current year		
Defined benefit obligation at beginning of year	1,729	1,865
Current service cost	61	71
Past service cost	2	1
Interest cost	157	172
Plan participants' contributions	21	21
Remeasurements gains	(150)	(151)
- Membership experience loss	33	3
- Demographic assumptions (gains) loss	(2)	146
- Financial assumptions gains	(181)	(300)
Benefits paid	(194)	(250)
Defined benefit obligation at end of year	<u>1,626</u>	<u>1,729</u>
Movement in the fair value of the plan assets in the current year		
Fair value of plan assets at beginning of year	1,965	2,178
Interest income	176	196
Employer contributions	61	63
Plan participants' contributions	21	21
Remeasurements loss	(142)	(239)
- Actuarial loss arising on assets	(142)	(239)
Benefits paid	(194)	(250)
Fund administration costs	(5)	(4)
Fair value of plan assets at end of year	<u>1,882</u>	<u>1,965</u>
Recognised pension plan assets	<u>(256)</u>	<u>(236)</u>

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

22. Post-employment benefits - pensions (continued)

The major categories of plan assets at fair value are presented as follows:

	2018	2017
<u>Investments quoted in active markets</u>		
- Equity, property and high yield investments		
- Domestic	242	290
- Foreign	6	290
- Investment grade debt instruments		
- Nominal	1,413	1,231
<u>Unquoted investments</u>		
- Other	4	-
<u>Cash and cash equivalents</u>	217	154
	1,882	1,965

Plan assets do not include any investments in the group's own quoted shares. These were held by an appointed investment manager as part of the routine mandate to invest in domestic equities.

The fair values of the various equity and debt instruments are determined based on quoted market prices in active markets, whereas the fair values of certain property and derivatives are not based on quoted market prices in active markets. Plans generally buy and hold bonds as a hedge against interest rate and inflation rate risk.

The principal assumptions used in determining pension subsidies for the group's plans are shown below:

	Consolidated	
	2018	2017
Discount rate (%)	9.69	9.28
Future salary increases (%)	7.09	7.28
Cost of living adjustment for pensions in payment (%)	4.87	5.03
Average life expectancy in years		
- For current beneficiaries (male of 60 years)	19.20	19.20
- Future retiree (male of 60 years in 20 years' time)	20.20	20.20

A quantitative sensitivity analysis for significant assumptions as at financial year-end is disclosed below:

Significant actuarial assumptions for the determination of the defined benefit obligations are discount rate, expected salary increase, cost of living adjustments to pensions in payment and mortality. The sensitivity analysis below has been determined based on reasonably possible changes of the respective assumptions occurring at the end of the reporting period, whilst holding all other assumptions constant.

- If the discount rate is 100 basis points higher (lower), the defined benefit obligation would decrease by R217 million (increase by R252 million).
- If the expected salary increase rate is 100 basis points higher (lower), the defined benefit obligation would increase by R135 million (decrease by R128 million)
- If the expected cost of living adjustment (pension increase) rate is 100 basis points higher (lower), the defined benefit obligation would increase by R118 million (decrease by R111 million)
- If the life expectancy increases (decreases) by one year for both men and women, the defined benefit obligation would increase by R37 million (decrease R32 million).

The sensitivity analysis presented above may not be representative of the actual change in the defined benefit obligation as it is unlikely that the change in assumptions would occur in isolation of one another as some of the assumptions may be correlated.

Furthermore, in presenting the sensitivity analysis above, the present value of the defined benefit obligation has been calculated using the projected unit credit method at the end of the reporting period, which is the same as that applied in calculating that applied in calculating the defined benefit obligation recognised in the balance sheet. There was no change in the methods and assumptions used in preparing the sensitivity analysis from prior years.

The average duration of the defined benefit plan obligations at the end of the reporting period is 9 years.

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

23. Post-employment benefits - post-retirement healthcare

R'million	2018	2017
Post-employment plan costs recognised in profit or loss	32	25

Post-employment benefits - post-retirement healthcare subsidy

The company sponsors a defined benefit post-employment plan that provides certain health care and life insurance benefits to eligible retired employees. Employees who joined the company before 1 October 1999 and maintain uninterrupted membership of eligible medical aid schemes are then generally eligible for the subsidy upon retirement.

Expected company contributions across group subsidiaries over the next financial year are R5.3 million.

Components of defined benefit cost recognised in profit or loss

	2018	2017
Current service cost	8	7
Past service cost	-	(3)
Net interest cost on defined benefits	24	21
Net amount recognised in profit or loss	<u>32</u>	<u>25</u>
Net amount attributed to Operating Cost	8	4
Net amount attributed to Finance Cost	24	21
Net amount recognised in profit or loss	<u>32</u>	<u>25</u>

Components of defined benefit cost recognised in other

Actuarial losses arising from membership experience	(1)	(9)
Actuarial losses arising from changes in demographic assumptions	(25)	(27)
Actuarial gains arising from changes in financial assumptions	38	24
Actuarial (losses) gains arising on assets	(1)	1
Net gain (loss) recognised in other comprehensive income	<u>11</u>	<u>(11)</u>

Movement in the present value of the defined benefit obligation in

Defined benefit obligation at beginning of year	359	328
Current service cost	8	7
Past service cost	-	(3)
Interest expense	34	31
Remeasurements (gain) loss	(12)	12
- Membership experience loss	1	9
- Demographic assumption loss	25	27
- Financial assumption gain	(38)	(24)
Non-routine settlements	-	(4)
Benefits paid	(13)	(12)
Defined benefit obligation at end of year	<u>376</u>	<u>359</u>

Movement in the fair value of the plan assets in the current year

Fair value of plan assets at beginning of year	109	114
Interest income	10	10
Remeasurements (loss) gain	(1)	1
- Actuarial (loss) gain arising on assets	(1)	1
Non-routine plan settlements	-	(4)
Benefits paid	(13)	(12)
Fair value of plan assets at end of year	<u>105</u>	<u>109</u>
Net balance sheet defined benefit liability	<u>271</u>	<u>250</u>

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

23. Post-employment benefits - post-retirement healthcare subsidy (continued)

The major categories of plan assets at fair value are presented as follows:

	2018	2017
<u>Investments quoted in active markets</u>		
- Investment grade debt instruments		
- Nominal	-	-
- Index linked	-	-
<u>Unquoted investments</u>		
- Other	94	98
Cash and cash equivalents	12	12
	106	110

The fair values of the various equity and debt instruments are determined based on quoted market prices in active markets, whereas the fair values of certain property and derivatives are not based on quoted market prices in active markets. Plans generally buy and hold bonds as a hedge against interest rate and inflation rate risk.

The principal assumptions used in determining post-employment medical aid subsidies for the group's plans are shown below:

	2018	2017
Discount rate (%)	10.00	9.75
Healthcare cost trend rate (%)	7.75	8.25
Average expectancy in years		
- For current beneficiaries (male of 60 years)	19.50	19.50

A quantitative sensitivity analysis for significant assumptions as at financial year-end is disclosed below:

Significant actuarial assumptions for the determination of the defined benefit obligations are discount rate, expected salary increase, health care cost trends and mortality. The sensitivity analysis below has been determined based on reasonably possible changes of the respective assumptions occurring at the end of the reporting period, whilst holding all other assumptions constant.

- If the discount rate is 100 basis points higher (lower), the defined benefit obligation would decrease by R45 million (increase by R56 million)
- If the expected health care cost trend rate is 100 basis points higher (lower), the defined benefit obligation would increase by R57 million (decrease by R47 million)
- If the life expectancy increases (decreases) by one year for both men and women, the defined benefit obligation would increase by R12 million (decrease R12 million).

The sensitivity analysis presented above may not be representative of the actual change in the defined benefit obligation as it is unlikely that the change in assumptions would occur in isolation of one another as some of the assumptions may be correlated.

Furthermore, in presenting the sensitivity analysis above, the present value of the defined benefit obligation has been calculated using the projected unit credit method at the end of the reporting period, which is the same as that applied in calculating the defined benefit obligation liability recognised in the balance sheet.

There was no change in the methods and assumptions used in preparing the sensitivity analysis from prior years.

The average duration of the defined benefit plan obligations at the end of the reporting period is 15 years.

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

24. Share-based payments

The Sappi Limited Share Incentive Trust and The Sappi Limited Performance Share Incentive Trust

Shareholders, at prior annual general meetings, fixed the aggregate number of shares which may be acquired by all participants under The Sappi Limited Share Incentive Trust (the Scheme) and The Sappi Limited Performance Share Incentive Trust (the Plan) at 42,700,870 shares.

The Sappi Limited Share Incentive Trust (the Scheme)

Under the rules of the Scheme, participants (a) may be offered options to acquire ordinary shares (share options) and (b) may be offered the opportunity to acquire ordinary shares (scheme shares).

Under the rules of the Scheme:

- Share options entitle the participant to purchase one ordinary share per share option, and
- Scheme shares entitle the participant to enter into a loan with the Scheme to acquire Sappi Limited shares at a specific issue price.

The scheme shares are registered in the participant's name and pledged to the Scheme as security for the loan. Upon payment of the loan, the scheme shares become unsecured Sappi Limited shares owned by the participant.

The amount payable by a participant is the closing price at which shares are traded on the JSE Limited on the trading date immediately preceding the date upon which the board authorised the grant of the opportunity to acquire relevant share options or scheme shares, as the case may be.

The share options and scheme shares vest in blocks of 25% per annum on the anniversary date of the offer and expire eight years after the offer date. Only once the options vest, may share options be exercised by the participants and may scheme shares be released from the Scheme to participants.

The Scheme rules provide that appropriate adjustments are to be made to the rights of participants in the event that the company, *inter alia*, undertakes a rights offer, a capitalisation issue, or consolidation of ordinary shares or any reduction in its ordinary share capital.

The Sappi Limited Performance Share Incentive Trust (the Plan)

Under the rules of the Plan, participants may be awarded conditional contracts to acquire ordinary shares for no cash consideration. The conditional contracts are subject to performance criteria being met or exceeded after the fourth anniversary date. Should the performance criteria not be met, the number of shares allotted are adjusted downwards from 100% to 75%, or 50%, or none depending on the degree of not meeting the criteria. The performance criteria, which entails a benchmarking of the company's performance against an appropriate peer group of companies, is set by the board at the offer date for each conditional share award.

The Plan rules provide that appropriate adjustments are made to the rights of participants in the event that the company, *inter alia*, undertakes:

- a rights offer, or
- is a party to a scheme of arrangement affecting the structuring of its issued share capital or reduces its share capital.

The Plan rules also provide that if:

- the company undergoes a change in control after an allocation date other than a change in control initiated by the board itself, or
- the persons who have control of the company as at an allocation date, take any decision, pass any resolution or take any action, the effect of which is to delist the company from the JSE Limited and the company becomes aware of such decision, resolution, or action;

then the company is obliged to notify every participant thereof that such participant may within a period of one month (or such longer period as the board may permit) take delivery of those shares which they would have been entitled to had the performance criteria been achieved.

Movements in share options and performance shares for the financial years ended September 2018 and September 2017 are as follows:

	Performance shares ⁽¹⁾	Share options	Weighted average share option exercise price (ZAR)	Total Shares
Outstanding at September 2016	3,558,672	983,971	30.14	4,542,643
- Offered	698,400	-	-	698,400
- Paid for/vested	(782,192)	(398,500)	31.56	(1,180,692)
- Returned, lapsed, forfeited and transfers	(161,700)	(70,861)	32.47	(232,561)
Outstanding at September 2017	3,313,180	514,610	29.08	3,827,790
- Offered	706,550	-	-	706,550
- Paid for/vested	(956,978)	(294,540)	31.28	(1,251,518)
- Returned, lapsed, forfeited and transfers	(66,662)	(23,900)	33.85	(90,562)
Outstanding at September 2018	2,996,090	196,170	26.15	3,192,260
Exercisable at September 2017	-	514,610	29.08	514,610
Exercisable at September 2018	-	196,170	26.15	196,170

⁽¹⁾ Performance shares are issued in terms of the Plan and are for no cash consideration. The value is determined on the day the shares vest.

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

24 Share-based payments (continued)

The following assumptions have been utilised to determine the fair value of the shares granted in the financial period in terms of the Scheme and the Plan:

	Issue 43	Issue 43
Date of grant	04 December 2017	04 December 2017
Type of award	Performance	Performance
Share price at grant date	ZAR 95.64	ZAR 95.64
Vesting period	4 years	4 years
Vesting conditions	Market-related - relative to peers	Cash flow return on net assets relative to peers
Life of options	n/a	n/a
Market-related vesting conditions	Yes	No
Percentage expected to vest	61%	61%
Number of shares offered	1,377,825	1,377,825
Volatility	31%	n/a
Risk-free discount rate	2.148% (US yield)	n/a
Expected dividend yield	2.2%	n/a
Model used to value	Monte-Carlo	Market price
Fair value of option	ZAR 68.40	ZAR 58.44

Volatility has been determined with reference to the historic volatility of the Sappi share price over the expected period.

Refer to note 30 for more information on directors' and prescribed officers' participation in the Scheme and the Plan.

Broad-based Black Economic Empowerment

In June 2010, Sappi completed a Broad-based Black Economic Empowerment (BBBEE) transaction (the 'BBBEE transaction') that enabled Sappi to meet its BBBEE targets in respect of BBBEE equity ownership. The South African government has through the years promulgated various pieces of legislation to increase the participation of Historically Disadvantaged South Africans (HDSAs) in the South African economy and, through BBBEE legislation, formalised the country's approach in this regard. Sappi views BBBEE as a key requirement for sustainable growth and social development in South Africa.

In April 2006, Sappi announced a BBBEE transaction (the 'Plantation BBBEE transaction') that included a consortium of investors and certain categories of Sappi's South African employees. However, the Plantation BBBEE transaction did not meet Sappi's undertakings under the Forestry Charter gazetted in June 2009 (which sets the objectives and principles for BBBEE in the forestry industry and includes the BBBEE scorecard and targets to be applied, as well as certain undertakings by government and South African forestry companies to assist the forestry industry to achieve its BBBEE targets). Accordingly, Sappi decided to unwind the Plantation BBBEE transaction and to implement the BBBEE transaction, a new sustainable transaction of equivalent value using its listed securities.

The BBBEE transaction has resulted in potentially 4.5% of the issued share capital of Sappi being held as follows:

- Sappi's South African employees (62.5%),
- South African black managers (15%),
- Strategic partners (12.5%) (refer below for more detail), and
- Communities surrounding the South African mill operations and plantations (10%).

The BBBEE transaction

The BBBEE transaction comprised two distinct parts:

- The value created through the Plantation BBBEE transaction was settled by the issue of 4.3 million fully paid-up ordinary shares at a price based on the 30-day volume weighted average share price (VWAP) of Sappi as at Friday, 05 February 2010 of R33.50.
- The creation and issuance of a new class of unlisted equity shares referred to as 'A' ordinary shares. The 'A' ordinary shares were issued at their par value of R1 to a trust formed for the benefit of certain Sappi employees including HDSAs (the 'ESOP Trust'), a trust formed for the benefit of certain Sappi managers that are HDSAs (the 'MSOP Trust') and a trust formed for the benefit of communities surrounding the major mills and/or plantations operated by Sappi in South Africa (the 'Sappi Foundation Trust', and together with the ESOP Trust and the MSOP Trust, the 'BBBEE trusts'). The issuance of the 'A' ordinary shares was financed through notional non-interest-bearing loans extended by Sappi to the BBBEE trusts. The BBBEE transaction resulted in the BBBEE trusts and the strategic partners holding, collectively, ordinary and 'A' ordinary shares equivalent to 4.5% of the share capital of Sappi Limited, which corresponds to an effective 30% interest in Sappi's South African business under the Forestry Charter and BBBEE legislation in general.

The number of ordinary shares allocated to the strategic partners and Sappi employees who were participants of the Plantation BBBEE transaction are as follows:

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

24. Share-based payments (continued)

	Ordinary share allocation
Strategic partners	
Lereko Investments Proprietary Limited	1,971,693
Malibongwe Women Development Trust	432,842
AMB Capital Limited	643,227
	<u>3,047,762</u>
Employees (through the ESOP Trust)	<u>1,280,597</u>
Total	<u>4,328,359</u>

The number of 'A' ordinary shares allocated to the BBBEE trusts are as follows:

Entity	A' ordinary share allocation
ESOP Trust	13,889,195
MSOP Trust	3,642,969
Sappi Foundation Trust	2,429,312
Total	<u>19,961,476</u>

The group incurred a share-based payment expense of R12.9 million (2017: R14.4 million) during the 2018 financial year that related to the 'A' ordinary shares that were awarded.

The following assumptions were utilised to determine the fair value of the 'A' ordinary shares granted:

Base price for hurdle rate price	ZAR 32.50
Share price hurdle rate	9.1%
Hurdle rate price	ZAR 72.18
Dividend yield (unadjusted)	3.0%
Volatility	40.0%
Dividend payout	Straight-line vesting
Straight-line dividend payout rate	50.0%
Employee turnover (annual)	7.1%
Management turnover (annual)	3.6%
Model used to value	Black Scholes model

Both the ESOP Trust and MSOP Trust have been set up with rules that detail the way in which the shares are allocated and how they are forfeited.

The vesting schedule for the MSOP Trust and ESOP Trust is illustrated below:

Completed months of service after effective date	Incremental vesting of entitlements (%)	Cumulative vesting of entitlements (%)
0 - 35	-	-
36 - 48	40	40
49 - 60	10	50
61 - 72	10	60
73 - 84	10	70
85 - 96	10	80
97 - 108	10	90
109 - termination date	10	100

25. Derivative financial instruments

R'millions		2018	2017
Hedging instrument	Hedged item		
Non-Current assets			
Forward exchange contracts	Various	54	-
		<u>54</u>	<u>-</u>
Current assets			
Interest rate swaps	ZAR500 and ZAR400 million loans	-	6
Forward exchange contracts	Various	123	15
		<u>123</u>	<u>21</u>
Current liabilities			
FX zero cost collar	Highly probable forecast sales	17	20
Forward exchange contracts	Various	63	-
		<u>80</u>	<u>20</u>

Refer to note 26 for more detail on financial instruments.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26. Financial instruments

The group's financial instruments consist mainly of cash and cash equivalents, trade receivables, certain investments, trade payables, borrowings and derivative instruments.

Introduction

The group's main financial risk management objectives are to identify, measure and manage, through financial instruments, the following principal risks to which the group is exposed to:

a) Market risk (the risk of loss arising from adverse changes in market rates and prices), arising from:

- Interest rate risk
- Currency risk and
- Commodity price risk

b) Liquidity risk and

c) Credit risk

Sappi's Group Treasury is primarily responsible for managing the group's interest rate, foreign currency, liquidity and credit risk (in so far as it relates to deposits of cash, cash equivalents and financial investments).

Credit risk, in so far as it relates to trade receivables, is primarily managed regionally but is co-ordinated on a group basis, whilst commodity price risk is managed regionally.

The group's Limits of Authority framework delegates responsibility and approval authority to various officers, committees and boards based on the nature, duration and size of the various transactions entered into by, and exposures of, the group including the exposures and transactions relating to those financial instruments and risks referred to in this note.

a) Market risk

Interest rate risk

Interest rate risk is the risk that the value of a borrowing or an investment will change due to a change in the absolute level of interest rates, the spread between two rates, the shape of the yield curve or any other interest rate relationship.

The group is exposed to interest rate risk as it borrows funds at both fixed and floating interest rates. The group monitors market conditions and may utilise approved interest rate derivatives to alter the existing balance between fixed and variable interest rate loans in response to changes in the interest rate environment. Hedging of interest rate risk for periods greater than one year is only allowed if income statement volatility can be minimised by means of hedge accounting, fair value accounting or other means. The group's exposure to interest rate risk is set out below.

Interest-bearing borrowings

The following table provides information about Sappi's principal amounts of current and non-current borrowings that are sensitive to changes in interest rates. The table presents cash flows of the carrying value by expected maturity dates and the estimated fair value of borrowings. The average fixed effective interest rates presented are based on weighted average contract rates applicable to the amount expected to mature in each respective year. Forward-looking average variable effective interest rates for the financial years ended September 2018 and thereafter are based on the yield curves for each respective currency as published by Bloomberg on 1 October 2018.

	Expected maturity date				2018 Carrying value	2018 Fair Value	2017 Carrying Value	2017 Fair Value
	2019	2020	2021	2022				
Rand millions								
Fixed rate debt	-	745	-	-	745	775	1,645	1,724
Average interest rate (%)	-	8.06	-	-	8.06		7.83	
Variable rate debt	-	400	-	-	400	424	-	-
Average interest rate (%)	-	9.46	-	-	9.46			
Fixed and variable	-	1,145	-	-	1,145	1,199	1,645	1,724
Current portion					-	-	500	512
Long-term portion					1,145	1,199	1,145	1,212
Total interest-bearing borrowings (refer to note 16)					1,145	1,199	1,645	1,724

For disclosure purposes, the fair value of non-current borrowings is estimated by Sappi based on rates from market quotations for non-current borrowings with fixed interest rates and on quotations provided by internationally recognised pricing services for notes, exchange debentures and revenue bonds.

The abovementioned fair values include Sappi's own credit risk. Please refer to the sensitivity analysis on interest rate risk in this note for additional information regarding Sappi's rating.

A detailed analysis of the group's borrowings is presented in note 16.

Sensitivity analyses

Sensitivity analysis: interest rate risk - in case of a credit rating change of Sappi Southern Africa Limited

To the extent of any downgrade on the group's revolving credit facility, a change in the group's own credit rating will affect the funding rate. Assuming an annual drawdown of R1 million, a one notch downgrade will negatively impact profit before tax by R0.3 million (2017:R0.4 million) and a one notch upgrade will have a Rnil (2017:R0.3 million) positive impact. The revolving credit facility was undrawn at financial year-end.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26. Financial instruments (continued)

Currency risk

The objective of the group in managing currency risk is to ensure that foreign exchange exposures are identified as early as possible and actively managed. Sappi is exposed to the following currency risks:

- Economic exposures which consist of planned net foreign currency trade in goods and services not yet manifested in the form of actual invoices and orders, and
- Transaction exposures arise from transactions entered into which result in a flow of cash in foreign currency such as payments under foreign currency long- and short-term loan liabilities, purchases and sales of goods and services, capital expenditure and dividends. Where possible, commercial transactions are only entered into in currencies that are readily convertible by means of formal external forward exchange contracts.

In managing currency risk, the group first makes use of internal hedging techniques with external hedging being applied thereafter.

External hedging techniques consist primarily of foreign currency forward exchange contracts. Foreign currency capital expenditure on projects must be covered as soon as practical (subject to regulatory approval).

Currency risk analysis

In the preparation of the currency risk analysis, derivative instruments are allocated to the currency of the hedged item.

The following tables for the 2018 and 2017 financial years disclose financial instruments as determined by IAS 39 *Financial Instruments: Recognition and Measurement*, classified by underlying currency, and does not indicate the group's foreign currency exchange exposure.

September 2018

R'million	Total	Total in scope	Currency				
			USD	EUR	ZAR	GBP	Other
Classes of financial instruments							
Non-current assets							
Derivative financial instruments	54	54	-	54	-	-	-
Amounts owing by group companies	4,377	4,377	-	-	4,377	-	-
Current assets							
Trade and other receivables	610	304	-	-	304	-	-
Derivative financial instruments	123	123	69	48	-	-	6
Amounts owing by group companies	2,155	2,155	-	-	2,155	-	-
Cash and cash equivalents	1,014	1,014	-	-	1,014	-	-
		8,027	69	102	7,850	-	6
Non-current liabilities							
Interest-bearing borrowings	1,145	1,145	-	-	1,145	-	-
Current liabilities							
Interest-bearing borrowings	-	-	-	-	-	-	-
Trade and other payables	3,675	3,256	-	-	3,256	-	-
Derivative financial instruments	80	80	-	-	80	-	-
Amounts owing to the group	218	218	-	-	218	-	-
		4,699	-	-	4,699	-	-
Foreign exchange gap		3,328	69	102	3,151	-	6

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26 Financial instruments (continued) September 2017 R'million	Total	Total in scope	Currency				
			USD	EUR	ZAR	GBP	Other
Classes of financial instruments							
Non-current assets							
Derivative financial instruments	-	-	-	-	-	-	-
Current assets							
Trade and other receivables	347	274	58	-	216	-	-
Derivative financial instruments	21	22	(1,363)	244	1,086	1	54
Amounts owing by the group	5,139	5,139	-	-	5,139	-	-
Cash and cash equivalents	2,923	2,924	17	13	2,885	3	6
		8,359	(1,288)	257	9,326	4	60
Non-current liabilities							
Interest-bearing borrowings	1,145	1,145	-	-	1,145	-	-
Current liabilities							
Interest-bearing borrowings	500	500	-	-	500	-	-
Trade and other payables	2,842	2,398	238	62	2,088	3	7
Derivative financial instruments	20	20	-	-	20	-	-
Amounts owing to the group	223	223	-	-	223	-	-
		4,286	238	62	3,976	3	7
Foreign exchange gap		4,073	(1,526)	195	5,350	1	53

Hedging of foreign currency risk

Foreign currency forward exchange contracts

The group's foreign currency forward exchange contracts at September are detailed below:

		2018		2017	
		Contract amount (notional amount) R'millions	Fair value (unfavourable) favourable R'millions	Contract amount (notional amount) R'millions	Fair value (unfavourable) favourable R'millions
Foreign currency					
Bought:	US Dollar	731	721	165	162
	Euro	1,400	1,311	308	300
	Swedish Krona	124	118	53	52
	Japanese yen	3	4	-	-
	GBP	1	1	1	1
		-	-	1	1
Sold:	Euro	(299)	(310)	(64)	(64)
	US Dollar	(1,012)	(1,057)	(1,528)	(1,532)
	Swedish Krona	(3)	(3)	-	-
	Japanese yen	(1)	(1)	-	-
		944	784	(1,064)	(1,080)

The fair value of foreign currency contracts has been computed by the group using the market data at the end of the 2018 financial year.

All forward exchange contracts are valued at fair value with the resultant profit or loss included in net finance costs for the year.

The foreign currency forward exchange contracts have different maturities, with the most extended maturity date being 31 August 2020.

As at September 2018, there was an open exposure of R34.9 million that has since been hedged.

Sensitivity analysis - (loss) gain

Base currency	Exposure R'millions	+ 10 % R'millions	- 10 % R'millions
CHF	-	-	-
EUR	(23)	(2)	3
GBP	-	-	-
JPY	-	-	-
SEK	-	-	-
USD	(12)	(1)	1
TOTAL	(35)	(3)	4

Based on the exposure at the end of September 2018, if the foreign currency rates had moved 10% upwards or downwards compared to the closing rates, the result would have been impacted by a loss of R3.2 million or a gain of R3.9 million respectively.

During 2018, we contracted non-deliverable average rate foreign exchange transactions for a total notional value of US\$301.0 million which were used as an overlay hedge of export sales from Southern Africa. We also contracted zero cost foreign exchange collars for a total notional value of US\$220 million. This collar complements the other strip cover hedges (using non-deliverable FX forwards) by covering a different portion of the economic FX exposure. The total combined impact on profit or loss amounted to a profit of R23.5 million (including positive forward points of R45.7 million and R22.2 million negative spot to spot movements).

As at September 2018 the impact of the marking to market relating to the time value of the collar amounted to an unrealised loss of R53.5 million.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26. Financial instruments (continued)

Cash flow hedges

Export sales

In Southern Africa, Sappi is exposed to an economic risk arising from its export sales of its dissolving wood pulp product. As sales prices are linked to a US Dollar price but sales are invoiced in Rand, any change in the foreign currency exchange rate between the US Dollar and the Rand would result in a different Rand selling price. This results in an economic foreign currency exchange rate exposure between the order date and invoicing date.

Sappi therefore enters into cash flow hedges with the objective to eliminate this economic foreign exchange rate exposure by entering into non-deliverable forward exchange contracts and zero cost foreign exchange collars which were designated as hedging instruments. Only the intrinsic value of the zero cost foreign exchange collar is designated as the hedging instrument.

The hedging instruments are recorded at fair value on the balance sheet with changes in fair value recorded through OCI. In assessing the effectiveness of the hedge of the foreign currency risk, Sappi compares the critical terms (expected maturity dates, underlying foreign currencies and the notional amounts) of the hedging instrument to the hedged item. An assessment is then performed on a cumulative basis at each reporting period. Throughout the hedge designation, the hedge relationship has been assessed to be highly effective in offsetting changes in the cash flows attributable to the hedged risk.

During the 2018 financial year, the hedge was highly effective and a net realised loss of R23.0 million (2017:R251.8 million) relating to the realised non-deliverable forward exchange contracts was transferred from OCI to sales. At the financial year-end, a positive amount of R22.3 million (2017:R1.9 million) was deferred in equity.

a) Liquidity risk

Liquidity risk is the risk that the group will be unable to meet its current and future financial obligations as they fall due.

The group's objective is to manage its liquidity risk by:

- managing its bank balances, cash concentration methods and cash flows,
- managing its working capital and capital expenditure,
- ensuring the availability of a minimum amount of short-term borrowing facilities at all times, to meet any unexpected funding requirements, and ensuring appropriate long-term funding is in place to support the group's long-term strategy.

Details of the group's borrowings, including the maturity profile thereof, as well as the group's committed and uncommitted facilities are set out in note 16.

The group is in compliance with all material financial covenants applicable to its borrowing facilities.

Liquidity risk management

The following tables for the 2018 and 2017 financial years disclose financial instruments, as determined by IAS 39 *Financial Instruments: Recognition and Measurement*, are classified by liquidity and does not necessarily indicate the group's actual cash flows.

September 2018

R'millions	Total financial assets and liabilities	Fair value of financial instruments	Undiscounted cash flows					Total
			0-6 months	6-12 months	1-2 years	2-5 years	> 5 years	
Non-current assets								
Derivative financial instruments	54	54			54	-	-	54
Amounts owing by the group	4,377	4,377				4,377		4,377
Current assets								
Trade and other receivables	304	304	304	-	-	-	-	304
Derivative financial instruments	123	123	68	55	-	-	-	123
Amounts owing by the group	2,155	2,155	2,155	-	-	-	-	2,155
Cash and cash equivalents	1,014	1,014	1,014	-	-	-	-	1,014
			3,541	55	54	4,377	-	8,027
Non-current liabilities								
Interest-bearing borrowings	1,145	1,145			1,145			1,145
Current liabilities								
Trade and other payables	3,257	3,257	3,257	-	-	-	-	3,257
Derivative financial instruments	80	80	80	-	-	-	-	80
Amounts owing to the group	218	218	218	-	-	-	-	218
			3,555	-	1,145	-	-	4,700
Liquidity surplus (gap)			(14)	55	(1,091)	4,377	-	3,327

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26 Financial instruments (continued) September 2017

R'millions	Total financial assets and liabilities	Fair value of financial instruments	Undiscounted cash flows					Total
			0-6 months	6-12 months	1-2 years	2-5 years	> 5 years	
Current assets								
Trade and other receivables	274	274	274	-	-	-	-	274
Derivative financial instruments	21	21	2	19	-	-	-	21
Amounts owing by the group	5,139	5,139	5,139	-	-	-	-	5,139
Cash and cash equivalents	2,923	2,923	2,923	-	-	-	-	2,923
			8,338	19	-	-	-	8,357
Non-current liabilities								
Interest-bearing borrowings	1,145	1,145	-	-	-	1,145	-	1,145
Current liabilities								
Trade and other payables	2,897	2,897	2,397	500	-	-	-	2,897
Derivative financial instruments	20	20	20	-	-	-	-	20
Amounts owing to the group	223	223	223	-	-	-	-	223
			2,640	500	-	1,145	-	4,285
Liquidity surplus (gap)			5,698	(481)	-	(1,145)	-	4,072

Derivative financial instruments with maturity profile

The following tables indicate the different types of derivative financial instruments for the 2018 and 2017 financial years that are included within the various categories on the balance sheet. The reported maturity analysis is calculated on an undiscounted basis.

September 2018

R'millions	Maturity analysis					
	Undiscounted cash flows					
	Total	0-6 months	6-12 months	1-2 years	2-5 years	> 5 years
Classes of derivative financial instruments						
Foreign exchange risk						
Short term - FEC's	177	67	56	54	-	-
- paying leg	(34)	(34)	-	-	-	-
- receiving leg	211	101	56	54	-	-
Liabilities						
Fair value of derivatives by risk factor						
Foreign exchange risk						
Short term - FEC's	80	80	-	-	-	-
- paying leg	80	80	-	-	-	-
- receiving leg	-	-	-	-	-	-

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26. Financial instruments (continued)
September 2017

R'millions	Maturity analysis					
	Undiscounted cash flows					
Classes of derivative financial instruments	Total	0-6 months	6-12 months	1-2 years	2-5 years	> 5 years
Assets						
Fair value of derivatives by risk factor						
Interest rate risk						
Long term - Interest rate swaps	6	2	4	-	-	-
- paying leg	(63)	(39)	(24)	-	-	-
- receiving leg	69	41	28	-	-	-
Foreign exchange risk						
Short term - FEC's	15	12	3	-	-	-
- paying leg	(1,065)	(1,213)	148	-	-	-
- receiving leg	1,080	1,225	(145)	-	-	-
Liabilities						
Fair value of derivatives by risk factor						
Foreign exchange risk						
Short term - FEC's	20	20	-	-	-	-
- paying leg	-	-	-	-	-	-
- receiving leg	20	20	-	-	-	-

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26. Financial instruments (continued)

Fair values

The group's financial instruments are initially recognized at fair value. The carrying amounts of other financial instruments which include cash and cash equivalents, accounts receivable, certain investments, accounts payable and the current portion of interest-bearing borrowings approximate their fair values due to their short-term nature.

As a result of the implementation of IFRS 13 Fair Value Measurement, the fair value of all financial instruments measured at fair value, are measured based on a market exit price incorporating credit risk, by using standard valuation techniques based on observable market data inputs.

The fair value of all external over-the-counter derivatives and material non-current borrowings (for disclosure purposes only) is calculated based on the discount rate adjustment technique. The discount rate used is derived from observable rates of return for comparable assets or liabilities traded in the market. The credit risk of the external counterparty is incorporated into the calculation of fair values of financial assets and own credit risk is incorporated in the measurement of financial liabilities. The change in fair value is therefore impacted by the move of the interest rate curves, by the volatility of the applied credit spreads, and by any changes of the credit profile of the involved parties.

There are no financial assets and liabilities that have been remeasured to fair value on a non-recurring basis. The carrying value of assets and liabilities (excluding plantations) which are held for sale, are considered to be below their net recoverable amount.

Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured, are measured at cost.

September 2018

	Total balance	Total out of scope	Total in scope	Categories in accordance with IAS 39		Fair value
				Fair value through profit or loss	Loans and receivables	
R'millions						
Classes of financial instruments						
Non-current assets						
Derivative financial instruments	54	-	54	-	-	54
Amounts owing by group companies	4,377	-	4,377	-	4,377	4,377
	4,431	-	4,431	-	4,377	4,431
Current assets						
Trade and other receivables	610	306	304	-	304	304
Derivative financial instruments	123	-	123	123	-	123
Amounts owing by group companies	2,155	-	2,155	-	2,155	2,155
Cash and cash equivalents	1,014	-	1,014	-	1,014	1,014
	3,902	306	3,596	123	3,473	3,596

	Total balance	Total out of scope	Total in scope	Categories in accordance with IAS 39		Fair value
				Fair value through profit or loss	Other financial liabilities	
R'millions						
Classes of financial instruments						
Non-current liabilities						
Interest-bearing borrowings	1,145	-	1,145	-	1,145	1,145
Other non-current liabilities	271	271	-	-	-	-
	1,416	271	1,145	-	1,145	1,145
Current liabilities						
Derivative financial instruments	80	-	80	80	-	80
Trade and other payables	3,675	418	3,257	-	3,257	3,257
Amounts owing to group companies	218	-	218	-	218	218
	3,973	418	3,555	80	3,475	3,555

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26. Financial instruments (continued)

R'millions	As determined by IAS 39			Categories in accordance with IAS 39		Fair value
	Total balance	Total out of scope	Total in scope	Fair value through profit or loss	Loans and receiv- ables	
September 2017						
Classes of financial instruments						
Non-current assets						
Other non-current assets	302	302	-	-	-	-
	302	302	-	-	-	-
Current assets						
Trade and other receivables	347	73	274	-	274	274
Derivative financial instruments	21	-	21	21	-	21
Amounts owing by group companies	5,139	-	5,139	-	5,139	5,139
Cash and cash equivalents	2,923	-	2,923	-	2,923	2,923
	8,430	73	8,357	21	8,336	8,357
	Total balance	Total out of scope	Total in scope	Fair value through profit or loss	Other financial liabilities	Fair value
Classes of financial instruments						
Non-current liabilities						
Interest-bearing borrowings	1,145	-	1,145	-	1,145	1,145
Other non-current liabilities	254	254	-	-	-	-
	1,399	254	1,145	-	1,145	1,145
Current liabilities						
Interest-bearing borrowings	500	-	500	-	500	500
Derivative financial instruments	20	-	20	20	-	20
Trade and other payables	2,842	445	2,397	-	2,397	2,397
Amounts owing by group companies	223	-	223	-	223	223
	3,585	445	3,140	20	3,120	3,140

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

26. Financial instruments (continued)

The level in the fair value hierarchy into which financial instruments, that are measured at fair value, are categorised is disclosed below. There have been no transfers between the categories of the fair value hierarchy.

R'millions	2018				2017			
	Total fair value	Fair value hierarchy			Total fair value	Fair value hierarchy		
		Level 1	Level 2	Level 3		Level 1	Level 2	Level 3
Non-current assets								
Derivative financial instruments	54	-	54	-	-	-	-	-
Current assets								
Derivative financial instruments	123	-	123	-	21	-	21	-
	177	-	177	-	21	-	21	-
Non-current liabilities								
Interest-bearing borrowings	1,145	-	1,145	-	1,145	-	1,145	-
Current liabilities								
Interest-bearing borrowings	-	-	-	-	500	-	500	-
Derivative financial instruments	80	-	80	-	20	-	20	-
	1,225	-	1,225	-	1,665	-	1,665	-

c) Credit risk

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in a financial loss to the group. The group faces credit risk in relation to trade receivables, cash deposits and financial investments.

Credit risk relating to trade receivable management is the responsibility of regional management and is coordinated on a group basis.

The group's objective in relation to credit risk is to limit the exposure to credit risk through specific groupwide policies and procedures. Credit control procedures are designed to ensure the effective implementation of best trade receivable practices, the comprehensive maintenance of all related records, and effective management of credit risk for the group.

The group assesses the creditworthiness of potential and existing customers in line with its credit policies and procedures. Collateral is obtained to minimise risk. Exposures are monitored on an ongoing basis utilising various reporting tools which highlight potential risks when considered appropriate.

In the event of deterioration of credit risk, the appropriate measures are taken by the regional credit management team. All known risks are required to be fully disclosed, accounted for, and provided for as bad debts in accordance with the applicable accounting standards.

Overall, 94% of the group's total trade receivables, both on- and off-balance sheet, are insured or covered by letters of credit and bank guarantees.

Quantitative disclosures on credit risk are included in note 12.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

27. Related parties

Details of transactions between the group and other related parties are disclosed below:

R'millions	Income and sales to related parties		Purchases and charges from related parties		Amounts owed by related parties		Amounts owed to related parties	
	2018	2017	2018	2017	2018	2017	2018	2017
Sappi Europe SA**	6	-	178	268	-	-	48	65
Sappi International SA**	-	-	-	-	-	3	-	-
Sappi Limited***	10	-	96	-	4,377 *	3,348	-	-
Sappi Papier Holding GmbH**	10,595	11,049	24	33	2,148	1,788	-	-
The Sappi Limited Share Incentive Trust	-	-	-	-	-	-	-	13
The Sappi Limited Performance Share Incentive Trust	-	-	-	-	-	-	67	145
The Sappi Share Facilitation (Pty) Ltd	-	-	-	-	-	-	103	-
Sappisure Försäkrings AB**	-	-	55	-	7	-	-	-
	10,611	11,049	353	301	6,532	5,139	218	223

* Management's intention has changed and will not call on this receivable in the short term

** Fellow subsidiary of Sappi Limited

*** Holding company of SSA

Ngodwana energy investment of R23 million and Shareholder loan of R45 million provided by Sappi Southern Africa

All loans are interest free and are repayable on demand.

Sales of goods and purchases to and from related parties were on an arm's length basis.

The amounts outstanding at balance sheet date are unsecured and will be settled in cash.

Dividends received from equity accounted investee (current year Dividends Received)

2018	2017
77	91

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Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

27. Related party transactions (continued)

Broad-based Black Economic Empowerment (BBBEE) transaction

Refer to note 25 for details of the BBBEE transaction.

Shareholders

The company's shares are held by Sappi Limited which has a primary listing on the JSE Limited.

Key management personnel

The details of key management personnel compensation is disclosed below:

R'000	Prior year bonuses and performance related payments		Sums paid by way of expense allowance	Contributions paid under pension and medical aid scheme	Total
	Salary				
Steve Binnie	7,287	5,866	194	1,111	14,458
Glen Pearce	4,214	3,785	111	828	8,938
Alex Thiel	4,392	3,178	123	799	8,492
Pramy Moodley	2,011	805	-	436	3,252
Key management remuneration - 2018	17,904	13,634	428	3,174	35,140
Steve Binnie	6,104	6,264	162	1,025	13,555
Glen Pearce	4,050	4,301	111	818	9,280
Alex Thiel	4,226	3,136	124	792	8,278
Pramy Moodley	1,425	-	-	323	1,748
Total - ex directors *	12,502	11,939	171	2,951	27,563
Key management remuneration - 2017	28,307	25,640	568	5,909	60,424

There were four Directors on the Board at the end of the Fiscal 18.

* On the 1 April 2017 eleven directors resigned from their position as directors of the Company.

Interest of directors in contracts

None of the directors have material interests in any transaction with the company or any of its subsidiaries, other than those on a normal employment basis.

Subsidiaries

Details of investments in subsidiaries are disclosed in note 30.

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued)
for the year ended September 2018

27. Related party transactions (continued)

Changes in key management personnel share options, allocations and performance shares

		S. Binnie	A. Thiel	G. Pearce	P. Moodley	Total 2018	Total 2017
	Allocated price	Number of shares	Number of shares	Number of shares	Number of shares	Number of shares	Number of shares
Outstanding at beginning of year							
Number of shares		837,000	605,000	283,000	54,300	1,779,300	3,185,900
A Ordinary shares	R 72.18	-	-	-	16,200	16,200	-
Share option - issue 36	R 35.20	-	-	-	-	-	8,000
Share option - issue 37	R 22.90	-	-	-	-	-	10,500
Performance shares 38	R 0.00	-	-	-	-	-	574,400
Performance shares 39	R 0.00	310,000	310,000	33,000	5,200	658,200	1,036,000
Performance shares 40	R 0.00	175,000	100,000	85,000	5,000	365,000	712,000
Performance shares 41	R 0.00	190,000	105,000	90,000	5,900	390,900	845,000
Performance shares 42	R 0.00	162,000	90,000	75,000	22,000	349,000	-
Appointment of executive director during the year							
Number of shares		-	-	-	-	-	54,300
Offered and accepted during the year							
Performance shares 42		-	-	-	-	-	684,000
Performance shares 43		137,000	76,000	63,000	22,000	298,000	-
Exercised during the year							
Number of shares		(310,000)	(310,000)	(33,000)	(5,200)	(658,200)	(585,400)
Returned, lapsed and forfeited during the year							
Number of shares		-	-	-	-	-	-
Resignation of director during the year							
Number of shares		-	-	-	-	-	(1,559,500)
Outstanding at end of year							
Number of shares		664,000	371,000	313,000	71,100	1,419,100	1,779,300
A Ordinary shares	R 72.18	-	-	-	16,200	16,200	16,200
Performance shares 39	R 0.00	-	-	-	-	-	658,200
Performance shares 40	R 0.00	175,000	100,000	85,000	5,000	365,000	365,000
Performance shares 41	R 0.00	190,000	105,000	90,000	5,900	390,900	390,900
Performance shares 42	R 0.00	162,000	90,000	75,000	22,000	349,000	349,000
Performance shares 43	R 0.00	137,000	76,000	63,000	22,000	298,000	-

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements (continued) for the year ended September 2018

28. Events after balance sheet date

In January 2019 Sappi Southern Arica Limited funded R1.36 billion to Sappi Limited as per a loan agreement. This was done to enable Sappi Limited to pay dividends that were declared. This loan bears no interest, and is re-payable on demand.

29. Investment in subsidiaries

Set out below are the more significant subsidiaries of the group as at financial year-end:

Name of subsidiary	Share Capital (Rands)	Principal activity	Effective holding (%)	
			2018	2017
Canonbrae Development Company Proprietary Limited	1,000	Property developments	63.2%	63.2%
Sappi Property Company Proprietary Limited	7,000	Land holdings	100.0%	100.0%

Sappi Southern Africa Limited

Notes to the Group Annual Financial Statements for the year ended September 2018

30. Segment information

The group's reportable segments comprise Specialised Cellulose and Packaging and Specialities which is the basis of how the group allocates resources and evaluates performance. The Specialised Cellulose segment sells dissolving wood pulp and the Packaging and paper pulp, uncoated and commodity paper.

The group accounts for intra-group sales and transfers as if the sales or transfers were to third parties. All such sales and transfers are eliminated on consolidation.

The group regards its primary measures of segment performance as operating profit excluding special items.

R'millions	Specialised Cellulose		Packaging & Specialities		Group	
	2018	2017	2018	2017	2018	2017
External sales including external forestry sales	10,870	10,742	6,997	7,096	17,867	17,839
Operating profit excluding special items	2,291	3,465	671	460	2,962	3,925
Reconciliation of operating profit excluding special items to profit before taxation:						
Operating profit excluding special items	2,291	3,464	744	460	2,962	3,925
Special items* - gains (losses)					331	124
Net finance costs					85	93
Profit before taxation					3,378	4,142

There is no one customer whose sales comprise more than 10% of the group's turnover in the current financial year.

- * Special items cover those items which management believe are material by nature or amount to the operating results and require separate disclosure. Such items would generally include profit or loss on disposal on property, investments and businesses, asset impairments, restructuring charges, non recurring integration costs related to acquisitions, financial impacts of natural disasters, non cash gains or losses on the price fair value adjustment of plantations and alternative fuel tax credits receivable in cash.

Sappi Southern Africa Limited

Annexure A

for the year ended September 2018

Definitions

- FSC:** In terms of the Forest Stewardship Council® (FSC®) scheme, there are two types of certification. In order for forest land to achieve FSC certification, its forest management practices must meet the FSC 10 principles based on environmental, social and economic criteria. Roundwood (logs) with FSC-certification: Sappi Southern Africa Forests FSC C012316 and Sappi Southern Africa Group Scheme FSC – C017054. For manufacturers of forest products, including paper manufacturers like Sappi, Chain-of-Custody (CoC)-certification involves independent verification of the supply chain, which identifies and tracks the timber through all stages of the production process from the tree farm to the end product. Sappi's mills in South Africa are licenced – Ngodwana Mill – FSC C021636, Saiccor Mill - FSC C011012, Stanger Mill – FSC C019831 and Tugela Mill – FSC C012468
- ISO:** Developed by the International Standardisation Organisation ("ISO"), ISO 9000 is a series of standards focused on quality management systems, while the ISO 14001 series is focused on environmental performance and management
- NBSK:** Northern Bleached Softwood Kraft pulp. One of the main varieties of market pulp, produced from coniferous trees (ie spruce, pine) in Scandinavia, Canada and northern USA
- OHSAS:** Is an international health and safety standard aimed at minimising occupational health and safety risks firstly, by conducting a variety of analyses and secondly, by setting standards



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