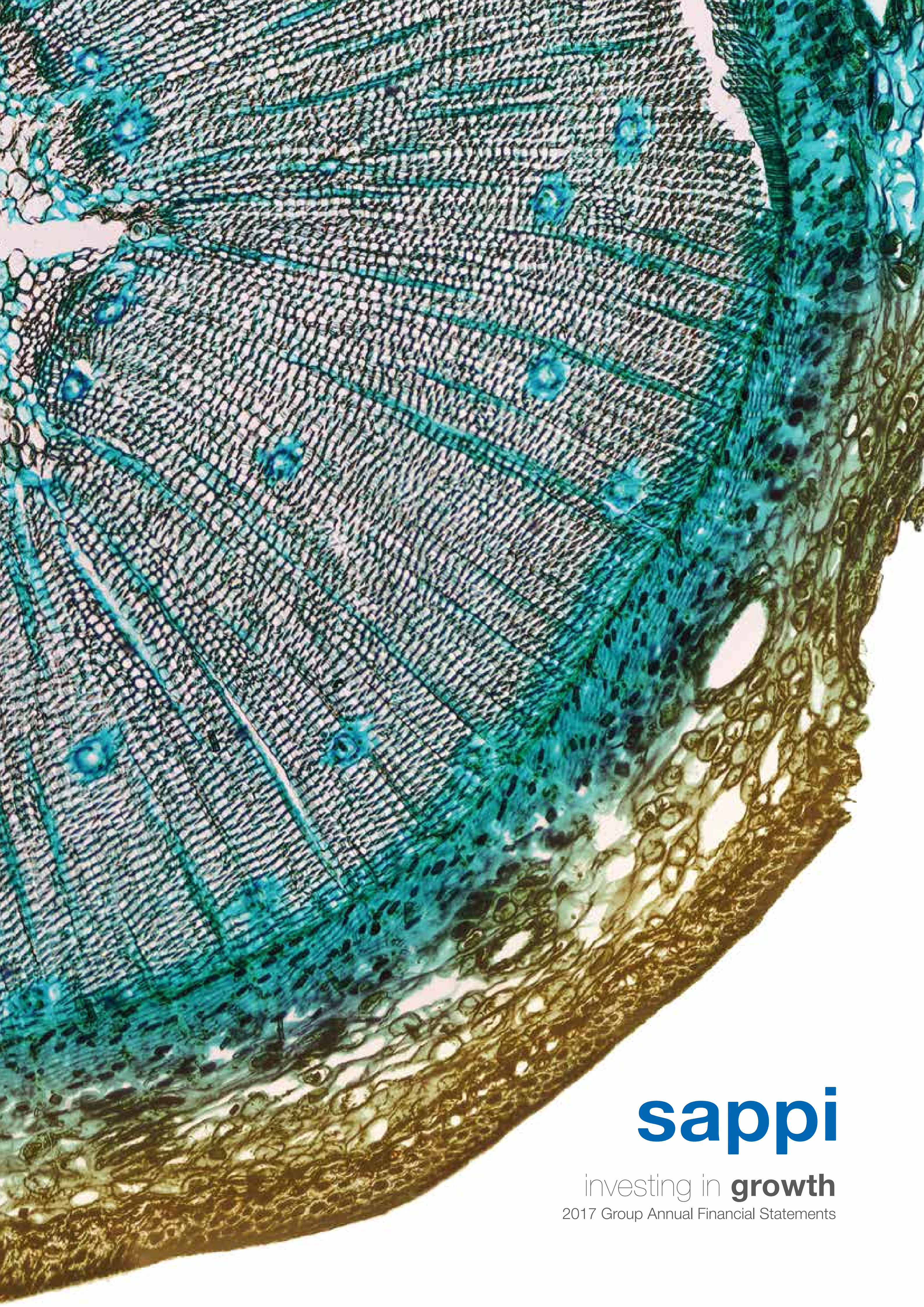

# sappi

investing in **growth**

2017 Group Annual Financial Statements

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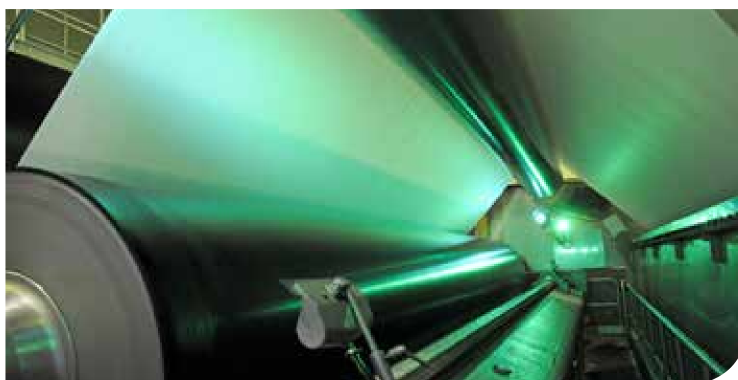
**Through the power of One Sappi** – committed to collaborating and partnering with stakeholders – we aim to be a trusted and sustainable organisation with an exciting future in woodfibre.



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# Directors' approval

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 and the SAICA Financial Reporting Guides as issued by the Accounting Practices Committee, the Financial Reporting Pronouncements as issued by Financial Reporting Standards Council and, the JSE Limited Listings Requirements and the requirements of the Companies Act of South Africa. In preparing the group financial statements, the group applied appropriate accounting policies supported by reasonable judgements and estimates. 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 by the group and are committed to maintaining a strong control environment. Details relating to the group's internal control environment are set out in the *Corporate governance* section of the Annual Integrated Report.

The directors are of the opinion, based on the information and explanations given by the company's officers and the internal auditors, 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, has satisfied the directors that the group will continue as a going concern for the foreseeable future. The group, therefore, continues to adopt the going concern basis in preparing its group financial statements.

The Directors' Report and the Group Annual Financial Statements appear on pages 4 to 88 and were approved by the board of directors on 07 December 2017 and signed on its behalf by:

**SR Binnie**
*Chief Executive Officer*

**GT Pearce**
*Chief Financial Officer*

Sappi Limited

07 December 2017

# Group 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 2017, 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 Southern Africa Limited**
*Secretaries*

per AJ Tregoning
*Group Company Secretary*

07 December 2017

# Audit Committee Report

for the year ended September 2017

## Introduction

The Audit Committee presents its report for the financial year ended September 2017. The Audit Committee is an independent statutory committee, whose duties are delegated to it by the board of directors. The committee has conducted its affairs in compliance with board-approved terms of reference, and has discharged its responsibilities contained therein.

## Objectives and scope

The overall objectives of the committee are:

- To assist the board in discharging its duties relating to the safeguarding of assets and the operation of adequate systems and control processes
- To control reporting processes and the preparation of financial statements in compliance with the applicable legal and regulatory requirements and accounting standards
- To provide a forum for the governance of risk, including control issues and developing recommendations for consideration by the board
- To oversee the internal and external audit appointments and functions, and
- To perform duties that are attributed to it by the South African Companies Act of 2008 (the Companies Act), the JSE Limited Listings Requirements and King IV.

Committee performance:

- Received and reviewed reports from both internal and external auditors concerning the effectiveness of the internal control environment, systems and processes
- Reviewed the reports of both internal and external audit findings and their concerns arising out of their audits and requested appropriate responses from management
- Made recommendations to the board of directors regarding the corrective actions to be taken as a consequence of audit findings
- Ensured that appropriate financial reporting procedures are being maintained and are operating effectively
- Considered the independence and objectivity of the external auditors and ensured that the scope of their additional services provided did not impair their independence
- Received and dealt with concerns and complaints through 'whistle-blowing' mechanisms that were reported to the committee by the group internal audit function
- Reviewed a documented assessment, including key assumptions, prepared by management on the going concern status of the group, and accordingly made recommendations to the board
- Reviewed and recommended for adoption by the board the financial information that is publicly disclosed, which included:
  - The Annual Integrated Report
  - The Group Annual Financial Statements, and
  - The quarterly financial results
- Considered the effectiveness of internal audit, approved the annual operational strategic internal audit plan and monitored adherence of internal audit to its plan
- Reviewed the performance and expertise of the Chief Financial Officer and confirmed his suitability for the position, and
- Satisfied itself that the internal audit function is efficient and effective and carried out its duties in an independent manner in accordance with a board approved Internal Audit Charter.

The committee is satisfied that it has fulfilled its obligations in respect of its scope of responsibilities.

## Membership

The membership of the committee comprises independent non-executive directors, all of whom are financially literate, with three members forming a quorum:

| | |
|---|---|
| Dr D Konar (Chairman) | (Appointed in January 2004, Chairman from January 2007) |
| Mr RJAM Renders | (Appointed in March 2017) |
| Mr MA Fallon | (Appointed in January 2012) |
| Mr NP Mageza | (Appointed in February 2010) |
| Mrs KR Osar | (Appointed in November 2007) |
| Mr GPF Beurskens | (Retired in February 2017) |

Biographical details of the current members of the committee are set out on our website, www.sappi.com.

In addition, the Chief Executive Officer, the Chief Financial Officer, Head of Group Internal Audit, the risk executive and the external auditors are also permanent invitees to the meeting. The Chairman of the board attends meetings ex officio. The effectiveness of the committee is assessed every year. In terms of the Companies Act, the committee is required to be elected annually at the Annual General Meeting.

## External audit

The committee, having considered all relevant matters, satisfied itself through enquiry that auditor independence, objectivity and effectiveness were maintained in 2017. Meetings were held with the auditors where management was not present.

No material non-audit services were provided by the external auditors during the year under review.

The committee has consequently nominated, for approval at the Annual General Meeting, KPMG as the external auditor for the 2018 financial year of whom Mr Coenie Basson is the designated auditor. The committee confirms that the auditor and designated auditor are accredited by the JSE Limited.

## Annual Integrated Report and the Group Annual Financial Statements

The Audit Committee has evaluated the Annual Integrated Report, incorporating the Group Annual Financial Statements, for the year ended September 2017. The Audit Committee has also considered the sustainability information as disclosed in the Annual Integrated Report and has assessed its consistency with operational and other information known to Audit Committee members. The committee has also considered the report and is satisfied that the information is reliable and consistent with the financial results. The Group Annual Financial Statements have been prepared using appropriate accounting policies, which conform to International Financial Reporting Standards.

The committee has therefore recommended the Annual Integrated Report and the Group Annual Financial Statements for approval to the board. The board has subsequently approved the Annual Integrated Report and the Group Annual Financial Statements, which will be open for discussion at the Annual General Meeting.

Based on the results of the formal documented review of the group's system of internal financial controls for the year which was performed by the internal audit function and external auditors, nothing has come to the attention of the Audit Committee to indicate that the internal financial controls were not operating effectively.

**D Konar**
*Chairman of the Audit Committee*

07 December 2017

# Directors' Report

for the year ended September 2017

The directors have pleasure in presenting their report for the year ended September 2017.

## Nature of business

Sappi is a global diversified woodfibre company focused on providing dissolving wood pulp, specialities and packaging papers, graphic/printing papers, as well as biomaterials and biochemicals to our direct and indirect customer base across more than 150 countries.

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, luxury carry bags, 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, textiles, automobile and household industries. Our market-leading range of coated and uncoated graphic paper products are used by printers in the production of books, brochures, magazines, catalogues, direct mail, newspapers and many other print applications.

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.

## Financial results

The group generated a profit of US$338 million for the year ended September 2017 (63 US cents) compared to US$319 million profit (60 US cents) for the prior year.

Detailed commentary on the 2017 financial results is contained in various reviews throughout the Annual Integrated Report.

## Dividends

The directors have declared a dividend of 15 US cents per share, payable in Rand using the exchange rate at the date of declaration, representing a four times earnings cover adjusted for non-cash items.

## 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.

## Corporate governance

Sappi is committed to high standards of corporate governance and endorses the recommendations contained in the King Code of Corporate Governance principles. Please refer to our *Corporate governance* section contained in our Annual Integrated Report for full details and to our website for Sappi's application of the principles of King IV.

## Health, safety, environment and community

Information on our health, safety and environmental performance is provided in the *Sustainability* section in our Annual Integrated Report.

## Significant announcements during the year under review and subsequent to year-end

There were two significant announcements:
- In March 2017 the group announced the redemption of its US$400 million public bond due July 2017 at par during the call window period from available cash resources. This was repaid in April 2017.
- On 05 December 2017, Sappi agreed to acquire the speciality paper business of Cham Paper Group Holding AG (CPG) for CHF146.5 million (approximately US$149 million). The transaction includes all brands and know-how, the Carmignano and Condino Mills in Italy, as well as their digital imaging business and facility situated in Cham, Switzerland. The acquisition will be financed from internal resources. We are working to obtain approval from the relevant competition authorities and trust that we can announce completion during the first calendar quarter 2018.

## Liquidity and financing

At September 2017, we had liquidity comprising US$550 million of cash on hand, which exceeds the amount of short-term interest-bearing debt (including bank overdrafts) of US$133 million by US$417 million, and US$623 million available from undrawn committed facilities in Europe and Southern Africa.

Net debt decreased further to US$1,322 million (2016: US$1,408 million) due to the net cash generation of US$108 million during the year (2016: US$359 million). The decrease in net cash generated was largely due to higher working capital movements, greater cash taxes, the dividend paid and increases in capital expenditure which was offset by lower finance costs.

Details of our non-current borrowings are set out in note 21.

## Risks and insurance
Details of the group's risks and insurance are set out in the *Risk management* section of our Annual Integrated Report.

## Property, plant and equipment
There were no major changes in the nature of the group's property, plant and equipment during the period under review.

Capital expenditure for the year ended September 2017 of US$357 million (2016: US$241 million) was greater than the prior year due to various upgrade and expansion projects throughout the group. Maintenance expenditure of US$140 million (2016: US$155 million) was in line with prior year and largely incurred on efficiency projects.

## Subsequent events
The dividend of 15 US cents per share was declared on 16 November 2017 being after the reporting date.

## Directorate
The composition of the board of directors is set out in *Our leadership* section in our Annual Integrated Report. During the year, the following changes were announced:
- The appointment of Dr Boni Mehlomakulu as an independent non-executive director and as a member of the Social, Ethics, Transformation and Sustainability Committee with effect from 01 March 2017.

At the end of September 2017, there were 13 directors, two of whom are executive directors. Nine of the 11 non-executive directors are considered to be independent. The independence of those directors who are designated as independent was reviewed and confirmed during the year by the Nomination and Governance Committee.

In terms of the company's Memorandum of Incorporation, Sir Nigel Rudd and Messrs P Mageza and MV Moosa will retire by rotation from the board at the forthcoming Annual General Meeting and all being eligible, have offered themselves for re-election. Having assessed the individual performances of the directors concerned, the board recommends each of them for re-appointment.

Details of the secretaries and their business and postal addresses are set out in the *Administration* section of the Annual Integrated Report.

Details of the directors' and prescribed officers' shareholding and remuneration are set out in notes 34 to 36.

## Directors' and officers' disclosure of interests in contracts
During the period under review, the group awarded a contract, via a tender process, for engineering services worth US$55 million for a capital project to The Boldt Company of whom Mr DeKoch, one of the group's non-executive directors, is the President and Chief Operating Officer. The interest was disclosed by Mr DeKoch and he recused himself from the meeting.

The other directors and officers have certified that they do not have any material interest in any significant transaction with either the company or any of its subsidiaries.

## Directors' liabilities
Directors and officers of the group are covered by directors' and officers' liability insurance.

## Subsidiary companies
Details of the company's significant subsidiaries are set out in note 37.

# Independent Auditor's Report

## To the shareholders of Sappi Limited

## Report on the consolidated financial statements

### Opinion

We have audited the consolidated financial statements of Sappi Limited (the group) set out on pages 9 to 88, which comprise the group balance sheet as at September 2017, 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 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 Limited as at September 2017, 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 (ISA). 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 for 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.

| The key audit matter | How the matter was addressed in our audit |
|---|---|
| **Valuation of post-employment benefit obligations** | |
| Refer to note 2.3.6 for the accounting policies applied and note 28 in the consolidated financial statements.<br><br>The group operates several principal defined pension and/or retirement lump sum plans in all regions which have been established in accordance with applicable legal requirements, customs and existing circumstances in each country.<br><br>Accounting for post-employment benefit obligations, particularly defined benefit plans, is inherently complex and requires significant actuarial assumptions to be applied and involves estimation uncertainty. Benefits are formula-driven comprising a variety of earnings definitions, as indicated in note 28. The valuation of the defined benefit obligations requires the application of the following key assumptions:<br>• Discount rates<br>• Salary increases<br>• Cost of living adjustments<br>• Healthcare cost trends, and<br>• Average life expectancy of employees.<br><br>In the case of net assets, recognised assets are limited to the present value of any future refunds from the plan or reductions in future contributions to the plan, considered in the context of the relevant scheme rules and local regulations.<br><br>Due to the complexity, significant actuarial assumptions and estimation uncertainty involved in the recognition, measurement and disclosure of the defined benefit pension and/or retirement lump sum plans, this was considered a key audit matter. | Our audit procedures related to the defined pension and/or retirement lump sum plans included, among others:<br>• Obtaining actuarial reports and using our actuarial specialists in the respective regions, that formed part of the audit team, to determine the reasonableness of the key assumptions applied within the valuations based on their industry knowledge and experience<br>• Assessing the competence, independence and integrity of the group's actuarial specialists<br>• Critically assessing the appropriateness of the accounting treatment adopted in respect of net assets recognised by understanding the relevant scheme rules and local regulations and applying the relevant accounting standards and interpretations, and<br>• Assessing the appropriateness of the disclosures in the consolidated financial statements. |

| The key audit matter | How the matter was addressed in our audit |
|---|---|
| **Valuation of plantations** | |
| Refer to note 2.3.5 for the accounting policies applied and note 11 in the consolidated financial statements.<br><br>Plantations are stated at fair value less estimated cost to sell at the harvesting stage, using the income approach, and is a level 3 measure in terms of IFRS 13 *Fair Value Measurements.*<br><br>The valuation of plantations requires complex measurements and involves estimation uncertainty. The key measurements and assumptions having the most significant impact on the fair value of the plantations include:<br>• Market prices<br>• Discount rates<br>• Volumes, and<br>• Growth.<br><br>Given the complexity and estimation involved in the determination of fair value of the plantations, this matter was considered a key audit matter. | Our audit procedures related to the valuation of plantations included, among others:<br>• Critically evaluating the fair value methodology, 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<br>• 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<br>• Assessing the reasonableness of the group's fair value calculation, and the related sensitivity disclosures, by performing our own sensitivity analysis of the plantation valuations. |
| **Valuation of deferred tax assets** | |
| Refer to note 2.3.3(ii) for the accounting policies applied and note 12 in the consolidated financial statements.<br><br>As detailed in note 12, the existence of historical unused tax losses, particularly in the European tax jurisdictions, requires judgement to be applied in determining how much of these tax losses should be recognised as deferred tax assets. The recognition is based on forecasts of future taxable profits which involves estimating if and when the losses will be utilised.<br><br>Given the quantum of both the recognised and unrecognised deferred tax assets and the inherent uncertainty involved in forecasting future taxable profits, this has been identified as a key audit matter. | Our audit procedures related to the valuation of deferred tax assets included, among others:<br>• Challenging the reasonableness of the key assumptions applied by management in the recognition of deferred tax assets relating to tax losses by:<br>– critically assessing the utilisation of the losses<br>– reviewing the forecast future taxable profits considering approved budgets, and<br>– considering management's historical accuracy in forecasting taxable profits<br>• Considering the application of the relevant accounting standards in respect of recognising deferred tax assets for entities with a history of tax losses<br>• Challenging the judgements applied by management in not recognising deferred tax assets in relation to unused tax losses by considering the nature of the underlying operations of the entities, the taxable profits or losses achieved in recent years along with the forecast future taxable profits, and<br>• Assessing the adequacy and appropriateness of the group's disclosures in respect of recognised and unrecognised deferred tax assets in the consolidated financial statements. |

**Other matter**
The financial statements for Sappi Limited for the year ended September 2016 were audited by another auditor who expressed an unmodified opinion on those statements dated 09 December 2016.

**Other information**
The directors are responsible for the other information. The other information comprises the Group Company Secretary's certificate, the Audit Committee Report and the Directors' Report as required by the Companies Act of South Africa and the directors' approval and the Annual Integrated Report, which we obtained prior to the date of this report. 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.

# Independent Auditor's Report continued

**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 ISA 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 ISA, 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 04 December 2015, we report that KPMG Inc. was appointed as the auditor of Sappi Limited in the current year.

**KPMG Inc**
*Registered Auditor*

**Per Peter MacDonald**
*Chartered Accountant (SA)*
*Registered Auditor*
*Director*

85 Empire Road, Parktown
Johannesburg, 2193

07 December 2017

# Group income statement

for the year ended September 2017

| (US$ million) | Note | 2017 | 2016 |
|---|---|---|---|
| **Revenue** | | **5,296** | 5,141 |
| Cost of sales | 4 | **4,429** | 4,270 |
| Gross profit | | **867** | 871 |
| Selling, general and administrative expenses | 4 | **334** | 336 |
| Other operating (income) expenses | | **14** | – |
| Share of profit from equity-accounted investees | | **(7)** | (9) |
| **Operating profit** | 4 | **526** | 544 |
| Net finance costs | 5 | **80** | 121 |
| Finance costs | | **107** | 140 |
| Finance income | | **(15)** | (16) |
| Net foreign exchange gains | | **(12)** | (2) |
| Net fair value (gain) loss on financial instruments | | **–** | (1) |
| **Profit before taxation** | | **446** | 423 |
| Taxation charge | 6 | **108** | 104 |
| **Profit for the year** | | **338** | 319 |
| **Basic earnings per share (US cents)** | 7 | **63** | 60 |
| Weighted average number of ordinary shares in issue (millions) | | **533.9** | 529.4 |
| **Diluted earnings per share (US cents)** | 7 | **62** | 59 |
| Weighted average number of ordinary shares in issue on a fully diluted basis (millions) | | **547.4** | 540.3 |

# Group statement of comprehensive income

for the year ended September 2017

| (US$ million) | Note | 2017 | 2016 |
|---|---|---|---|
| Profit for the year | | **338** | 319 |
| **Other comprehensive income (loss), net of tax** | 19 | **78** | 30 |
| ***Item that will not be reclassified subsequently to profit or loss*** | | **68** | (12) |
| Actuarial gains (losses) on post-employment benefit funds | | **101** | (20) |
| Deferred tax on above item | | **(33)** | 8 |
| ***Items that may be reclassified subsequently to profit or loss*** | | **10** | 42 |
| Exchange differences on translation to presentation currency | | **(1)** | 38 |
| Movement in hedging reserves | | **10** | 4 |
| Deferred tax on above items | | **1** | – |
| **Total comprehensive income (loss) for the year** | | **416** | 349 |

# Group balance sheet

as at September 2017

| (US$ million) | Note | 2017 | 2016 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | **3,378** | 3,171 |
| Property, plant and equipment | 10 | **2,681** | 2,501 |
| Plantations | 11 | **458** | 441 |
| Deferred tax assets | 12 | **123** | 152 |
| Goodwill and intangible assets | 13 | **39** | 17 |
| Equity accounted investees | 14 | **26** | 20 |
| Other non-current assets | 15 | **51** | 39 |
| Derivative financial instruments | 30 | **–** | 1 |
| **Current assets** | | **1,869** | 2,006 |
| Inventories | 16 | **636** | 606 |
| Trade and other receivables | 17 | **668** | 642 |
| Derivative financial instruments | 30 | **3** | 44 |
| Taxation receivable | | **12** | 11 |
| Cash and cash equivalents | | **550** | 703 |
| **Total assets** | | **5,247** | 5,177 |
| **Equity and liabilities** | | | |
| **Shareholders' equity** | | **1,747** | 1,378 |
| Ordinary share capital and share premium | 18 | **894** | 879 |
| Non-distributable reserves | 20 | **123** | 114 |
| Foreign currency translation reserve | | **(158)** | (147) |
| Hedging reserves | | **(34)** | (43) |
| Retained earnings | | **922** | 575 |
| **Non-current liabilities** | | **2,457** | 2,325 |
| Interest-bearing borrowings | 21 | **1,739** | 1,535 |
| Deferred tax liabilities | 12 | **295** | 272 |
| Other non-current liabilities | 22 | **423** | 518 |
| **Current liabilities** | | **1,043** | 1,474 |
| Interest-bearing borrowings | 21 | **133** | 576 |
| Trade and other payables | | **858** | 839 |
| Provisions | 23 | **10** | 15 |
| Derivative financial instruments | 30 | **5** | 2 |
| Taxation payable | | **37** | 42 |
| **Total equity and liabilities** | | **5,247** | 5,177 |

# Group statement of cash flows

for the year ended September 2017

| (US$ million) | Note | 2017 | 2016 |
|---|---|---|---|
| **Cash retained from operating activities** | | **481** | 550 |
| Cash generated from operations | 24.1 | **748** | 693 |
| – Increase (decrease) in working capital | 24.2 | **(27)** | 4 |
| Cash generated from operating activities | | **721** | 697 |
| – Finance costs paid | 24.3 | **(96)** | (107) |
| – Finance income received | | **15** | 16 |
| – Taxation paid | 24.4 | **(100)** | (56) |
| – Dividends paid | | **(59)** | – |
| **Cash utilised in investing activities** | | **(373)** | (191) |
| Investment to maintain operations | | **(140)** | (155) |
| Investment to expand operations | | **(217)** | (86) |
| Proceeds on disposal of assets held for sale | | **–** | 39 |
| Proceeds on disposal of other non-current assets | 24.5 | **4** | 5 |
| Other (increase) decrease in non-current assets | | **(9)** | 6 |
| Acquisitions | 9 | **(11)** | – |
| **Cash effects of financing activities** | | **(279)** | (130) |
| Proceeds from interest-bearing borrowings | | **186** | 389 |
| Repayment of interest-bearing borrowings | | **(465)** | (499) |
| Cash costs attributable to refinancing transactions | | **–** | (20) |
| **Net movement in cash and cash equivalents** | | **(171)** | 229 |
| Cash and cash equivalents at beginning of year | | **703** | 456 |
| Translation effects | | **18** | 18 |
| **Cash and cash equivalents at end of year** | | **550** | 703 |

# Group statement of changes in equity

for the year ended September 2017

| (US$ million) | Number of ordinary shares | Ordinary share capital | Share premium | Ordinary share capital and share premium | Non-distri-butable reserves | Foreign currency trans-lation reserve | Hedging reserves | Retained earnings | **Total equity** |
|---|---|---|---|---|---|---|---|---|---|
| **Balance – September 2015** | 526.4 | 38 | 813 | 851 | 113 | (170) | (47) | 268 | **1,015** |
| Share-based payments | – | – | – | – | 7 | – | – | – | **7** |
| Transfers of vested share options | 4.2 | – | 14 | 14 | (7) | – | – | – | **7** |
| Translation of parent company's ordinary share capital and share premium | – | 1 | 13 | 14 | – | (14) | – | – | **–** |
| Total comprehensive (loss) income | – | – | – | – | 1 | 37 | 4 | 307 | **349** |
| **Balance – September 2016** | 530.6 | 39 | 840 | 879 | 114 | (147) | (43) | 575 | **1,378** |
| Share-based payments | – | – | – | – | 9 | – | – | – | **9** |
| Transfers of vested share options | 4.4 | 1 | 4 | 5 | (2) | – | – | – | **3** |
| Translation of parent company's ordinary share capital and share premium | – | – | 10 | 10 | – | (10) | – | – | **–** |
| Dividend paid – 11 US cents per share | – | – | – | – | – | – | – | (59) | **(59)** |
| Total comprehensive income | – | – | – | – | 2 | (1) | 9 | 406 | **416** |
| **Balance – September 2017** | 535.0 | 40 | 854 | 894 | 123 | (158) | (34) | 922 | **1,747** |
| *Note* | | | | *18* | *20* | | | | |

# Notes to the Group Annual Financial Statements

for the year ended September 2017

## 1. Basis of preparation

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 Listings Requirements of the JSE Limited, and
- The requirements of the Companies Act 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.

## 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.

### 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
- Property, plant and equipment is accounted for using the cost model, and
- The step-by-step method of reclassification of foreign currency translation reserves from equity to profit or loss on disposal.

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

The Group Annual Financial Statements are presented in United States Dollar (US$) as it is the major trading currency of the pulp and paper industry and are rounded to the nearest million except as otherwise indicated.

The preparation of the Group Annual Financial Statements was supervised by the Chief Financial Officer, GT Pearce CA(SA).

#### *(i) Financial year*

The group's financial year-end is on the Sunday closest to the last day of September. Accordingly, the last three financial years were as follows:
- 26 September 2016 to 01 October 2017 (53 weeks)
- 28 September 2015 to 25 September 2016 (52 weeks)
- 29 September 2014 to 27 September 2015 (52 weeks).

#### *(ii) Underlying concepts*

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

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

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.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 2. Accounting policies continued

### 2.2 Summary of accounting policies

### *2.2.1 Foreign currencies*

*(i) Functional and presentation currency*

Items included in the financial statements of each of the group's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The Group Annual Financial Statements are presented in US Dollar, which is the group's presentation currency.

The functional currency of the parent company is Rand (ZAR). The share capital and share premium of the parent company are translated into US Dollar at the period-end rate. The exchange differences arising on this translation are included in the foreign currency translation reserve and cannot be recycled through profit or loss.

*(ii) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. 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.

*(iii) Foreign operations*

The results and financial position of each group entity that has a functional currency that is different to the presentation currency of the group is translated into the presentation currency of the group as follows:

- Assets and liabilities are translated at the period-end rate, and
- Income statement items are translated at the average exchange rate for the year.

Exchange differences on translation are accounted for in OCI. These differences will be recognised in earnings on realisation of the underlying operation.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations (ie the reporting entity's interest in the net assets of that operation), and of borrowings designated as hedging instruments of such investments, are taken to OCI.

Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and are translated at the period-end rate on each reporting date.

The group used the following exchange rates for financial reporting purposes:

| | **2017** | 2016 |
|---|---|---|
| Period-end rate | | |
| US$1 = ZAR | **13.556** | 13.714 |
| €1 = US$ | **1.181** | 1.123 |
| Annual average rate | | |
| US$1 = ZAR | **13.381** | 14.788 |
| €1 = US$ | **1.106** | 1.111 |

## 2. Accounting policies continued

### 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) Associates and joint ventures (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.

# Notes to the Group Annual Financial Statements

continued

for the year ended September 2017

## 2. Accounting policies continued

### 2.2 Summary of accounting policies continued

#### 2.2.3 *Financial instruments continued*

*(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.

*(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) Interest income and expense*

Interest income and expense 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*

Brands acquired are capitalised and amortised on a straight-line basis over their estimated useful lives which, on average, is 10 years.

*(iv) Other intangible assets*

Other intangible assets comprise customer relationships, know-how and licence fees which are amortised on a straight-line basis over their useful lives between 10 and 20 years.

## 2. Accounting policies continued

### 2.2 Summary of accounting policies continued

#### *2.2.6 Inventories*

Inventories are stated at the lower of cost or net realisable value. Cost includes all costs of purchase, 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*

*(i) The group as lessee*

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.

*(ii) Recognition of lease of land*

The land and buildings elements of a lease are considered separately for the purpose of lease classification. Where the building is a finance lease, and the lease payments cannot be allocated reliably between these two elements, the entire lease is classified as a finance lease.

#### *2.2.8 Segment reporting*

The group's reportable segments, which have been determined in accordance with how the group allocates resources and evaluates performance, is predominantly on a geographical basis and comprise North America, Europe and Southern Africa.

Assets, liabilities, revenues or expenses that are not directly attributable to a particular segment are allocated between segments where there is a reasonable basis for doing so. The group accounts for intra-segment revenues and transfers as if the transactions were with third parties at current market prices.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 2. Accounting policies continued

### 2.2 Summary of accounting policies continued

#### *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. These costs, when included in the sales price charged for the group's products, are recognised in sales.

#### *2.2.11 Emission trading*

The group recognises government grants for emission rights as intangible assets at the cost of the rights as well as a liability which equals the cost of the rights at the time of the grant.

The group does not recognise a liability for emissions to the extent that it has sufficient allowances to satisfy emission liabilities. Where there is a shortfall of allowances that the group would have to deliver for emissions, a liability is recognised at the current market value of the shortfall.

Where the group sells allowances to parties outside the group at amounts greater than the carrying amount, a gain is recognised in selling, general and administrative expenses in profit or loss for the period.

#### *2.2.12 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.

#### *2.2.13 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 carousel products across different operating units in determining CGUs and in allocating goodwill to those CGUs.

## 2. Accounting policies continued

### 2.2 Summary of accounting policies continued

#### *2.2.14 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 for non-market-related performance conditions.

*(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 or 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 29 provides further detail on key estimates, assumptions and other information on share-based payments applicable as at the end of the year.

### 2.3 Critical accounting policies

#### *2.3.1 Impairment of assets other than goodwill and financial instruments*

The group assesses all assets (other than goodwill and intangible assets not yet available for use) at each balance sheet date for indications of impairment or, for intangible assets other than goodwill, whether an impairment reversal is required.

Intangible assets not yet available for use are tested at least annually for impairment.

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.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 2. Accounting policies continued

### 2.3 Critical accounting policies continued

### *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.

### *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.

## 2. Accounting policies continued

### 2.3 Critical accounting policies continued

#### *2.3.3 Taxation continued*

*(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.

Refer to note 12 for the movement in unrecognised deferred tax assets.

*(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.

#### *2.3.4 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 forecast 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.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 2. Accounting policies continued

### 2.3 Critical accounting policies continued

#### *2.3.4 Derivatives and hedge accounting continued*

*(iii) Hedge of a net investment in a foreign operation*

The effective portion of the gain or loss on the hedging instrument is recognised in OCI and is only reclassified to profit or loss on the disposal or partial disposal of the foreign operation.

*(iv) 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 forecast 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 30 and 31 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.

#### *2.3.5 Plantations*

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*. 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 11.

- *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 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 is 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.

## 2. Accounting policies continued

### 2.3 Critical accounting policies continued

#### *2.3.5 Plantations continued*

- *Discount rate*

  The discount rate used is the applicable pre-tax weighted average cost of capital of the business unit.

- *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 five 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 ton allocation method multiplied by unadjusted current market prices. Tons 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 eight 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 tending of trees.

  The associated costs for managing plantations are recognised as silviculture costs in cost of sales (see note 4).

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 2. Accounting policies continued

### 2.3 Critical accounting policies continued

#### *2.3.6 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 recognises 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 28 for the key estimates, assumptions and other information on post-employment benefits.

#### *2.3.7 Provisions*

A provision is recognised when the group has a legal or constructive obligation arising from a past event which can be reliably measured and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation. 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.

Environmental accruals are recorded based on current interpretation of environmental laws and regulations (refer to note 2.3.8).

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.

Refer to note 23 for the nature of provisions recorded.

## 2. Accounting policies continued

### 2.3 Critical accounting policies continued

#### *2.3.8 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.

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.

### 2.4 Adoption of accounting standards in the current year

The group has not adopted any new or revised standards, interpretations, amendments and improvements to standards in the current fiscal year.

### 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 – September 2019. Management has implemented a project to assess the revised classification and measurement impact of this standard and the effect of the expected credit loss method.
- IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture – Effective date deferred indefinitely.
- IFRS 15 *Revenue from Contracts with Customers* – provides a single, principles-based five-step model to be applied to all contracts with customers – September 2019. Management is currently reviewing the significant customer contracts to determine the impact of this standard.
- 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* – September 2020. Management is currently reviewing the operating lease contracts in place to determine the impact of this standard.
- 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 – September 2018.
- IAS 12 – *Income Taxes* – Recognition of Deferred Tax Assets for Unrealised Losses – September 2018.
- IFRIC 22 – *Foreign Currency Transactions and Advance Consideration* – September 2019.
- IFRIC 23 – *Uncertainty over Income Tax Treatments* – September 2020.
- IFRS 17 – *Insurance Contracts* – Supersedes IFRS 4 – September 2022.
- IAS 40 – *Investment Property* – Transfers of Investment Property – September 2019.
- Annual Improvements 2014 – 2016 Cycle – September 2018.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 3. Segment information

Reportable segments are components of an entity for which separate financial information, that is evaluated regularly by the chief operating decision maker in deciding on how to allocate resources and assess performance, is available. The group's reportable segments comprise the geographic regions of North America, Europe and Southern Africa as this is the basis on which financial information is reported to the chief operating decision maker for the purposes of deciding on how to allocate resources and assess performance.

The group's revenue is comprised mostly of the sale of dissolving wood pulp, coated paper and speciality paper in North America; coated, uncoated and speciality paper in Europe as well as dissolving wood pulp, paper pulp and uncoated and commodity paper in Southern Africa.

The group operates a trading network called Sappi Trading for the international marketing and distribution of dissolving wood pulp and paper pulp throughout the world and of the group's other products in areas outside its core operating regions of North America, Europe and Southern Africa. The financial results and position associated with Sappi Trading are allocated to our reportable segments.

The group accounts for intra-group sales and transfers as if the sales or transfers were to third parties, that is, at current market prices. All such sales and transfers are eliminated on consolidation.

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

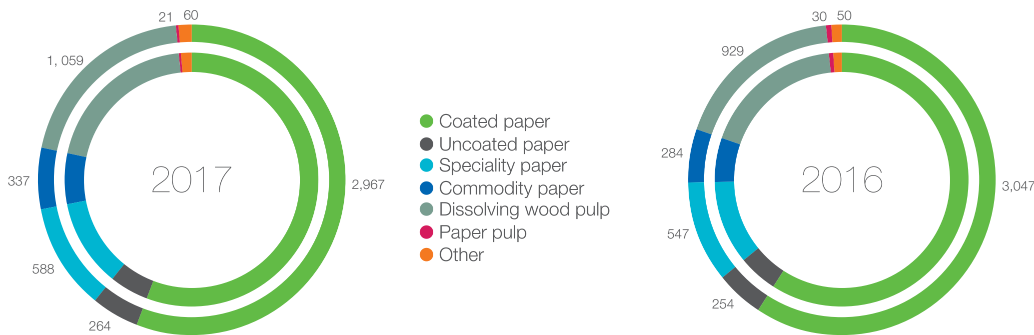
| | North America | | Europe | |
|---|---|---|---|---|
| (US$ million) | **2017** | 2016 | **2017** | 2016 |
| **Income statement** | | | | |
| External sales[1] | **1,360** | 1,367 | **2,564** | 2,582 |
| Operating profit excluding special items | **47** | 49 | **140** | 131 |
| Special items – gains (losses)[2] | **–** | 6 | **(4)** | (6) |
| Segment operating profit (loss) | **47** | 55 | **136** | 125 |
| EBITDA excluding special items[2] | **126** | 124 | **262** | 261 |
| Share of profit of equity investments | **–** | – | **–** | 1 |
| Depreciation and amortisation | **(79)** | (75) | **(122)** | (130) |
| Net asset impairments | **–** | – | **(1)** | (2) |
| Profit (loss) on disposal and written off assets | **–** | – | **(1)** | 1 |
| Fellings | **–** | – | **–** | – |
| Plantation fair value adjustment | **–** | – | **–** | – |
| Restructuring provisions (raised) released and closure costs | **–** | – | **–** | (3) |
| Employee benefit liability settlement | **–** | 8 | **–** | – |
| Other non-cash items | **(16)** | (14) | **(15)** | (10) |
| **Balance sheet** | | | | |
| Capital expenditures | **132** | 44 | **131** | 90 |
| Segment assets[2] | **1,026** | 967 | **1,373** | 1,256 |
| Property, plant and equipment | **841** | 788 | **1,042** | 968 |

Reconciliation of operating profit excluding special items to segment operating profit (loss):

| | North America | | Europe | |
|---|---|---|---|---|
| (US$ million) | **2017** | 2016 | **2017** | 2016 |
| Operating profit excluding special items | **47** | 49 | **140** | 131 |
| Special items – gains (losses)[2] | **–** | 6 | **(4)** | (6) |
| Segment operating profit (loss) | **47** | 55 | **136** | 125 |

[1] *Sales of products are allocated to where the product is manufactured.*
[2] *Refer to the Glossary in the Annual Integrated Report for the definition of the term.*
[3] *Primarily includes the group's treasury operations and its self-insurance captive.*

**Sales by products**




| Southern Africa 2017 | Southern Africa 2016 | Unallocated and eliminations[3] 2017 | Unallocated and eliminations[3] 2016 | Group 2017 | Group 2016 |
|---|---|---|---|---|---|
| **1,372** | 1,192 | **–** | – | **5,296** | 5,141 |
| **337** | 305 | **2** | 2 | **526** | 487 |
| **10** | 62 | **(6)** | (5) | **–** | 57 |
| **347** | 367 | **(4)** | (3) | **526** | 544 |
| **396** | 352 | **1** | 2 | **785** | 739 |
| **6** | 8 | **1** | – | **7** | 9 |
| **(59)** | (47) | **1** | – | **(259)** | (252) |
| **(3)** | – | **–** | – | **(4)** | (2) |
| **(1)** | 14 | **–** | – | **(2)** | 15 |
| **(63)** | (56) | **–** | – | **(63)** | (56) |
| **79** | 120 | **–** | – | **79** | 120 |
| **–** | (1) | **(1)** | – | **(1)** | (4) |
| **–** | – | **–** | – | **–** | 8 |
| **6** | (22) | **–** | 6 | **(25)** | (40) |
| **105** | 90 | **2** | 5 | **370** | 229 |
| **1,263** | 1,182 | **2** | 19 | **3,664** | 3,424 |
| **789** | 738 | **9** | 7 | **2,681** | 2,501 |

| Southern Africa 2017 | Southern Africa 2016 | Unallocated and eliminations[3] 2017 | Unallocated and eliminations[3] 2016 | Group 2017 | Group 2016 |
|---|---|---|---|---|---|
| **337** | 305 | **2** | 2 | **526** | 487 |
| **10** | 62 | **(6)** | (5) | **–** | 57 |
| **347** | 367 | **(4)** | (3) | **526** | 544 |

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 3. Segment information continued

Reconciliation of EBITDA excluding special items and operating profit (loss) excluding special items to profit (loss) before taxation:

| (US$ million) | North America 2017 | North America 2016 | Europe 2017 | Europe 2016 |
|---|---|---|---|---|
| EBITDA excluding special items[2] | **126** | 124 | **262** | 261 |
| Depreciation and amortisation | **(79)** | (75) | **(122)** | (130) |
| Operating profit excluding special items | **47** | 49 | **140** | 131 |
| Special items – gains (losses)[2] | **–** | 6 | **(4)** | (6) |
| Segment operating profit (loss) | **47** | 55 | **136** | 125 |
| Net finance costs | | | | |
| Profit before taxation | | | | |

Reconciliation of segment assets to total assets:

| (US$ million) |
|---|
| Segment assets[2] |
| Deferred tax assets |
| Cash and cash equivalents |
| Trade and other payables |
| Provisions |
| Derivative financial instruments (included in current liabilities) |
| Taxation payable |
| **Total assets** |

In addition to regularly reviewing separate financial information by reportable segment, the chief operating decision maker also reviews certain financial information by major product category which comprises:

| (US$ million) |
|---|
| **Sales** |
| Specialised cellulose |
| Paper |
| Forestry |
| Total |
| **Operating profit excluding special items** |
| Specialised cellulose |
| Paper |
| Unallocated and eliminations[3] |
| Total |
| **EBITDA excluding special items** |
| Specialised cellulose |
| Paper |
| Unallocated and eliminations[3] |
| Total |

[2] *Refer to the Glossary in the Annual Integrated Report for the definition of the term.*
[3] *Primarily includes the group's treasury operations and its self-insurance captive.*

| | Southern Africa | | Unallocated and eliminations[3] | | Group | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 |
| | **396** | 352 | **1** | 2 | **785** | 739 |
| | **(59)** | (47) | **1** | – | **(259)** | (252) |
| | **337** | 305 | **2** | 2 | **526** | 487 |
| | **10** | 62 | **(6)** | (5) | **–** | 57 |
| | **347** | 367 | **(4)** | (3) | **526** | 544 |
| | | | | | **(80)** | (121) |
| | | | | | **446** | 423 |

| | Group | |
|---|---|---|
| | **2017** | 2016 |
| | **3,664** | 3,424 |
| | **123** | 152 |
| | **550** | 703 |
| | **858** | 839 |
| | **10** | 15 |
| | **5** | 2 |
| | **37** | 42 |
| | **5,247** | 5,177 |

| | Group | |
|---|---|---|
| | **2017** | 2016 |
| | **1,059** | 929 |
| | **4,172** | 4,156 |
| | **65** | 56 |
| | **5,296** | 5,141 |
| | **334** | 294 |
| | **190** | 191 |
| | **2** | 2 |
| | **526** | 487 |
| | **386** | 339 |
| | **398** | 398 |
| | **1** | 2 |
| | **785** | 739 |

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 4. Operating profit

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

| (US$ million) | 2017 Cost of sales | 2017 Selling, general and administrative expenses | 2016 Cost of sales | 2016 Selling, general and administrative expenses |
|---|---|---|---|---|
| Raw materials, energy and other direct input costs | **2,705** | **–** | 2,630 | – |
| Wood (includes growth and felling adjustments)[1] | **603** | **–** | 624 | – |
| Energy | **372** | **–** | 355 | – |
| Chemicals | **787** | **–** | 726 | – |
| Pulp | **753** | **–** | 740 | – |
| Other variable costs | **190** | **–** | 185 | – |
| Plantation price fair value adjustment | **(21)** | **–** | (64) | – |
| Employment costs | **769** | **160** | 739 | 155 |
| Depreciation | **247** | **8** | 241 | 9 |
| Delivery charges | **441** | **–** | 431 | – |
| Maintenance | **213** | **–** | 201 | – |
| Other overheads | **75** | **–** | 92 | – |
| Marketing and selling expenses | **–** | **81** | – | 74 |
| Administrative and general expenses | **–** | **85** | – | 98 |
| | **4,429** | **334** | 4,270 | 336 |

| (US$ million) | 2017 | 2016 |
|---|---|---|
| Silviculture costs (included within cost of sales) | **58** | 46 |
| Leasing charges for premises | **13** | 14 |
| Leasing charges for plant and equipment | **14** | 14 |
| Remuneration paid other than to employees of the company in respect of | **27** | 25 |
| Technical services | **11** | 12 |
| Administration services | **16** | 13 |
| Auditor's remuneration | **4** | 5 |
| Tax planning and advice | **1** | – |
| Research and development costs | **29** | 26 |
| Amortisation | **4** | 2 |
| Cost on derecognition of loans and receivables[2] | **11** | 8 |
| Net asset impairment of assets and investments | **4** | 2 |
| Restructuring provisions and closure costs raised (reversed) | **1** | 4 |
| (Profit) loss on assets held for sale and written off assets | **2** | (15) |
| Post-retirement plan settlements and amendments | **–** | (8) |
| Broad-based Black Economic Empowerment (BBBEE) charge | **1** | 1 |
| Employment costs consist of | **929** | 894 |
| Wages and salaries | **838** | 814 |
| Defined contribution plan expense | **36** | 34 |
| Defined benefit pension plan expense | **21** | 12 |
| Other defined benefit plan expense | **2** | 3 |
| Share-based payment expense | **9** | 6 |
| Other | **23** | 25 |
| [1] *Changes in plantation volumes* | | |
| *Fellings* | **63** | 56 |
| *Growth* | **(58)** | (56) |

[2] *The cost on derecognition of trade receivables relates to the derecognition of trade receivables related to the securitisation programme in South Africa and to the sale of letters of credit in Hong Kong.*

| | (US$ million) | 2017 | 2016 |
|---|---|---|---|
| **5.** | **Net finance costs** | | |
| | Interest and other finance costs on liabilities carried at amortised cost | **100** | 129 |
| | Interest on overdrafts | **–** | 1 |
| | Interest on redeemable bonds and other loans | **100** | 111 |
| | Premium and costs on early redemption of redeemable bonds and other loans | **–** | 12 |
| | Accelerated amortisation on early settlement of redeemable bonds and other loans | **–** | 5 |
| | Net interest on employee benefit liabilities | **7** | 11 |
| | Finance income received on assets carried at amortised cost | **(15)** | (16) |
| | Interest income on bank accounts | **(12)** | (15) |
| | Interest income on other loans and investments | **(3)** | (1) |
| | Net foreign exchange gains | **(12)** | (2) |
| | Net fair value loss (gain) on financial instruments | **–** | (1) |
| | Hedge ineffectiveness | **–** | (1) |
| | | **80** | 121 |

| | (US$ million) | 2017 | 2016 |
|---|---|---|---|
| **6.** | **Taxation charge** | | |
| | Current taxation | | |
| | Current year | **99** | 63 |
| | Prior year overprovision | **(5)** | (2) |
| | Other company taxes | **1** | 3 |
| | Deferred taxation | | |
| | Current year | **12** | 44 |
| | Prior year underprovision | **1** | (4) |
| | Attributable to tax rate changes | **–** | – |
| | | **108** | 104 |
| | **Reconciliation of the tax rate** | | |
| | Profit before taxation | **446** | 423 |
| | Profit-making regions | **447** | 423 |
| | Loss-making regions | **(1)** | – |
| | Taxation at the average statutory tax rate | **125** | 119 |
| | Profit-making regions at 28% (2016: 28%) | **125** | 119 |
| | Exempt income | **(26)** | (17) |
| | Non-deductible expenditure | **29** | 17 |
| | No tax relief on losses | **3** | – |
| | No tax charge on profits | **(4)** | (12) |
| | Recognition of deferred tax assets | **(16)** | – |
| | Prior year adjustments | **(4)** | (6) |
| | Other taxes | **1** | 3 |
| | Taxation charge | **108** | 104 |
| | Effective tax rate for the year | **24%** | 25% |

In addition to income taxation charges to profit or loss, a taxation charge of US$33 million (2016: US$8 million relief) has been recognised directly in other comprehensive income (refer to note 12).

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 7. Earnings per share

**Basic earnings per share (EPS)**

EPS is based on the group's profit for the year divided by the weighted average number of shares in issue during the year under review.

| | **2017** | | | 2016 | | |
|---|---|---|---|---|---|---|
| | **Profit US$ million** | **Shares million** | **Earnings per share US cents** | Profit US$ million | Shares million | Earnings per share US cents |
| *Basic EPS calculation* | **338** | **533.9** | **63** | 319 | 529.4 | 60 |
| Share options and performance shares under Sappi Limited Share Trust | **–** | **13.5** | | – | 10.9 | |
| *Diluted EPS calculation* | **338** | **547.4** | **62** | 319 | 540.3 | 59 |

The diluted EPS calculations are based on Sappi Limited's daily average share price of ZAR85.47 (2016: ZAR64.88). In the current and prior financial year, all share options that could potentially dilute EPS in the future are included in the calculation above.

**Headline earnings per share[1]**

Headline earnings per share are based on the group's headline earnings divided by the weighted average number of shares in issue during the year.

Reconciliation between attributable earnings to ordinary shareholders and headline earnings:

| | **2017** | | | 2016 | | |
|---|---|---|---|---|---|---|
| (US$ million) | **Gross** | **Tax** | **Net** | Gross | Tax | Net |
| Attributable earnings to ordinary shareholders | **446** | **108** | **338** | 423 | 104 | 319 |
| Impairments of assets and investments | **6** | **–** | **6** | 2 | – | 2 |
| Profit on disposal of assets held for sale, businesses and other assets | **2** | **(1)** | **1** | (15) | (3) | (12) |
| Asset impairment reversals | **(2)** | **–** | **(2)** | – | – | – |
| Headline earnings | **454** | **107** | **343** | 410 | 101 | 309 |
| Weighted average number of ordinary shares in issue (millions) | | | **533.9** | | | 529.4 |
| Headline earnings per share (US cents) | | | **64** | | | 58 |
| Weighted average number of ordinary shares in issue on a fully diluted basis (millions) | | | **547.4** | | | 540.3 |
| Diluted headline earnings per share (US cents) | | | **63** | | | 57 |

[1] *Headline earnings – as defined in Circular 2/2015, issued by the South African Institute of Chartered Accountants in October 2015, which separates from earnings all separately identifiable remeasurements. It is not necessarily a measure of sustainable earnings. It is a Listings Requirement of the JSE Limited to disclose headline earnings per share.*

## 7. Earnings per share continued

### EPS excluding special items

EPS excluding special items is based on the group's earnings adjusted for special items (as disclosed in note 3) and certain once-off finance and tax items, divided by the weighted average number of shares in issue during the year.

| (US$ million) | 2017 Gross | 2017 Tax | 2017 Net | 2016 Gross | 2016 Tax | 2016 Net |
|---|---|---|---|---|---|---|
| Attributable earnings to ordinary shareholders | **446** | **108** | **338** | 423 | 104 | 319 |
| Special items | **–** | **(2)** | **2** | (57) | (18) | (39) |
| Refinancing costs | **–** | **–** | **–** | 23 | – | 23 |
| Earnings excluding special items | **446** | **106** | **340** | 389 | 86 | 303 |
| Weighted average number of ordinary shares in issue (millions) | | | **533.9** | | | 529.4 |
| EPS excluding special items (US cents) | | | **64** | | | 57 |
| Weighted average number of ordinary shares in issue on a fully diluted basis (millions) | | | **547.4** | | | 540.3 |
| Diluted EPS excluding special items (US cents) | | | **62** | | | 56 |

## 8. Dividends

The directors have resolved to declare a gross dividend (number 87) of 15 US cents per share, payable in Rand at an exchange rate (US$1 = ZAR) of 14.37037, being ZAR215.55555 cents per share, for the year ended September 2017 out of income, in respect of Sappi ordinary shares in issue on the record date as detailed below. Holders of Sappi 'A' ordinary unlisted shares in issue on the record date shall be entitled to receive 7.5 US cents per share being 50% of the ordinary dividend declared.

## 9. Cash paid on acquisition

On 03 July 2017 Sappi acquired a 100% interest in Rockwell Solutions Limited for a purchase consideration of US$23 million (GBP18 million) of which US$12 million (GBP10 million) is a contingent consideration and US$11 million was paid in cash. The net assets acquired include tangible net assets of US$7 million, goodwill of US$3 million and identified intangible assets of US$13 million.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **10. Property, plant and equipment** | | |
| Land and buildings[1] | | |
| At cost | **1,385** | 1,317 |
| Accumulated depreciation and impairments | **(860)** | (800) |
| | **525** | 517 |
| Plant and equipment[2] | | |
| At cost | **6,864** | 6,401 |
| Accumulated depreciation and impairments | **(4,709)** | (4,419) |
| | **2,155** | 1,982 |
| Capitalised leased assets | | |
| At cost | **432** | 412 |
| Accumulated depreciation and impairments | **(431)** | (410) |
| | **1** | 2 |
| Aggregate cost | **8,681** | 8,130 |
| Aggregate accumulated depreciation and impairments | **(6,000)** | (5,629) |
| Aggregate book value[3] | **2,681** | 2,501 |

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

| (US$ million) | Land and buildings | Plant and equipment | Capitalised leased assets | Total |
|---|---|---|---|---|
| Net book value at September 2015 | 510 | 1,996 | 2 | **2,508** |
| Additions | 10 | 218 | 1 | **229** |
| Disposals | – | (2) | – | **(2)** |
| Depreciation | (28) | (221) | (1) | **(250)** |
| Transfers to assets held for sale | 22 | (22) | – | **–** |
| Translation differences | 3 | 13 | – | **16** |
| Net book value at September 2016 | 517 | 1,982 | 2 | **2,501** |
| Additions | 20 | 350 | – | **370** |
| Acquisition | 5 | 5 | – | **10** |
| Disposals | (1) | (5) | – | **(6)** |
| Depreciation | (29) | (225) | (1) | **(255)** |
| Translation differences | 13 | 48 | – | **61** |
| Net book value at September 2017 | 525 | 2,155 | 1 | **2,681** |

[1] *Details of land and buildings are available at the registered offices of the respective companies that 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 US$298 million (2016: US$124 million) relates to assets under construction.*

Refer to note 25 for details of encumbrances.

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **11. Plantations** | | |
| Fair value of plantations at beginning of year | **441** | 383 |
| Gains arising from growth | **58** | 56 |
| Fire, flood, storms and related events | **(5)** | (13) |
| In-field inventory | **1** | (1) |
| Gain arising from fair value price changes | **21** | 64 |
| Harvesting – agriculture produce (fellings) | **(63)** | (56) |
| Disposals | **–** | (1) |
| Translation differences | **5** | 9 |
| Fair value of plantations at end of year | **458** | 441 |

Sappi manages the establishment, maintenance and harvesting of its plantations on a compartmentalised basis. These plantations comprise 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 20 years. In certain circumstances, the group provides loans to farmers 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 9.77%. 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 17 tons of timber per hectare while immature timber comprise approximately 101,000 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 below:

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **Market price changes** | | |
| 1% increase in market prices | **2** | 2 |
| 1% decrease in market prices | **(2)** | (2) |
| **Discount rate (for immature timber)** | | |
| 1% increase in rate | **(3)** | (2) |
| 1% decrease in rate | **3** | 2 |
| **Volume assumption** | | |
| 1% increase in estimate of volume | **4** | 4 |
| 1% decrease in estimate of volume | **(4)** | (4) |
| **Costs to sell** | | |
| 1% increase in costs to sell | **(2)** | (2) |
| 1% decrease in costs to sell | **2** | 2 |
| **Growth assumptions** | | |
| 1% increase in rate of growth | **1** | 1 |
| 1% decrease in rate of growth | **(1)** | (1) |

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

| (US$ million) | 2017 Assets | 2017 Liabilities | 2016 Assets | 2016 Liabilities |
|---|---|---|---|---|
| **12. Deferred tax** | | | | |
| Other liabilities, accruals and prepayments | **(69)** | **(90)** | (63) | (63) |
| Inventory | **10** | **2** | 10 | 2 |
| United States of America (USA) tax credits carry forward | **16** | **–** | 20 | – |
| Tax loss carry forward | **127** | **29** | 119 | 30 |
| Property, plant and equipment | **(64)** | **(209)** | (5) | (207) |
| Plantations | **–** | **(32)** | – | (48) |
| Other non-current assets | **18** | **2** | 40 | 2 |
| Other non-current liabilities | **85** | **3** | 31 | 12 |
| | **123** | **(295)** | 152 | (272) |

**Negative asset and liability positions**

These balances reflect the impact of tax assets and liabilities arising in different tax jurisdictions, which cannot be netted against tax assets and liabilities arising in other tax jurisdictions.

**Deferred tax assets recognised on the balance sheet**

The recognised deferred tax assets relate mostly to available unused tax losses. It is expected that there will be sufficient future taxable profits against which these losses can be recovered. In the estimation of future taxable profits, future product pricing and production capacity utilisation are taken into account.

**Unrecognised deferred tax assets**

Deferred tax assets arising from unused tax losses and unused tax credits are not recognised for carry forward when it cannot be demonstrated that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

| (US$ million) | 2017 | 2016 |
|---|---|---|
| Unrecognised deferred tax assets relate to the following: | | |
| Net deductible temporary differences | **29** | 36 |
| Tax losses | **682** | 712 |
| | **711** | 748 |
| Attributable to the following tax jurisdictions: | | |
| Austria | **529** | 552 |
| Belgium | **115** | 115 |
| Finland | **40** | 38 |
| The Netherlands | **27** | 43 |
| | **711** | 748 |
| Expiry between one and five years | **70** | 86 |
| Expiry after five years | **24** | 24 |
| Indefinite life | **617** | 638 |
| | **711** | 748 |

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **12. Deferred tax** continued | | |
| The following table shows the movement in the unrecognised deferred tax assets for the year: | | |
| Balance at beginning of year | **748** | 836 |
| No tax relief on losses | **1** | – |
| No tax charge on profits | **(60)** | (31) |
| Recognition of deferred tax assets | **(16)** | – |
| Expired | **–** | (59) |
| Prior year adjustments | **4** | – |
| Movement in foreign exchange rates | **34** | 2 |
| Balance at end of year | **711** | 748 |
| **Reconciliation of deferred tax** | | |
| Deferred tax balances at beginning of year | | |
| Deferred tax assets | **152** | 162 |
| Deferred tax liabilities | **(272)** | (245) |
| | **(120)** | (83) |
| Deferred tax charge for the year | **(13)** | (40) |
| Other liabilities, accruals and prepayments | **(28)** | (38) |
| Inventory | **1** | – |
| USA tax credits | **(3)** | – |
| Tax loss carry forward | **–** | (53) |
| Property, plant and equipment | **(58)** | 11 |
| Plantations | **17** | 18 |
| Other non-current assets | **(30)** | (27) |
| Other non-current liabilities | **88** | 49 |
| Amounts recorded directly in other comprehensive income | **(33)** | 8 |
| Acquisition of subsidiary | **(3)** | – |
| Translation differences | **(3)** | (5) |
| Deferred tax balances at end of year | **(172)** | (120) |
| Deferred tax assets | **123** | 152 |
| Deferred tax liabilities | **(295)** | (272) |

# Notes to the Group Annual Financial Statements
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for the year ended September 2017

## 13. Goodwill and intangible assets

| (US$ million) | 2017 Goodwill | 2017 Brands | 2017 Other | 2017 Total | 2016 Goodwill | 2016 Brands | 2016 Other | 2016 Total |
|---|---|---|---|---|---|---|---|---|
| Net carrying amount at beginning of year | **3** | **5** | **9** | **17** | 4 | 7 | 8 | 19 |
| Additions | **–** | **–** | **2** | **2** | – | – | 4 | 4 |
| Acquisitions | **3** | **9** | **13** | **25** | – | – | – | – |
| Amortisation | **–** | **(2)** | **(4)** | **(6)** | – | (2) | – | (2) |
| Impairment | **–** | **–** | **(1)** | **(1)** | – | – | (2) | (2) |
| Disposals | **–** | **–** | **(1)** | **(1)** | – | – | – | – |
| Translation difference | **1** | **1** | **1** | **3** | (1) | – | (1) | (2) |
| Net carrying amount | **7** | **13** | **19** | **39** | 3 | 5 | 9 | 17 |
| Cost (gross carrying amount) | **7** | **32** | **20** | **59** | 3 | 20 | 12 | 35 |
| Accumulated amortisation and impairments | **–** | **(19)** | **(1)** | **(20)** | – | (15) | (3) | (18) |
| Net carrying amount | **7** | **13** | **19** | **39** | 3 | 5 | 9 | 17 |

Goodwill was increased by US$3 million during the year related to the acquisition of Rockwell Solutions Limited. Goodwill is attributable to the cash-generating units of specialities (US$3 million) and coated woodfree (US$4 million) in Sappi Europe. The goodwill has been assessed for impairment by comparing the carrying amount against the recoverable amount.

## 14. Equity accounted investees

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **Group's share of carrying amount of equity accounted investees** | | |
| Umkomaas Lignin Pty Limited | **14** | 14 |
| Other equity accounted investees | **12** | 6 |
| | **26** | 20 |

Dividends received from joint ventures for the 2017 financial year were US$7 million (2016: US$7 million).

***Umkomaas Lignin Proprietary Limited***

A 50% joint venture agreement with Borregaard AS for the construction and operation of a lignin plant at Umkomaas, South Africa and the development, production and sale of products based on lignosulphonate in order to build a sustainable lignin business. The financial statements of 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 IFRS are used to account for the joint venture's income to Sappi's year-end.

Summarised financial information of Umkomaas Lignin Proprietary Limited:

| (US$ million) | 2017 | 2016 |
|---|---|---|
| Current assets | **25** | 21 |
| Non-current assets | **19** | 14 |
| Current liabilities | **(7)** | (6) |
| Non-current liabilities | **(9)** | (1) |
| The above assets and liabilities include the following: | | |
| Cash and cash equivalents | **10** | 6 |
| Current financial liabilities (excluding trade and other payables, and provisions) | **(7)** | (6) |
| Non-current financial liabilities (excluding trade and other payables, and provisions) | **(9)** | (1) |

| (US$ million) | 2017 | 2016 |
| --- | --- | --- |
| **14. Equity accounted investees** continued | | |
| ***Umkomaas Lignin Proprietary Limited*** *continued* | | |
| Sales | **49** | 56 |
| Depreciation and amortisation | **2** | 1 |
| Taxation charge | **4** | 7 |
| Profit from continuing operations | **13** | 16 |
| Total comprehensive income | **13** | 16 |

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

| (US$ million) | 2017 | 2016 |
| --- | --- | --- |
| Net assets of the joint venture | **28** | 28 |
| Proportion of the group's ownership interest | **50%** | 50% |
| Carrying amount of the joint venture | **14** | 14 |

**Details of other equity accounted investees**

The group has entered into various joint venture agreements primarily for the purchase of wood and wood chips for the common benefit of the venturers. The financial year-end of each of these joint ventures is 31 December which is a common date for entities operating in the joint ventures' countries of incorporation and which is also the year-end of the other venturers.

Aggregate financial information for joint ventures that are not individually material:

| (US$ million) | 2017 | 2016 |
| --- | --- | --- |
| Profit from continuing operations | **3** | 1 |
| Total comprehensive income | **3** | 1 |

| (US$ million) | 2017 | 2016 |
| --- | --- | --- |
| Carrying amount of these other equity accounted investees | **12** | 6 |

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

| | (US$ million) | 2017 | 2016 |
|---|---|---|---|
| **15.** | **Other non-current assets** | | |
| | Investment funds | **7** | 7 |
| | Defined benefit pension plan assets (refer to note 28) | **35** | 23 |
| | Advances to tree growers | **3** | 3 |
| | Other financial assets | **4** | 4 |
| | Other | **2** | 2 |
| | | **51** | 39 |

| | (US$ million) | 2017 | 2016 |
|---|---|---|---|
| **16.** | **Inventories** | | |
| | Raw materials | **134** | 134 |
| | Work in progress | **56** | 56 |
| | Finished goods | **311** | 281 |
| | Consumable stores and spares | **135** | 135 |
| | | **636** | 606 |

The charge to the group income statement relating to the write-down of inventories to net realisable value amounted to US$6 million (2016: US$8 million). There were no reversals of any inventory write-downs for the periods presented.

The cost of inventories recognised as an expense and included in cost of sales amounted to US$3,995 million (2016: US$3,896 million)

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **17. Trade and other receivables** | | |
| Trade accounts receivable, gross | **581** | 531 |
| Allowance for credit losses | **(10)** | (14) |
| Trade accounts receivable, net | **571** | 517 |
| Prepayments and other receivables | **97** | 125 |
| | **668** | 642 |

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.

Prepayments and other receivables primarily represent prepaid insurance, prepaid taxes and other sundry receivables.

Trade receivables (including securitised trade receivables) represent 12.3% (2016: 12.1%) of turnover.

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **17.1 Reconciliation of the allowance for credit losses** | | |
| Balance at beginning of year | **14** | 11 |
| Raised during the year | **8** | 8 |
| Released during the year | **(8)** | (1) |
| Utilised during the year | **(5)** | (4) |
| Translation differences | **1** | – |
| Balance at end of year | **10** | 14 |

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

**17.2 Analysis of amounts past due**

**September 2017**

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

| (US$ million) | Not impaired | Impaired | Total |
|---|---|---|---|
| Less than 7 days overdue | **21** | **1** | **22** |
| Between 7 and 30 days overdue | **11** | **–** | **11** |
| Between 30 and 60 days overdue | **3** | **–** | **3** |
| More than 60 days overdue | **1** | **9** | **10** |
| | **36** | **10** | **46** |

**September 2016**

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

| (US$ million) | Not impaired | Impaired | Total |
|---|---|---|---|
| Less than 7 days overdue | 7 | – | 7 |
| Between 7 and 30 days overdue | 7 | – | 7 |
| Between 30 and 60 days overdue | 2 | 1 | 3 |
| More than 60 days overdue | 2 | 12 | 14 |
| | 18 | 13 | 31 |

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

The group holds collateral of US$1 million (2016: US$1 million) against trade receivables past contractual repayment terms.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 17. Trade and other receivables continued

### 17.3 Trade receivables securitisation

The group operates on and off-balance sheet trade receivables securitisation programmes in order to improve working capital and to utilise the cost effectiveness of such structures.

***On-balance sheet structure***

The group operates an on-balance sheet securitisation programme with UniCredit Bank AG which ends in August 2020. This programme has a limit of US$390 million (€330 million). The trade receivables sold in terms of this programme are disclosed on the group balance sheet together with a corresponding liability.

At financial year-end, trade receivables with a value of US$432 million (2016: US$392 million) have been pledged as collateral for amounts received as funding under the programme of US$364 million (2016: US$314 million). The group is restricted from selling or repledging the trade receivables that have been pledged as collateral for this liability. For more detail on this programme, refer to note 21.

***Off-balance sheet structures***

*Southern African securitisation facility*

Sappi sells the majority of its Rand 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.

The total amount of trade receivables sold at the end of September 2017 amounted to US$72 million (2016: US$91 million).

Details of the securitisation programme at the end of the 2017 and 2016 financial years are disclosed in the table below:

| Bank | Currency | Value | Facility[1] | Discount charges |
|---|---|---|---|---|
| **2017** | | | | |
| Rand Merchant Bank Limited | **ZAR** | **ZAR980 million** | **Unlimited** | **Linked to 3-month JIBAR** |
| **2016** | | | | |
| Rand Merchant Bank Limited | ZAR | ZAR1,249 million | Unlimited | Linked to 3-month JIBAR |

*[1] The securitisation facility is unlimited, but subject to the sale of qualifying receivables to the bank.*

## 17. Trade and other receivables continued

### 17.3 Trade receivables securitisation continued

***Off-balance sheet structures*** *continued*

*Letters of credit discounting*

At the end of each financial month and on a non-recourse basis, the group sells certain letters of credit to Citibank (Hong Kong) and KBC Bank (Hong Kong) and, similarly, discounts certain trade receivables with Union Bancaire Privee (Switzerland), Erste Bank Austria (Erste), HSBC (Mexico), Citibank (São Paulo) and Citibank (New York) by utilising the customers' credit facilities with the discounting bank.

### 17.4 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 2017 and September 2016. 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 US$668 million (2016: US$642 million) represents the group's maximum credit risk exposure from trade and other receivables.

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

| | **2017** | | | 2016 | | |
|---|---|---|---|---|---|---|
| Threshold | **Number of customers** | **US$ million** | **Percentage** | Number of customers | US$ million | Percentage |
| Greater than US$10 million | **6** | **109** | **19** | 5 | 96 | 19 |
| Between US$5 million and US$10 million | **8** | **50** | **9** | 8 | 49 | 9 |
| Less than US$5 million | **2,450** | **412** | **72** | 2,315 | 372 | 72 |
| | **2,464** | **571** | **100** | 2,328 | 517 | 100 |

At balance sheet date, none of the group's customers with balances equal to or greater than US$5 million had breached their contractual maturity terms and thus no impairment charges have been recognised in respect of such customers.

Refer to note 31 for further details on credit risk.

# Notes to the Group Annual Financial Statements

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for the year ended September 2017

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | **Number of shares** | **US$ million** | Number of shares | US$ million |
| **18. Ordinary share capital and share premium** | | | | |
| **Authorised share capital:** | | | | |
| Ordinary shares of ZAR1 each | **725,000,000** | | 725,000,000 | |
| 'A' ordinary shares of ZAR1 each[1] | **19,961,476** | | 19,961,476 | |
| **Issued share capital:** | | | | |
| Fully paid ordinary shares of ZAR1 each | **557,202,573** | **41** | 541,446,223 | 40 |
| Fully paid 'A' ordinary shares of ZAR1 each[1] | **19,961,476** | **2** | 19,961,476 | 1 |
| Treasury shares[2] | **(42,143,854)** | **(3)** | (30,844,098) | (2) |
| Share premium | | **854** | | 840 |
| | **535,020,195** | **894** | 530,563,601 | 879 |
| The movement in ordinary share capital and share premium is reconciled as follows: | | | | |
| Opening balance | | **879** | | 851 |
| Transfers from Sappi Limited Share Incentive Trust | | **4** | | 14 |
| Translation movements | | **11** | | 14 |
| Closing balance | | **894** | | 879 |

[1] *The 'A' ordinary shares are unlisted but rank pari passu with the ordinary shares in all respects except for dividend entitlements where the 'A' ordinary shares are entitled to 50% of the dividends payable on the ordinary shares. The 'A' ordinary shares have the same voting rights as ordinary shares but are not listed on the JSE Limited. Sappi will have the option to repurchase a number of 'A' ordinary shares in August 2019. The number of any 'A' ordinary shares that Sappi elects to buy back on the repurchase date will depend on the price performance of the ordinary shares over the period of the transaction with the remaining 'A' ordinary shares being distributed to the beneficiaries and converted into ordinary shares. The 'A' ordinary shares' rights, terms, conditions of conversion and privileges are contained in Article 38 of Sappi's Memorandum of Incorporation, details of which are available for inspection at the company's registered offices.*

[2] *Includes 22,182,378 (2016: 10,882,622) ordinary shares as well as 19,961,476 (2016: 19,961,476) 'A' ordinary shares that are held by group entities, including the Sappi Limited Share Incentive Trust and the trusts set up to house the Broad-based Black Economic Empowerment transaction. These shares may be utilised to meet the requirements of the trusts.*

## 18. Ordinary share capital and share premium continued

The movement in the number of treasury shares is set out in the table below:

| Number of shares | 2017 | 2016 |
|---|---|---|
| **Ordinary treasury shares:** | | |
| Opening balance | **10,882,622** | 15,041,212 |
| Issue of treasury shares | **15,756,350** | – |
| Treasury shares issued to participants | **(4,456,594)** | (4,158,590) |
| Scheme shares (Refer to note 29) | **(1,218,849)** | (3,396,445) |
| Plan shares (Refer to note 29) | **(3,237,745)** | (762,145) |
| **Closing balance** | **22,182,378** | 10,882,622 |
| **'A' ordinary treasury shares:** | | |
| 'A' ordinary shares issued to the BBBEE trusts | **19,961,476** | 19,961,476 |
| | **42,143,854** | 30,844,098 |

Included in the issued and unissued share capital of 725,000,000 shares is a total of 42,700,870 shares which may be used to meet the requirements of the Sappi Limited Share Incentive Trust (the Scheme) and/or the Sappi Limited Performance Share Incentive Trust (the Plan). In terms of the rules of the Scheme and the Plan, the maximum number of shares which may be acquired in aggregate by the Scheme and/or the Plan, and allocated to participants of the Scheme and/or the Plan, is 42,700,870 shares subject to adjustment of Sappi's issued share capital arising from any conversion, redemption, consolidation, sub-division and/or any rights or capitalisation issue of shares. Sappi is, at all times, obliged to reserve and keep available such number of shares (together with any treasury shares held by Sappi subsidiaries which may be used for the purposes of the Scheme and/or the Plan) as shall then be required in terms of the Scheme and/or the Plan out of its authorised but unissued share capital. Authority to use treasury shares for the purposes of the Scheme and/or the Plan was granted by shareholders at the Annual General Meeting held on 07 March 2005.

### 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 21, 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.

During the 2017 and 2016 financial years, the group was in compliance with the financial covenants relating to the loans payable.

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

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

| | (US$ million) | 2017 | 2016 |
|---|---|---|---|
| **19.** | **Other comprehensive income (loss)** | | |
| | ***Item that will not be reclassified subsequently to profit or loss*** | | |
| | Actuarial gains (losses) on post-employment benefit funds | **68** | (12) |
| | Gross amount | **101** | (20) |
| | Tax | **(33)** | 8 |
| | ***Items that may be or are reclassified subsequently to profit or loss*** | | |
| | Exchange differences on translation to presentation currency | **(1)** | 38 |
| | Translation of foreign operations | **(1)** | 37 |
| | Exchange differences arising on non-distributable reserves | **2** | 1 |
| | Exchange differences arising on hedging reserves | **(2)** | – |
| | Tax | **–** | – |
| | Hedging reserves | **11** | 4 |
| | Movements during the year | **30** | 4 |
| | Reclassified to profit or loss | **(19)** | – |
| | Reclassified to property, plant and equipment | **(1)** | – |
| | Tax | **1** | – |
| | **Other comprehensive income (loss) recorded directly in equity** | **78** | 30 |
| | Profit for the year | **338** | 319 |
| | **Total comprehensive income (loss) for the year** | **416** | 349 |

| (US$ million) | 2017 Legal reserves[1] | 2017 Share-based payment reserve | 2017 Other | 2017 Total | 2016 Legal reserves[1] | 2016 Share-based payment reserve | 2016 Other | 2016 Total |
|---|---|---|---|---|---|---|---|---|
| **20. Non-distributable reserves** | | | | | | | | |
| Opening balance | **58** | **53** | **3** | **114** | 58 | 52 | 3 | 113 |
| Transfers of vested share options | **–** | **(2)** | **–** | **(2)** | – | (7) | – | (7) |
| Share-based payment expense | **–** | **9** | **–** | **9** | – | 7 | – | 7 |
| Translation differences | **2** | **1** | **(1)** | **2** | – | 1 | – | 1 |
| | **60** | **61** | **2** | **123** | 58 | 53 | 3 | 114 |

*[1] Represents equity of the group that is not available for distribution to shareholders other than on liquidation. This is a legal requirement in certain countries which require a percentage of profit (loss) for the year to be transferred to a legal reserve until a certain threshold is reached. This threshold varies from country to country.*

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **21. Interest-bearing borrowings** | | |
| Securitisation debt[1] | **364** | 314 |
| Unsecured borrowings | **1,508** | 1,797 |
| Total borrowings (Refer to note 31) | **1,872** | 2,111 |
| *Less:* Current portion included in current liabilities | **(133)** | (576) |
| Total non-current interest-bearing borrowings | **1,739** | 1,535 |
| The repayment profile of the interest-bearing borrowings is as follows: | | |
| Payable in the year ended September: | | |
| 2017 | | 576 |
| 2018 | **133** | 350 |
| 2019 | **24** | – |
| 2020 | **481** | 83 |
| 2021 | **32** | – |
| 2022 (September 2016: Thereafter) | **533** | 1,102 |
| Thereafter | **669** | |
| | **1,872** | 2,111 |

*[1] Pledged over trade receivables (Refer to note 25 for details of encumbered assets).*

**Capitalised lease liabilities**

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

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 21. **Interest-bearing borrowings** continued

Set out below are details of the more significant interest-bearing borrowings in the group at September 2017:

| | Currency | Interest rate[1] | Principal amount outstanding | Balance sheet value | Security/ cession | Expiry | Financial covenants |
|---|---|---|---|---|---|---|---|
| **Redeemable bonds** | | | | | | | |
| Public bond | EUR | Fixed | €450 million | €444 million[3][4][5] | Unsecured | April 2022 | No financial covenants |
| Public bond | EUR | Fixed | €350 million | €344 million[3][4][5] | Unsecured | April 2023 | No financial covenants |
| Public bond | USD | Fixed | US$221 million | US$218 million[4][5][6] | Unsecured | June 2032 | No financial covenants |
| Public bond | ZAR | Fixed[7] | ZAR500 million | ZAR500 million | Unsecured | April 2018 | No financial covenants |
| Public bond | ZAR | Fixed | ZAR745 million | ZAR744 million[4] | Unsecured | April 2020 | No financial covenants |
| **Secured loans** | | | | | | | |
| UniCredit Bank | EUR | Variable | €200 million | €200 million | Trade receivables (securitisation programme) | August 2020 | EBITDA to net interest and net debt to EBITDA[8] |
| UniCredit Bank | USD | Variable | US$127 million | US$127 million | Trade receivables (securitisation programme) | August 2020 | EBITDA to net interest and net debt to EBITDA[8] |
| **Unsecured bank term loans** | | | | | | | |
| Österreichische Kontrollbank | EUR | Variable | €58 million | €58 million | | December 2017 | No financial covenants |
| Österreichische Kontrollbank | EUR | Fixed | €82 million | €81 million[2][4] | | June 2021 | EBITDA to net interest and net debt to EBITDA[8] |
| Österreichische Kontrollbank | EUR | Fixed | €59 million | €58 million[2][4] | | March 2024 | EBITDA to net interest and net debt to EBITDA[8] |
| GroCapital Financial Services | ZAR | Fixed[7] | ZAR400 million | ZAR400 million | | May 2020 | No financial covenants |

[1] *The nature of the rates for the group bonds are explained in note 31. The nature of the interest rates is determined with reference to the underlying economic hedging instrument.*
[2] *The OeKB provides the funding for this facility but the majority of the credit risk is guaranteed by some of Sappi's relationship banks.*
[3] *Under the relevant indenture, certain limitations exist including dividend distributions and other payments, indebtedness, asset sales, liens, guarantees, and mergers and consolidations. In case of a change of control, holders have a right to require the relevant issuer to repurchase all or any part of their bonds at a purchase price of 101% of the principal amount of bonds.*
[4] *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.*
[5] *Sappi Papier Holding GmbH, Sappi Limited or Sappi International SA may at any time redeem any public bonds (the securities), in whole or in part, at a redemption price equal to the greater of (i) 100% of the principal amount of the securities to be redeemed and (ii) a make-whole amount based on the present values of remaining payments at a rate based on yields of specified US treasury securities plus a premium, as defined in the bond indentures, together with interest calculated on the principal amount of the securities to be redeemed up to the date of redemption.*
[6] *Under the relevant indenture, limitations exist on liens, sale and leaseback transactions, and mergers and consolidations. Sappi Limited must maintain a majority holding in Sappi Papier Holding GmbH group.*
[7] *Rand variable interest rates have been swapped into fixed Rand interest rates. These swaps are subject to hedge accounting.*
[8] *Financial covenants relate to the Sappi Limited group.*

| | Local currency million | US$ million |
|---|---|---|
| **21. Interest-bearing borrowings** continued | | |
| The analysis of the currency per debt is: | | |
| USD | 345 | **345** |
| EUR | 1,190 | **1,406** |
| ZAR | 1,644 | **121** |
| | | **1,872** |

A detailed analysis of total interest-bearing borrowings has been disclosed in note 31.

**Other restrictions**

As is the norm for bank loan debt, a portion of the group's financial indebtedness is subject to cross default provisions above certain de minimis amounts. Breaches in bank covenants in certain subsidiaries, if not corrected in time, might result in a default in group debt, and in this case, a portion of the group's consolidated liabilities might eventually become payable on demand.

During the 2017 and 2016 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.

**Borrowing facilities secured by trade receivables**

The on-balance sheet securitisation programme with UniCredit Bank AG has a limit of US$390 million (€330 million) and, to the extent utilised, is disclosed on the balance sheet together with a corresponding trade receivable. The interest arising on this programme is recorded within finance costs.

In terms of the programme, the securitisation sellers being Sappi Lanaken NV on behalf of Europe, Sappi NA Finance LLC (a special purpose entity) on behalf of North America, and Sappi Papier Holding GmbH on behalf of Sappi Trading sell certain eligible trade receivables to Elektra Purchase N° 29 Limited (Elektra), a securitisation special purpose entity, that is consolidated by the Sappi group. Elektra has a commissioning agreement with Arabella Finance Limited (Arabella), an entity belonging to UniCredit Bank AG that issues commercial paper to fund the purchase of the trade receivables (alternative funding resources are available should the market for commercial paper be disrupted). The funding is settled in US Dollar and Euro.

As at September 2017, a funding reserve, that is reset on a monthly basis, amounted to 14.80% (2016: 19.75%).

The cost of the programme includes a variable component based on EURIBOR/LIBOR (floor 0%), a fixed margin and a commitment fee computed on the difference between US$354 million (€300 million) and the used portion of the programme limit.

The trade receivables are legally transferred; however, these receivables do not qualify for derecognition under IAS 39 as most of the market risk (foreign exchange risk and interest rate risk) and the credit risk is retained by Sappi.

Further detail of the value of trade receivables pledged as security for this programme is included in notes 17 and 25.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 21. Interest-bearing borrowings continued

### 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 is included in the determination of the headroom available.

| (US$ million) | Currency | Interest rate | 2017 | 2016 |
|---|---|---|---|---|
| ***Unutilised committed facilities*** | | | | |
| Syndicated loan/revolving credit facility[(1)] | EUR/ZAR | Variable (EURIBOR/ JIBAR) | **623** | 595 |
| Securitisation facility (if underlying eligible trade receivables would be available) | EUR | Variable (cost of funding bank) | **26** | 56 |
| | | | **649** | 651 |
| ***Unutilised uncommitted facilities*** | | | | |
| Cash management overdraft facility/short-term banking facilities | ZAR | Variable (ZAR bank prime rate) | **20** | 20 |
| Cash management overdraft facility | USD | Variable (LIBOR) | **20** | 20 |
| | | | **40** | 40 |
| **Total unutilised facilities (committed and uncommitted) excluding cash** | | | **689** | 691 |

*[(1)] Two syndicated loans with a consortium of banks with revolving facilities available of €465 million (2016: €465 million) and ZAR1,000 million (2016: ZAR1,000 million). Both facilities were unutilised as at financial year-end. The €465 million facility matures in April 2020, is subject to financial covenants relating to the Sappi Limited group and is unsecured. The ZAR1,000 million 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. The group has paid a total combined commitment fee of US$4.7 million (2016: US$4.7 million) in respect of the two facilities.*

### Fair value

The fair values of all interest-bearing borrowings are disclosed in note 31.

## 22. Other non-current liabilities

| (US$ million) | 2017 | 2016 |
|---|---|---|
| Defined benefit pension plan liabilities (Refer to note 28) | **238** | 326 |
| Other defined benefit plan liabilities (Refer to note 28) | **106** | 108 |
| Long-term employee benefits | **1** | 1 |
| Workmen's compensation | **16** | 20 |
| Long-service awards | **20** | 21 |
| Land restoration obligation | **15** | 13 |
| Restructuring provisions | **4** | 9 |
| Deferred income | **1** | 1 |
| Other | **22** | 19 |
| | **423** | 518 |

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **23. Provisions** | | |
| Restructuring provisions | **13** | 23 |
| Long-term (refer to note 22) | **4** | 9 |
| Short-term | **9** | 14 |
| Other provisions | **1** | 1 |
| | **14** | 24 |

Details of restructuring provisions are provided below:

| (US$ million) | Severance, retrenchment and related costs |
|---|---|
| Balance at September 2015 | 26 |
| Increase in provisions | 6 |
| Utilised | (8) |
| Released during the year | (2) |
| Other movements | 1 |
| Balance at September 2016 | 23 |
| Increase in provisions | 1 |
| Utilised | (7) |
| Released during the year | (5) |
| Translation effect | 1 |
| **Balance at September 2017** | **13** |

**Sappi Europe**

Due to the decline in demand for coated paper, Sappi Europe has embarked on various cost-saving measures during the current and prior financial years. These measures include the centralisation of certain services such as sales and procurement, improving production efficiencies, disposals and closures of non-core assets as well as plant conversions to produce speciality products which are growing market segments. As a result, provisions for severance, retrenchment and related costs have been raised with the majority of the costs expected to be incurred by September 2017 with the long-term provisions expected to be fully utilised by September 2025.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

| | (US$ million) | 2017 | 2016 |
|---|---|---|---|
| **24.** | **Notes to the group statement of cash flows** | | |
| **24.1** | **Cash generated from operations** | | |
| | Profit for the year | **338** | 319 |
| | Adjustment for: | | |
| | Depreciation | **255** | 250 |
| | Fellings | **63** | 56 |
| | Amortisation | **4** | 2 |
| | Taxation charge | **108** | 104 |
| | Net finance costs | **80** | 121 |
| | Restructuring provisions and closure costs raised (reversed) | **1** | 4 |
| | Fair value adjustment gains and growth on plantations | **(79)** | (120) |
| | Post-employment benefits funding | **(43)** | (51) |
| | Non-cash post-retirement plan settlements and amendments | **–** | (8) |
| | Profit (loss) on disposal of assets and businesses | **2** | (15) |
| | Other non-cash items | **19** | 31 |
| | | **748** | 693 |
| **24.2** | **Decrease (increase) in working capital** | | |
| | (Increase) decrease in inventories | **(19)** | (2) |
| | Decrease (increase) in receivables | **(4)** | 9 |
| | (Decrease) increase in payables | **(4)** | (3) |
| | | **(27)** | 4 |
| **24.3** | **Finance costs paid** | | |
| | Interest and other finance costs on liabilities carried at amortised cost | **(107)** | (123) |
| | Premium and costs on early redemption of redeemable bonds and other loans | **–** | (17) |
| | Net foreign exchange gains | **12** | 2 |
| | Net fair value gain (loss) on financial instruments | **–** | 1 |
| | Transfers to financing activities and non-cash items | **(1)** | 30 |
| | | **(96)** | (107) |
| **24.4** | **Taxation paid** | | |
| | Net amounts payable at beginning of year | **(31)** | (20) |
| | Taxation charge to profit or loss | **(95)** | (64) |
| | Translation and other | **1** | (3) |
| | *Less:* Net amounts payable at end of year | **25** | 31 |
| | | **(100)** | (56) |
| **24.5** | **Proceeds on disposal of other non-current assets** | | |
| | Book value of non-current assets disposed of | **6** | 3 |
| | Gain (loss) on disposal | **(2)** | 2 |
| | | **4** | 5 |

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **25. Encumbered assets** | | |
| The book value of trade receivables which are mortgaged, hypothecated or subject to a pledge as security for borrowings, subject to third-party ownership in terms of capitalised leases or suspensive sale agreements, are as follows: | | |
| Trade receivables | **432** | 392 |

The encumbered trade receivables relate to the securitisation facility with UniCredit Bank of US$390 million (€330 million), of which, US$364 million (€308 million) was utilised at financial year-end (refer to notes 17 and 21).

| (US$ million) | 2017 | 2016 |
|---|---|---|
| **26. Commitments** | | |
| **Capital commitments** | | |
| Contracted but not provided | **253** | 42 |
| Approved but not contracted | **219** | 71 |
| | **472** | 113 |
| Future forecast cash flows of capital commitments at September: | | |
| 2017 | | 90 |
| 2018 | **435** | 15 |
| 2019 | **26** | 4 |
| 2020 | **3** | 4 |
| Thereafter | **8** | – |
| | **472** | 113 |
| 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: | | |
| 2017 | | 20 |
| 2018 | **22** | 13 |
| 2019 | **14** | 7 |
| 2020 | **11** | 4 |
| 2021 | **8** | 2 |
| 2022 (2016: Thereafter) | **5** | 4 |
| Thereafter | **17** | |
| | **77** | 50 |

# Notes to the Group Annual Financial Statements

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| | (US$ million) | 2017 | 2016 |
|---|---|---|---|
| **27.** | **Contingent liabilities** | | |
| | Guarantees and suretyships | – | 10 |
| | Other contingent liabilities | 19 | 11 |
| | | 19 | 21 |

Other contingent liabilities mainly relate to environmental and other taxation queries in respect of certain group companies.

As at September 2017, there are no outstanding guarantees issued by Sappi. For September 2016, the bills of exchange where Sappi guaranteed third-party funding of payments to Sappi for certain German accounts receivable were included under guarantees and suretyships.

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.

In September 2012, the Competition Commission of South Africa notified the group that it has initiated an investigation into alleged anti-competitive behaviour between Sappi and a competitor in the South African pulp and paper market. At that time, we reported that the investigation was still in the early stages. As at the end of the 2017 financial year, the investigation remains in its early stages as the dispute is one of a procedural nature.

## 28. Post-employment benefits

**Summary of results**

| | Defined contribution plans | | Defined benefit pension plans | | Post-employment healthcare subsidy | |
|---|---|---|---|---|---|---|
| (US$ million) | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| Post-employment plan costs (credits) recognised in profit or loss | 36 | 34 | 24 | 10 | 6 | 7 |
| Employer contributions paid during the financial year | | | 36 | 38 | 3 | 8 |
| **Amounts presented in the group balance sheet are as follows:** | | | | | | |
| Net pension/healthcare subsidy liabilities (refer to note 22) | | | 238 | 326 | 106 | 108 |
| Net pension assets (refer to note 15)[1] | | | (35) | (23) | – | – |
| Net balance sheet liabilities | | | 203 | 303 | 106 | 108 |
| **Development in the balance sheet for the pension/healthcare subsidy** | | | | | | |
| Net pension/healthcare subsidy liabilities at beginning of year | | | (303) | (315) | (108) | (107) |
| Net pension/healthcare subsidy costs for the year | | | (24) | (18) | (6) | (7) |
| Settlement gains for the year | | | – | 8 | – | – |
| Employer contributions | | | 36 | 38 | 3 | 8 |
| Net actuarial gains for the year | | | 96 | (17) | 5 | (3) |
| Translation differences | | | (8) | 1 | – | 1 |
| Net pension/healthcare liabilities at end of year | | | (203) | (303) | (106) | (108) |

[1] *Defined benefit plans in South Africa and United Kingdom.*

Actuarial valuations of all plans are performed annually with the exception of our South African and United Kingdom defined benefit pension plans where actuarial reviews are performed annually and formal actuarial funding valuations are performed tri-annually.

## 28. Post-employment benefits continued

**Defined contribution plans**

The group operates defined contribution plans of various sizes for all qualifying employees in most regions 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 US$36 million (2016: US$34 million) represents contributions payable to these plans by the group based on rates specified in the rules of these plans. Expected contributions to be paid in the next financial year is US$35 million.

In addition to company-sponsored plans across the group, employees commonly participate in local state plans wherever they exist. State plans exist in most regions to provide such benefits as disability, unemployment income protection, basic state pension, top-ups thereon, and spousal benefits. Eligibility and participation is generally mandatory to local tax payers, usually on residence-based criteria in accordance with domestic laws.

State benefits vary widely in value and accrual formulae from country to country. Contributions are normally paid with domestic taxation or as supplemental national insurance contributions (or the like), at rates set by domestic governments. Participation in state plans involves no obligations on group companies other than to pay contributions according to the rates specified by domestic governments. Costs, where incurred, are included with other employee costs reported elsewhere in the group accounts, and excluded from figures reported in this note.

**Defined benefit pension or retirement lump sum plans**

The group operates several principal defined benefit pension and/or lump sum plans in all regions plus a number of smaller plans. The extent of employee access to these plans vary. Plans open to new entrants or future accrual cover all qualifying employees. All plans have been established in accordance with applicable legal requirements, customs and existing circumstances in each country.

With the exception of our German and Austrian plans, which are unfunded, the assets of our funded plans are held in separate trustee-administered funds which are subject to varying statutory requirements in the particular countries concerned. Generally, the trusts are required by local legislation as well as their respective 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 pension funds comprise management and member-appointed trustees, including (in some instances) an independent trustee, who collectively are responsible for the administration and governance of the trusts.

Benefits are formula-driven, comprising a variety of earnings definitions (such as final average salary or career average revalued earnings) and years of service. Exceptions are certain plans in Germany and Austria that provide fixed value Euro benefits and certain plans in North America that provide benefits based on years of service and a 'US$ multiplier' (a nominal US Dollar value which increases from time to time only by collective bargaining agreement). The table below briefly illustrates the nature of defined benefits and their link with earnings.

| Type of benefit revaluation rate/pensionable salary definition | Location of scheme |
|---|---|
| Final average salary | South Africa, Austria, Germany |
| Career average revalued earnings | Belgium, The Netherlands |
| Frozen benefit | United Kingdom, North America (Salaried plan) |
| Fixed EUR value | Germany |
| Nominal USD value (Periodically revalued) | North America (Works plans) |

Plans remain open to new hires except for plans in North America, South Africa, Austria and some in Germany. Plans in the United Kingdom and one in North America are closed to future accrual.

**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 in each region. 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 with varying degrees of complexity according to the needs of each plan, analysing risk-and-return profiles in order to help set investment and contribution policies for our plans.

The main strategic asset allocation choices that are formulated in the actuarial and technical policies of our plans across the group are shown below. Local regulations impose minimum funding targets which significantly influence the strategic asset allocation of individual plans.

- **South Africa:** Asset mix based on 20% equity instruments, 55% debt instruments, 20% multi-asset and other instruments, 5% cash.
- **Europe including United Kingdom (UK)[1]:** Asset mix based on 35% equity and real estate instruments, 47% debt instruments, 18% multi-asset and other instruments.
- **North America:** Asset mix based on 34% equity instruments, 47% debt instruments, 19% multi-asset and other instruments.

*[1] Weighted average of plans in this region.*

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 28. Post-employment benefits continued

### 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 (including medical aid inflation) 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.

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 (nominal coupon and index-linked coupon) 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.

### Funding policy

The group's subsidiaries fund the entire cost of the entitlements expected to be earned on an annual basis, with the exception of one plan in South Africa, where employees contribute a fixed percentage of pensionable salary. The funding requirements are based on local actuarial measurement frameworks. For prefunded plans, contributions are determined on a current salary base or fixed nominal amounts and, for unfunded plans, contributions are paid to meet ongoing pension payroll. 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.

Apart from paying the costs of the entitlements, the group's subsidiaries are, to various extents, liable to pay additional contributions in cases where the plans do not hold sufficient assets. These range from enforcement by local regulators, reducing accrued entitlements, or a charge over assets.

Expected company contributions for our defined benefit pension/lump sum plans across group subsidiaries over the next financial year are US$33 million.

### Post-employment healthcare subsidy

The group sponsors two defined benefit post-employment plans that provide certain healthcare and life insurance benefits to eligible retired employees of the North American and Southern African operations. Employees are generally eligible for benefits upon retirement and on completion of a specified number of years of service, or joining the company prior to a certain date.

Our healthcare subsidy plan in Southern Africa is partially funded with assets held in a local cell captive. Our subsidy plan in North America is wholly unfunded.

Expected company contributions to fund these subsidies over the next financial year are US$6 million.

### Other employee benefits

Group companies have no significant post-employment defined benefit obligations other than the following:

| (US$ million) | 2017 | 2016 |
|---|---|---|
| Jubilee (long-service award) in continental Europe in other long-term liabilities | **20** | 21 |
| Early retirement (temporary pension) benefit in Belgium | **1** | 1 |
| ATZ (early retirement – temporary salary supplement) obligations in Germany and Austria | **11** | 13 |
| Workmen's compensation benefit obligations in North America | **16** | 20 |

## 28. **Post-employment benefits** continued

| (US$ million) | Defined benefit pension plans<br>**2017** | <br>2016 | Post-employment healthcare subsidy<br>**2017** | <br>2016 |
|---|---|---|---|---|
| **Components of defined benefit cost recognised in profit or loss** | | | | |
| Current service cost | **19** | 16 | **2** | 3 |
| Past service credit | **–** | (6) | **–** | – |
| Interest on net defined benefit | **3** | 6 | **4** | 4 |
| Fund administration costs | **2** | 2 | **–** | – |
| Non-routine settlement gain | **–** | (8) | **–** | – |
| Net amount recognised in profit or loss | **24** | 10 | **6** | 7 |
| Charge attributed to operating cost | **21** | 12 | **2** | 3 |
| Credit attributed to special items** | **–** | (8) | **–** | – |
| Charge attributed to finance cost | **3** | 6 | **4** | 4 |
| **Components of defined benefit cost recognised in other comprehensive income** | | | | |
| Actuarial gains arising from membership experience | **7** | 6 | **2** | 5 |
| Actuarial gains (losses) arising from changes in demographic assumptions | **27** | (2) | **(1)** | (2) |
| Actuarial gains (losses) arising from changes in financial assumptions | **63** | (145) | **4** | (6) |
| Return on plan assets (excluding amounts included in interest income) | **(1)** | 124 | **–** | – |
| Gain (loss) recognised in other comprehensive income | **96** | (17) | **5** | (3) |

*** US$55 million to special items in fiscal 2015: This is the sum of the non-routine settlement plus a portion of past service credit.*

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 28. Post-employment benefits continued

| (US$ million) | Defined benefit pension plans 2017 | Defined benefit pension plans 2016 | Post-employment healthcare subsidy 2017 | Post-employment healthcare subsidy 2016 |
|---|---|---|---|---|
| **Movement in the present value of the defined benefit obligation in the current year** | | | | |
| Defined benefit obligation at beginning of year | **1,409** | 1,365 | **116** | 118 |
| Current service cost | **19** | 16 | **2** | 3 |
| Past service credit | **–** | (6) | **–** | – |
| Interest expense | **45** | 53 | **5** | 5 |
| Plan participants' contributions | **2** | 1 | **–** | – |
| Remeasurements | **(97)** | 141 | **(5)** | 3 |
| Membership experience changes | **(7)** | (6) | **(2)** | (5) |
| Demographic assumption changes | **(27)** | 2 | **1** | 2 |
| Financial assumption changes | **(63)** | 145 | **(4)** | 6 |
| Acquisition of liabilities[1] | **13** | – | **–** | – |
| Non-routine plan settlements | **–** | (46) | **–** | (7) |
| Benefits paid | **(77)** | (80) | **(4)** | (5) |
| Translation difference | **20** | (35) | **–** | (1) |
| Defined benefit obligation at end of year | **1,334** | 1,409 | **114** | 116 |
| – Present value of wholly unfunded obligation | **177** | 157 | **88** | 92 |
| – Present value of wholly or partially funded obligation | **1,157** | 1,252 | **26** | 24 |
| **Movement in the fair value of the plan assets in the current year** | | | | |
| Fair value of plan assets at beginning of year | **1,106** | 1,050 | **8** | 11 |
| Interest income | **42** | 47 | **1** | 1 |
| Employer contributions | **36** | 38 | **3** | 8 |
| Plan participants' contributions | **2** | 1 | **–** | – |
| Remeasurements | | | | |
| Return (loss) on plan assets net of interest income | **(1)** | 124 | **–** | – |
| Acquisition of liabilities[1] | **13** | – | **–** | – |
| Non-routine plan settlements | **–** | (38) | **–** | (7) |
| Benefits paid | **(77)** | (80) | **(4)** | (5) |
| Fund administration costs | **(2)** | (2) | **–** | – |
| Translation difference | **12** | (34) | **–** | – |
| Fair value of plan assets at end of year | **1,131** | 1,106 | **8** | 8 |
| Net balance sheet defined benefit liability | **203** | 303 | **106** | 108 |

[1] *Acquisition of liabilities: Refers to minimum investment return obligations for contribution plans in Belgium. Insignificant effect on balance sheet.*

## 28. Post-employment benefits continued

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

| (US$ million) | Funded pension plans 2017 | Funded pension plans 2016 | Funded subsidy plans 2017 | Funded subsidy plans 2016 |
|---|---|---|---|---|
| Investments quoted in active markets | | | | |
| – Equity and high yield investments | **399** | 409 | **–** | – |
| – Investment grade debt instruments | **201** | 207 | **–** | – |
| – Property investment funds | **14** | 15 | **–** | – |
| Unquoted investments | | | | |
| – Equity and high yield investments[1] | **501** | 445 | **7** | 7 |
| Cash | **16** | 30 | **1** | 1 |
| | **1,131** | 1,106 | **8** | 8 |
| Total investment return on plan assets | **41** | 171 | **1** | 1 |

[1] *Funded plans consist of commingled funds that are not quoted in active markets. However, the underlying securities held by these funds are quoted in active markets or the prices of these underlying securities are determined by other observable market data. Funded subsidy plans consist of with-profit annuities where distributable income is subject to the discretion of the insurer's investment returns.*

As at financial year-end, there were no investments in the group's own quoted equity instruments.

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 and post-employment medical aid subsidies for the group's plans (weighted average per region) are shown below:**

| | 2017 North America | 2017 Europe (incl UK) | 2017 Southern Africa | 2016 North America | 2016 Europe (incl UK) | 2016 Southern Africa |
|---|---|---|---|---|---|---|
| Discount rate – pension (%) | **3.53** | **1.90** | **9.28** | 3.24 | 1.60 | 9.40 |
| Discount rate – post-employment healthcare subsidy (%) | **3.35** | **n/a** | **9.75** | 3.01 | n/a | 9.50 |
| Future salary increase rate – pension (%) | **–** | **1.00** | **7.28** | – | 0.90 | 8.50 |
| Cost of living adjustment for pensions in payment (%)[1] | **–** | **2.00** | **5.03** | – | 2.00 | 6.00 |
| Healthcare cost trend rate (%)[2] | **8.20 – >4.50** | **n/a** | **8.25** | 7.80 – >5.00 | n/a | 8.50 |
| Sample rate average life expectancy from retirement (years)[3] | | | | | | |
| – For current beneficiaries | **25.60** | **23.90** | **19.20** | 26.00 | 23.80 | 19.20 |
| – For future retiring beneficiaries | **27.30** | **25.70** | **20.20** | 28.00 | 25.70 | 20.20 |

[1] *Weighted average for plans granting cost of living adjustment whether fixed or variable.*
[2] *North America: Initial rate – > long-term rate trend over 10 years (2016: Nine years).*
[3] *Based on local mortality tables in use (with modifications to reflect expected changes in mortality over time) for males at age 60.*

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## 28. Post-employment benefits continued

**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, healthcare 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, while holding all other assumptions constant.

- If the discount rate is 100 basis points higher (lower), the defined benefit obligation would decrease by US$168 million (increase by US$207 million).
- If the expected salary increase rate is 100 basis points higher (lower), the defined benefit obligation would increase by US$19 million (decrease by US$16 million)
- If the expected cost of living adjustment rate is 100 basis points higher (lower), the defined benefit obligation would increase by US$49 million (decrease by US$49 million)
- If the expected healthcare cost trend rate is 100 basis points higher (lower), the defined benefit obligation would increase by US$6 million (decrease by US$5 million)
- If the life expectancy increases (decreases) by one year for both men and women, the defined benefit obligation would increase by US$37 million (decrease by US$35 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 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 (per region) is as follows:

| | Pension plans | Healthcare subsidy |
|---|---|---|
| North America | 12 years | 9 years |
| Europe (Including UK) | 12 years | n/a |
| Southern Africa | 18 years | 16 years |

**Regional split of results**

| (US$ million) | **2017** North America | **2017** Europe (incl UK) | **2017** Southern Africa | 2016 North America | 2016 Europe (incl UK) | 2016 Southern Africa |
|---|---|---|---|---|---|---|
| Defined benefit obligation (pension) | **(710)** | **(496)** | **(128)** | (763) | (510) | (136) |
| Defined benefit obligation (healthcare) | **(88)** | **n/a** | **(26)** | (92) | n/a | (24) |
| Fair value of plan assets (pension) | **696** | **290** | **145** | 667 | 280 | 159 |
| Fair value of plan assets (healthcare) | **–** | **n/a** | **8** | – | n/a | 8 |
| Net defined benefit liability | **(102)** | **(206)** | **(1)** | (188) | (230) | 7 |
| **Development of the regional balance sheets** | | | | | | |
| Net defined benefit liability at beginning of year | **(188)** | **(230)** | **7** | (196) | (234) | 8 |
| Defined benefit cost recognised in profit or loss (pension) | **(12)** | **(8)** | **(4)** | (4) | (3) | (3) |
| Defined benefit cost recognised in profit or loss (healthcare) | **(5)** | **n/a** | **(1)** | (5) | n/a | (2) |
| Net gain (loss) recognised in other comprehensive income (pension) | **80** | **23** | **(7)** | (4) | (8) | (5) |
| Net gain (loss) recognised in other comprehensive income (healthcare) | **6** | **n/a** | **(1)** | (3) | n/a | – |
| Company contributions paid during the year | **17** | **17** | **5** | 24 | 14 | 8 |
| Translation differences | **–** | **(8)** | **–** | – | 1 | 1 |
| Net defined benefit liability at end of year | **(102)** | **(206)** | **(1)** | (188) | (230) | 7 |

## 29. 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 (equivalent to 7.89% of the ordinary shares in issue).

**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.

# Notes to the Group Annual Financial Statements
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for the year ended September 2017

## 29. Share-based payments continued

Movements in share options and performance shares for the financial years ended September 2017 and September 2016 are as follows:

| | Performance shares[1] | Share options | Weighted average share option exercise price (ZAR) | **Total shares** |
|---|---|---|---|---|
| Outstanding at September 2015 | 12,014,143 | 6,433,248 | 34.77 | **18,447,391** |
| – Offered | 3,765,350 | – | – | **3,765,350** |
| – Paid for/vested | (762,145) | (3,396,445) | 37.93 | **(4,158,590)** |
| – Returned, lapsed and forfeited | (985,574) | (211,124) | 48.90 | **(1,196,698)** |
| Outstanding at September 2016 | 14,031,774 | 2,825,679 | 30.23 | **16,857,453** |
| – Offered | 3,021,770 | – | – | **3,021,770** |
| – Paid for/vested | (3,237,745) | (1,218,849) | 31.48 | **(4,456,594)** |
| – Returned, lapsed and forfeited | (331,044) | (181,041) | 34.88 | **(512,085)** |
| Outstanding at September 2017 | 13,484,755 | 1,425,789 | 28.99 | **14,910,544** |
| Exercisable at September 2015 | – | 5,785,544 | 36.10 | |
| Exercisable at September 2016 | – | 2,825,679 | 30.23 | |
| Exercisable at September 2017 | – | 1,425,789 | 28.99 | |

[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.*

The following table sets out the number of share options and performance shares outstanding:

| | **2017** | 2016 | Vesting conditions | Vesting date | Expiry date | Exercise price (ZAR) |
|---|---|---|---|---|---|---|
| **Share options:** | | | | | | |
| 22 December 2008 | **–** | 347,140 | Time | Vested | 22 December 2016 | 35.50 |
| 09 December 2009 | **272,550** | 629,540 | Time | Vested | 09 December 2017 | 33.85 |
| 03 December 2010 | **462,825** | 768,450 | Time | Vested | 03 December 2018 | 35.20 |
| 02 December 2011 | **690,414** | 1,080,549 | Time | Vested | 02 December 2019 | 22.90 |
| **Performance shares:** | | | | | | |
| 07 December 2012 | **–** | 3,226,303 | Performance | 07 December 2016 | n/a | n/a |
| 13 December 2013 | **3,658,024** | 3,750,723 | Performance | 13 December 2017 | n/a | n/a |
| 04 December 2014 | **3,190,630** | 3,307,105 | Performance | 04 December 2018 | n/a | n/a |
| 07 December 2015 | **3,644,447** | 3,747,643 | Performance | 07 December 2019 | n/a | n/a |
| 09 December 2016 | **2,991,654** | – | Performance | 09 December 2020 | n/a | n/a |
| | **14,910,544** | 16,857,453 | | | | |

## 29. 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 Plan:

| | Issue 42 | Issue 42 |
|---|---|---|
| Date of grant | 09 December 2016 | 09 December 2016 |
| Type of award | Performance | Performance |
| Share price at grant date | ZAR86.23 | ZAR86.23 |
| 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 | 80% | 80% |
| Number of shares offered | 1,505,950 | 1,505,950 |
| Volatility | 33% | n/a |
| Risk-free discount rate | 1.7% (US yield) | n/a |
| Expected dividend yield | 2.1% | 2.1% |
| Model used to value | Monte-Carlo | Market price |
| Fair value of option | ZAR65.09 | ZAR68.98 |

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

Refer to note 37 for more information on directors' and prescribed officers' participation in the Scheme and the Plan.

No new loans have been granted to the executive directors since 28 March 2002.

### 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 Southern 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 Southern African employees (62.5%)
- Southern African black managers (15%)
- Strategic partners (12.5%) (refer below for more detail), and
- Communities surrounding the Southern 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 ZAR33.50.
- 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 ZAR1 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 Southern 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 Southern African business under the Forestry Charter and BBBEE legislation in general.

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## 29. Share-based payments continued

***The BBBEE transaction*** continued

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

| Entity | Ordinary share allocation |
|---|---|
| **Strategic partners** | |
| Lereko Investments Proprietary Limited | 1,971,693 |
| Malibongwe Women Development Trust | 432,842 |
| AMB Capital Limited | 643,227 |
| | 3,047,762 |
| **Employees** (Through the ESOP Trust) | 1,280,597 |
| Total | 4,328,359 |

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 | 19,961,476 |

The group incurred a share-based payment expense of US$1 million (2016: US$1 million) during the 2017 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 | ZAR32.50 |
| Share price hurdle rate | 9.1% |
| Hurdle rate price | ZAR75.34 |
| 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 ESOP Trust and MSOP 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 |

Refer to note 18 for further details regarding the 'A' ordinary shares.

| | (US$ million) | | 2017 | 2016 |
|---|---|---|---|---|
| **30.** | **Derivative financial instruments** | | | |
| | **Hedging instrument** | **Hedged item** | | |
| | ***Non-current assets*** | | | |
| | Interest rate swap | Unsecured ZAR500 million bond due April 2018 | **–** | 1 |
| | | | **–** | 1 |
| | ***Current assets*** | | | |
| | Pulp swaps | Raw materials | **1** | – |
| | Interest rate currency swap | Public bond due July 2017[1] | **–** | 38 |
| | Forward exchange contracts | Various | **2** | 6 |
| | | | **3** | 44 |
| | ***Current liabilities*** | | | |
| | Pulp swaps | Raw materials | **–** | 1 |
| | Forward exchange contracts | Various | **3** | 1 |
| | FX zero cost collar | Highly probable forecast sales | **2** | – |
| | | | **5** | 2 |

[1] *This cash flow hedging instrument was settled upon the redemption of the 2017 public bond.*

Refer to note 31 for more detail on financial instruments.

## 31. Financial instruments

The group's financial instruments consist mainly of cash and cash equivalents, accounts receivable, certain investments, accounts payable, 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
- Commodity price risk

(b) Liquidity risk
(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 coordinated on a group basis, while 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.

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## 31. Financial instruments continued

### (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 principle 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 2017 and thereafter are based on the yield curves for each respective currency as published by Bloomberg on 1 October 2017. The information is presented in US Dollar, which is the group's reporting currency.

| (US$ equivalent in millions) | 2018 | 2019 | Expected maturity date 2020 | 2021 | 2022 | 2023+ | **2017 Carrying value** | **2017 Fair value** | 2016 Carrying value | 2016 Fair value |
|---|---|---|---|---|---|---|---|---|---|---|
| **US Dollar** | | | | | | | | | | |
| Fixed rate debt | – | – | – | – | – | 218 | **218** | **237** | 617 | 643 |
| Average interest rate (%) | – | – | – | – | – | 7.61 | **7.61** | | 7.72 | |
| Variable rate debt[1] | – | – | 127 | – | – | – | **127** | **127** | 109 | 109 |
| Average interest rate (%) | – | – | 3.49 | – | – | – | **3.49** | | 2.71 | |
| **Euro** | | | | | | | | | | |
| Fixed rate debt | 27 | 24 | 33 | 32 | 533 | 451 | **1,100** | **1,214** | 884 | 971 |
| Average interest rate (%) | 0.02 | 1.26 | 1.49 | 1.51 | 3.90 | 3.64 | **3.36** | | 3.71 | |
| Variable rate debt[2] | 69 | – | 237 | – | – | – | **306** | **306** | 382 | 383 |
| Average interest rate (%) | 0.50 | – | 1.81 | – | – | – | **1.51** | | 1.76 | |
| **Rand** | | | | | | | | | | |
| Fixed rate debt[3] | 37 | – | 84 | – | – | – | **121** | **127** | 119 | 125 |
| Average interest rate (%) | 7.46 | – | 7.99 | – | – | – | **7.83** | | 7.83 | |
| **Total** | | | | | | | | | | |
| Fixed rate debt | 64 | 24 | 117 | 32 | 533 | 669 | **1,439** | **1,578** | 1,620 | 1,739 |
| Average interest rate (%) | 4.27 | 1.26 | 6.18 | 1.51 | 3.40 | 5.11 | **4.38** | | 5.54 | |
| Variable rate debt | 69 | – | 364 | – | – | – | **433** | **433** | 491 | 492 |
| Average interest rate (%) | 0.50 | – | 2.40 | – | – | – | **2.09** | | 1.97 | |
| **Fixed and variable** | 133 | 24 | 481 | 32 | 533 | 669 | **1,872** | **2,011** | 2,111 | 2,231 |
| Current portion | | | | | | | **133** | **135** | 576 | 600 |
| Long-term portion | | | | | | | **1,739** | **1,876** | 1,535 | 1,631 |
| Total interest-bearing borrowings (refer to note 21) | | | | | | | **1,872** | **2,011** | 2,111 | 2,231 |

[1] *The US Dollar floating interest rates are based on the London Inter-bank Offered Rate (LIBOR).*
[2] *The Euro floating interest rates are based on the European Inter-bank Offered Rate (EURIBOR).*
[3] *Rand floating rates of ZAR900 million debt have been swapped into Rand fixed rates. These swaps are subject to hedge accounting.*

## 31. Financial instruments continued

**(a) Market risk** continued

***Interest rate risk*** continued

*Interest-bearing borrowings* continued

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.

The range of interest rates in respect of all non-current borrowings, comprising both fixed and floating rate obligations, is between 1.26% and 7.99% (depending on currency). At September 2017, after giving effect to interest rate swaps, 76.86% of Sappi's borrowings were at fixed rates of interest and 23.14% were at floating rates. Fixed rates of interest are based on contract rates.

A detailed analysis of the group's borrowings is presented in note 21.

*Hedging of interest rate risk*

Sappi uses interest rate swaps (IRS) and interest rate and currency swaps (IRCS) as a means of managing interest rate risk associated with outstanding debt entered into in the normal course of business. Sappi does not use these instruments for speculative purposes. Interest rate derivative financial instruments are measured at fair value at each reporting date with changes in fair value recorded in profit or loss for the period or in other comprehensive income (OCI), depending on the hedge designation as described in a documented hedging strategy.

***Cash flow hedges***

The effective gains or losses from changes in fair value of the derivatives designated in a cash flow hedge are recorded in OCI. These accumulated gains or losses will be recycled to profit or loss in the same account as the hedged item when the hedged item affects profit or loss.

At inception and at the beginning of each quarterly reporting period, the future effectiveness of the hedge relationship is assessed by using the linear regression analysis.

In order to measure retrospective hedge effectiveness, a hypothetical derivative with identical critical terms as the hedged item has been built as a perfect hedge. The periodic Dollar-offset retrospective hedge effectiveness test is based on the comparison of the actual past periodical changes in fair value between the hedging derivative and the hypothetical derivative. For effectiveness, the ratio of the periodic change in fair value of the hedging instrument since inception or since the last quarterly measurement divided by the periodic change in fair value of the hypothetical derivative since inception or since the last quarterly measurement for the hedge must fall within the range of 80% to 125%. If, however, both changes in fair value are less than 1% of the notional amount of the IRCS, these changes in fair value are considered to be both immaterial and the hedge effectiveness test is met.

The valuation of the hedging instruments includes an adjustment for credit risk, ie an asset includes a counterparty credit risk spread, whereas the fair value measurement of a liability includes Sappi's own credit risk spread.

*Interest rate and currency swaps (IRCS)*

In July 2012, Sappi entered into fixed for fixed IRCS which were designated as cash flow hedges of future cash flows linked to fixed rate debt denominated in foreign currency. The US$400 million senior notes due 2017 and the corresponding IRCS were repaid in April 2017 (the US$300 million senior secured notes due 2019 with corresponding swaps had already been redeemed in 2015). There are no remaining IRCS as at September 2017.

*Interest rate swaps floating to fixed*

In April and May 2013, Sappi issued floating rate debt to the total amount of ZAR1,155 million maturing in 2016, 2018 and 2020 and swapped the floating rates into fixed rates. These liabilities and the corresponding interest rate swaps are designated in cash flow hedging relationships, allowing all mark-to-market valuations of the swaps to be booked to equity. As all critical terms of the hedged items and the hedging instruments match perfectly, the hedges are expected to continue being highly effective. In April 2016, ZAR255 million floating rate debt and the corresponding swaps came to maturity and the debt was repaid.

At September 2017, the remaining hedges were highly effective and the swaps had in total a net positive fair value of US$0.4 million which was deferred to equity.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 31. Financial instruments continued

**(a) Market risk** continued

***Summary of outstanding cash flow and fair value hedges***

| (US$ million) | Interest rate | Maturity date | Nominal value | Total fair value[1] | Recorded in OCI | Recorded in Profit or loss |
|---|---|---|---|---|---|---|
| **September 2017** | | | | | | |
| **Cash flow hedges** | | | | | | |
| IRS | **Rand variable (JIBAR) to Rand 7.46% fixed** | **April 2018** | **ZAR500 million** | **–** | **–** | **–** |
| IRS | **Rand variable (JIBAR) to Rand 7.85% fixed** | **May 2018** | **ZAR400 million** | **–** | **–** | **–** |
| | | | | **–** | **–** | **–** |
| **September 2016** | | | | | | |
| **Cash flow hedges** | | | | | | |
| IRCS | US Dollar 7.75% into Euro 7.56% | July 2017 | US$400 million | 38 | (3) | 41 |
| IRS | Rand variable (JIBAR) to Rand 7.46% fixed | April 2018 | ZAR500 million | 1 | 1 | – |
| IRS | Rand variable (JIBAR) to Rand 7.85% fixed | May 2018 | ZAR400 million | – | 1 | – |
| | | | | 39 | (1) | 41 |

[1] *This refers to the carrying value.*

The total fair values of the IRCS and IRS are the estimated amounts that Sappi would pay or receive to terminate the agreements at balance sheet date after taking into account current interest rates and the current creditworthiness of the counterparties as well as the specific relationships of the group with those counterparties. However, this amount excludes the possible breakage and other fees that would be incurred in case of a sale before the maturity date.

***Sensitivity analyses***

The following are sensitivity analyses, in US Dollar, of the impact on profit or loss arising from:

*Sensitivity analysis: interest rate risk – in case of a credit rating downgrade of Sappi*

The table below shows the sensitivity of certain debt to changes in the group's own credit rating. The agreements of these specific external loans (including the on-balance sheet securitisation programme) stipulate that if the company were downgraded below its current rating, an additional margin would be added to the contractual funding rate.

| (US$ million) | Notional | Impact on profit or loss of downgrade below current credit rating |
|---|---|---|
| Securitisation – Elektra N° 29 Limited | 364 | 1.35 |
| Commitment fee on unused revolving credit facility | 549 | 0.66 |
| Interest on utilised bank syndicated loans | 70 | 0.17 |
| Commitment fee on unused bank syndicated loans | 108 | 0.09 |
| | 1,091 | 2.27 |
| Impact calculated on total portfolio amounts to | 0.21% | |

*Sensitivity analysis: interest rate risk of floating rate debt*

The table below shows the sensitivity of the floating rate debt to a move by 50bps to the interest rates.

| (US$ million) | Total | Fixed rate debt | Floating rate debt | Impact on profit or loss of 50bps interest |
|---|---|---|---|---|
| Total debt | 1,872 | 1,439 | 433 | 2 |
| **Ratio fixed/floating to total debt** | | 76.86% | 23.14% | |

The floating rate debt represents 23.14% of total debt. If interest rates were to increase (decrease) by 50bps, the finance cost on floating rate debt would increase (decrease) by US$2.17 million.

## 31. Financial instruments continued

### (a) Market risk 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
- 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, and
- Translation exposures arise from translating the group's assets, liabilities, income and expenditure into the group's presentation currency.

Borrowings are taken out in a range of currencies which are based on the group's preferred ratios of gearing and interest cover based on a judgement of the best financial structure for the group. This gives rise to translation exposure on consolidation.

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 2017 and 2016 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.

| (US$ million) | Total | Total in scope | USD | EUR | ZAR | GBP | Other |
|---|---|---|---|---|---|---|---|
| **September 2017** | | | | | | | |
| **Classes of financial instruments** | | | | | | | |
| ***Non-current assets*** | | | | | | | |
| Other non-current assets | **51** | **9** | – | 9 | – | – | – |
| ***Current assets*** | | | | | | | |
| Trade receivables | **571** | **571** | 262 | 240 | 8 | 29 | 32 |
| Prepayments and other receivables | **97** | **32** | 11 | 12 | 8 | – | 1 |
| Derivative financial instruments | **3** | **3** | (100) | 18 | 81 | – | 4 |
| Cash and cash equivalents | **550** | **550** | 268 | 47 | 215 | – | 20 |
| | | **1,165** | 441 | 326 | 312 | 29 | 57 |
| ***Non-current liabilities*** | | | | | | | |
| Interest-bearing borrowings | **1,739** | **1,739** | 345 | 1,309 | 85 | – | – |
| Other non-current liabilities | **423** | **1** | 1 | – | – | – | – |
| ***Current liabilities*** | | | | | | | |
| Interest-bearing borrowings | **133** | **133** | – | 96 | 37 | – | – |
| Derivative financial instruments | **5** | **5** | 1 | – | 2 | 2 | – |
| Trade payables | **502** | **502** | 168 | 217 | 115 | 1 | 1 |
| Other payables and accruals | **356** | **157** | 33 | 81 | 42 | – | 1 |
| | | **2,357** | 548 | 1,703 | 281 | 3 | 2 |
| Foreign exchange gap | | **(1,372)** | (107) | (1,377) | 31 | 26 | 55 |

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 31. **Financial instruments** continued

**(a) Market risk** continued

***Currency risk*** continued

*Currency risk analysis* continued

| (US$ million) | Total | Total in scope | USD | EUR | ZAR | GBP | Other |
|---|---|---|---|---|---|---|---|
| **September 2016** | | | | | | | |
| **Classes of financial instruments** | | | | | | | |
| ***Non-current assets*** | | | | | | | |
| Other non-current assets | 39 | 10 | – | 10 | – | – | – |
| Derivative financial instruments | 1 | 1 | – | – | 1 | – | – |
| ***Current assets*** | | | | | | | |
| Trade receivables | 517 | 517 | 224 | 226 | 11 | 29 | 27 |
| Prepayments and other receivables | 125 | 39 | 9 | 17 | 13 | – | – |
| Derivative financial instruments | 44 | 44 | (420) | 421 | 42 | 1 | – |
| Cash and cash equivalents | 703 | 703 | 309 | 94 | 279 | 1 | 20 |
| | | 1,314 | 122 | 768 | 346 | 31 | 47 |
| ***Non-current liabilities*** | | | | | | | |
| Interest-bearing borrowings | 1,535 | 1,535 | 327 | 1,088 | 120 | – | – |
| Other non-current liabilities | 518 | 1 | 1 | – | – | – | – |
| ***Current liabilities*** | | | | | | | |
| Interest-bearing borrowings | 576 | 576 | 398 | 178 | – | – | – |
| Derivative financial instruments | 2 | 2 | (15) | 1 | 16 | – | – |
| Trade payables | 455 | 455 | 161 | 162 | 130 | – | 2 |
| Other payables and accruals | 384 | 164 | 25 | 99 | 39 | – | 1 |
| | | 2,733 | 897 | 1,528 | 305 | – | 3 |
| Foreign exchange gap | | (1,419) | (775) | (760) | 41 | 31 | 44 |

*Hedging of foreign currency risk*

*Foreign currency forward exchange contracts*

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

| (US$ million) | | **2017** Contract amount (notional amount) | **2017** Fair value (unfavour-able) favourable | 2016 Contract amount (notional amount) | 2016 Fair value (unfavour-able) favourable |
|---|---|---|---|---|---|
| Foreign currency | | | | | |
| Bought: | USD | **3** | **3** | 5 | – |
| | EUR | **93** | **92** | 72 | 1 |
| | ZAR | **118** | **118** | 49 | 2 |
| Sold: | USD | **(97)** | **(99)** | (95) | 3 |
| | EUR | **(11)** | **(11)** | – | – |
| | ZAR | **(39)** | **(38)** | (23) | (1) |
| | | **67** | **65** | 8 | 5 |

## 31. Financial instruments continued

**(a) Market risk** continued

***Currency risk*** continued

*Foreign currency forward exchange contracts* continued

The fair value of foreign currency contracts has been computed by the group using the market data at the end of the 2017 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 April 2020.

As at September 2017, there was an open exposure of US$23 million that has since been hedged.

***Sensitivity analysis – (loss) gain***

| Base currency | Exposure (US$ million) | +10% | –10% |
|---|---|---|---|
| AUD | 4.7 | 0.4 | (0.5) |
| CHF | 5.1 | 0.5 | (0.6) |
| EUR | (6.8) | (0.6) | 0.8 |
| GBP | 2.6 | 0.2 | (0.3) |
| USD | (2.0) | (0.2) | 0.2 |
| ZAR | (26.8) | (2.4) | 3.0 |
| Other currencies | 0.5 | 0.0 | (0.1) |
| Total | (22.7) | (2.1) | 2.5 |

Based on the exposure at the end of September 2017, 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 US$2.1 million or a gain of US$2.5 million respectively.

During 2017, we contracted non-deliverable average rate foreign exchange transactions for a total notional value of US$421 million which were used as an overlay hedge of export sales from Southern Africa. The total impact on profit or loss amounted to a gain of US$26 million (including positive forward points of US$7 million). We also contracted zero cost foreign exchange collars for a total notional value of US$150 million. This collar complements the other strip cover hedges (using non-deliverable FX forwards) by covering a different portion of the economic FX exposure.

As at September 2017 the impact of the marking to market relating to the time value of the collar amounted to an unrealised loss of US$1.5 million.

***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 2017 financial year, the hedges were highly effective. A net realised gain of US$18.8 million relating to the realised non-deliverable forward exchange contracts was transferred from OCI to revenue in profit or loss and at the financial year-end, a negative amount of US$0.1 million was deferred in equity.

As per September 2017 the zero cost FX collars did not have any intrinsic value as the year-end FX rate was inside the range of the strike levels.

# Notes to the Group Annual Financial Statements

continued

for the year ended September 2017

## 31. **Financial instruments** continued

**(a) Market risk** continued

***Cash flow hedges*** continued

*Foreign currency forward exchange contracts* continued

*Net investment hedges*

The hedge of the net investment designated in February 2010, has been de-designated in March 2016. At the moment of the de-designation the life-to-date negative foreign exchange differences amounting to €36.9 million (US$41.5 million), will remain in equity until the disposal or liquidation of the foreign operation.

In March 2016, Sappi designated a new net investment hedge for an indeterminate period of Sappi Papier Holding GmbH (SPH) in SD Warren Holdings Corporation (North America) including all its subsidiaries and incorporating all net assets.

During 2017 several de-designations and re-designations took place in line with the evolving net US Dollar exposure linked to the net investment. As at September 2017 the hedged notional amount at amortised cost amounted to US$102 million.

The hedged risk is the currency risk associated with the spot retranslation of the net assets of the foreign operation into the functional currency of the consolidating parent entities at the level of which the hedge is designated, ie SPH for US Dollar/Euro spot exchange rate risk and Sappi Limited for US Dollar/Rand spot exchange rate risk. The hedging instrument is a non-derivative foreign currency external debt instrument. At the inception of the hedge (or on hedge designation date), both the designated portion of the net investment in the foreign operation (as hedged item) and the foreign currency denominated debt (as hedging instrument) were recorded at the spot rate.

To the extent that the hedge is effective, foreign exchange rate differences linked to the subsequent revaluation of the foreign currency debt in the books of the entity holding the debt are deferred in OCI until the foreign operation is disposed of or liquidated. These foreign exchange currency differences are recognised in profit or loss on disposal or liquidation of the foreign operation as part of the gain or loss on disposal.

Ineffectiveness can only occur if the net investment carrying value of the foreign operation would fall below the designated amount of the hedging instruments. The net investment value of the foreign operation is validated each quarter. Ineffective gains or losses are booked directly to the group income statement. As at the end of the 2017 financial year, the hedge was 100% effective.

| (US$ million) | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Hedged notional** | **Foreign exchange result deferred in OCI** | Hedged notional | Foreign exchange result deferred in OCI |
| Bond 2032 | **102** | **0.2** | 49 | (1) |
| Previous designations | **–** | **(34)** | – | (41) |
| | **102** | **(34)** | 49 | (42) |
| Net investment value of North America | **798** | | 733 | |

## 31. Financial instruments continued

### (a) Market risk continued

***Commodity price risk***

Commodity price risk arises mainly from price volatility and threats to supply of raw material and other inputs to the production process.

A combination of contract and spot deals are used to manage price volatility and contain costs. Contracts are limited to the group's own use requirements.

During 2017, pulp swaps in Europe were contracted for a limited volume of pulp (30,000 tons). Sappi Europe buys pulp from external suppliers at a variable price consisting of a reference price linked to the Pix Pulp index which is adjusted with a premium depending on the pulp market conditions.

As Sappi Europe expected pulp prices to increase, it was decided to fix the pulp price for one year by entering into a pulp swap whereby the variable price was swapped for an annual fixed price. A realised gain of US$1.6 million resulting from the settled pulp contracts was booked into the income statement.

The group's pulp swap contracts outstanding at September 2017 are detailed below:

| | | **2017** | | 2016 | |
|---|---|---|---|---|---|
| (US$ million) | Base currency | **Contract amount (notional amount)** | **Fair value (unfavour-able) favourable** | Contract amount (notional amount) | Fair value (unfavour-able) favourable |
| Bleached Hardwood Kraft Pulp (BHKP) Bought: | EUR | **–** | **–** | 6 | (1) |
| Bleached Hardwood Kraft Pulp (BHKP) Bought: | USD | **4** | **1** | | |
| | | **4** | **1** | 6 | (1) |

### (b) 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 21.

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

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 31. Financial instruments continued

**(b) Liquidity risk** continued

***Liquidity risk management***

The following tables for the 2017 and 2016 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.

| (US$ million) | Total financial assets and liabilities | Fair value of financial instru-ments | Undiscounted cash flows 0 – 6 months | 6 – 12 months | 1 – 2 years | 2 – 5 years | >5 years | Total |
|---|---|---|---|---|---|---|---|---|
| **September 2017** | | | | | | | | |
| ***Non-current assets*** | | | | | | | | |
| Other non-current assets | **9** | **9** | – | 1 | 3 | 5 | 1 | 10 |
| ***Current assets*** | | | | | | | | |
| Trade receivables | **571** | **571** | 571 | – | – | – | – | 571 |
| Prepayments and other receivables | **32** | **32** | 31 | 1 | – | – | – | 32 |
| Derivative financial instruments | **3** | **3** | 1 | 2 | – | – | – | 3 |
| Cash and cash equivalents | **550** | **550** | 550 | – | – | – | – | 550 |
| | | | 1,153 | 4 | 3 | 5 | 1 | 1,166 |
| ***Non-current liabilities*** | | | | | | | | |
| Interest-bearing borrowings | **1,739** | **1,871** | 27 | 28 | 62 | 1,248 | 922 | 2,287 |
| Other non-current liabilities | **1** | **1** | – | – | 1 | – | – | 1 |
| ***Current liabilities*** | | | | | | | | |
| Interest-bearing borrowings | **133** | **133** | 72 | 61 | – | – | – | 133 |
| Derivative financial instruments | **5** | **5** | 5 | – | – | – | – | 5 |
| Trade payables | **502** | **502** | 502 | – | – | – | – | 502 |
| Other payables and accruals | **157** | **157** | 157 | – | – | – | – | 157 |
| | | | 763 | 89 | 63 | 1,248 | 922 | 3,085 |
| Liquidity surplus (gap) | | | 390 | (85) | (60) | (1,243) | (921) | (1,919) |

## 31. Financial instruments continued

**(b) Liquidity risk** continued

***Liquidity risk management*** continued

| (US$ million) | Total financial assets and liabilities | Fair value of financial instru-ments | Undiscounted cash flows 0 – 6 months | 6 – 12 months | 1 – 2 years | 2 – 5 years | >5 years | Total |
|---|---|---|---|---|---|---|---|---|
| **September 2016** | | | | | | | | |
| ***Non-current assets*** | | | | | | | | |
| Other non-current assets | 10 | 10 | 2 | 2 | – | 5 | 1 | 10 |
| Derivative financial instruments | 1 | 1 | – | – | 1 | – | – | 1 |
| ***Current assets*** | | | | | | | | |
| Trade receivables | 517 | 517 | 517 | – | – | – | – | 517 |
| Prepayments and other receivables | 39 | 39 | 38 | 1 | – | – | – | 39 |
| Derivative financial instruments | 44 | 44 | 8 | 42 | – | – | – | 50 |
| Cash and cash equivalents | 703 | 703 | 703 | – | – | – | – | 703 |
| | | | 1,268 | 45 | 1 | 5 | 1 | 1,320 |
| ***Non-current liabilities*** | | | | | | | | |
| Interest-bearing borrowings | 1,535 | 1,632 | 16 | 30 | 393 | 247 | 1,351 | 2,037 |
| Other non-current liabilities | 1 | 1 | – | – | 1 | – | – | 1 |
| ***Current liabilities*** | | | | | | | | |
| Interest-bearing borrowings | 576 | 576 | 105 | 508 | – | – | – | 613 |
| Derivative financial instruments | 2 | 2 | 2 | – | – | – | – | 2 |
| Trade payables | 455 | 455 | 455 | – | – | – | – | 455 |
| Other payables and accruals | 164 | 164 | 165 | – | – | – | – | 165 |
| | | | 743 | 538 | 394 | 247 | 1,351 | 3,273 |
| Liquidity surplus (gap) | | | 525 | (493) | (393) | (242) | (1,350) | (1,953) |

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 31. Financial instruments continued

**(b) Liquidity risk** continued

***Derivative financial instruments with maturity profile***

The following tables indicate the different types of derivative financial instruments for the 2017 and 2016 financial years that are included within the various categories on the balance sheet. The reported maturity analysis is calculated on an undiscounted basis.

| (US$ million) | Total | Fair value hedge | Cash flow hedge | No hedge accounting | Maturity analysis Undiscounted cash flows 0 – 6 months | 6 – 12 months | 1 – 2 years | 2 – 5 years | >5 years |
|---|---|---|---|---|---|---|---|---|---|
| **September 2017** | | | | | | | | | |
| **Assets** | | | | | | | | | |
| Fair value of derivatives by risk factor | | | | | | | | | |
| ***Interest rate risk*** | | | | | | | | | |
| Interest rate swaps | **–** | **–** | **–** | **–** | – | – | – | – | – |
| receiving leg | **5** | **–** | **5** | **–** | 3 | 2 | – | – | – |
| paying leg | **(5)** | **–** | **(5)** | **–** | (3) | (2) | – | – | – |
| ***Foreign exchange risk*** | | | | | | | | | |
| IRCS and FX forward contracts | **2** | **–** | **–** | **2** | 1 | 1 | – | – | – |
| receiving leg | **150** | **–** | **–** | **150** | 161 | (11) | – | – | – |
| paying leg | **(148)** | **–** | **–** | **(148)** | (160) | 12 | – | – | – |
| Commodity price risk | **1** | **–** | **–** | **1** | 1 | – | – | – | – |
| **Liabilities** | | | | | | | | | |
| Fair value of derivatives by risk factor | | | | | | | | | |
| ***Foreign exchange risk*** | | | | | | | | | |
| IRCS and FX forward contracts | **5** | **–** | **–** | **5** | 5 | – | – | – | – |
| receiving leg | **134** | **–** | **–** | **134** | 134 | – | – | – | – |
| paying leg | **(129)** | **–** | **–** | **(129)** | (129) | – | – | – | – |

## 31. Financial instruments continued

**(b) Liquidity risk** continued

***Derivative financial instruments with maturity profile*** continued

| (US$ million) | Total | Fair value hedge | Cash flow hedge | No hedge accounting | Maturity analysis Undiscounted cash flows 0 – 6 months | 6 – 12 months | 1 – 2 years | 2 – 5 years | >5 years |
|---|---|---|---|---|---|---|---|---|---|
| **September 2016** | | | | | | | | | |
| **Assets** | | | | | | | | | |
| Fair value of derivatives by risk factor | | | | | | | | | |
| ***Interest rate risk*** | | | | | | | | | |
| Interest rate swaps | 1 | – | 1 | – | – | 1 | 1 | 1 | – |
| receiving leg | 10 | – | 10 | – | 3 | 3 | 6 | 5 | – |
| paying leg | (9) | – | (9) | – | (3) | (2) | (5) | (4) | – |
| ***Foreign exchange risk*** | | | | | | | | | |
| IRCS and FX forward contracts | 44 | – | 38 | 6 | 7 | 47 | – | – | – |
| receiving leg | 344 | – | 421 | (77) | (62) | 297 | – | – | – |
| paying leg | (300) | – | (383) | 83 | 69 | (250) | – | – | – |
| **Liabilities** | | | | | | | | | |
| Fair value of derivatives by risk factor | | | | | | | | | |
| ***Foreign exchange risk*** | | | | | | | | | |
| IRCS and FX forward contracts | 1 | – | – | 1 | 1 | – | – | – | – |
| receiving leg | 39 | – | – | 39 | 41 | 52 | – | – | – |
| paying leg | (38) | – | – | (38) | (40) | (52) | – | – | – |
| Commodity price risk | 1 | – | – | 1 | 1 | – | – | – | – |

***Fair values***

The group's financial instruments are initially recognised 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.

The contingent consideration is based on a multiple of targeted future earnings of which a 92% weighted average outcome has been projected.

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.

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 31. **Financial instruments** continued

**(b) Liquidity risk** continued

***Fair values*** continued

| (US$ million) | As determined by IAS 39 | | | Categories in accordance with IAS 39 | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Total balance** | Total out of scope | Total in scope | Fair value through profit or loss | Loans and receivables | Held to maturity | Available for sale | Fair value |
| **September 2017** | | | | | | | | |
| ***Non-current assets*** | | | | | | | | |
| Other non-current assets | **51** | 42 | 9 | – | 2 | – | 7 | 9 |
| | **51** | 42 | 9 | – | 2 | – | 7 | 9 |
| ***Current assets*** | | | | | | | | |
| Trade receivables | **571** | – | 571 | – | 571 | – | – | 571 |
| Prepayments and other receivables | **97** | 65 | 32 | – | 32 | – | – | 32 |
| Derivative financial instruments | **3** | – | 3 | 3 | – | – | – | 3 |
| Cash and cash equivalents | **550** | – | 550 | – | 550 | – | – | 550 |
| | **1,221** | 65 | 1,156 | 3 | 1,153 | – | – | 1,156 |

| (US$ million) | As determined by IAS 39 | | | Categories in accordance with IAS 39 | | |
|---|---|---|---|---|---|---|
| | **Total balance** | Total out of scope | Total in scope | Fair value through profit or loss | Other financial liabilities | Fair value |
| **September 2017** | | | | | | |
| ***Non-current liabilities*** | | | | | | |
| Interest-bearing borrowings | **1,739** | – | 1,739 | – | 1,739 | 1,871 |
| Other non-current liabilities | **423** | 422 | 1 | – | 1 | 1 |
| | **2,162** | 422 | 1,740 | – | 1,740 | 1,872 |
| ***Current liabilities*** | | | | | | |
| Interest-bearing borrowings | **133** | – | 133 | – | 133 | 133 |
| Derivative financial instruments | **5** | – | 5 | 5 | – | 5 |
| Trade payables | **502** | – | 502 | – | 502 | 502 |
| Other payables and accruals | **356** | 199 | 157 | – | 157 | 157 |
| | **996** | 199 | 797 | 5 | 792 | 797 |

## 31. **Financial instruments** continued

**(b) Liquidity risk** continued

***Fair values*** continued

| (US$ million) | As determined by IAS 39 | | | Categories in accordance with IAS 39 | | | | |
|---|---|---|---|---|---|---|---|---|
| | Total balance | Total out of scope | Total in scope | Fair value through profit or loss | Loans and receiv-ables | Held to maturity | Available for sale | Fair value |
| **September 2016** | | | | | | | | |
| ***Non-current assets*** | | | | | | | | |
| Other non-current assets | 39 | 29 | 10 | – | 3 | – | 7 | 10 |
| Derivative financial instruments | 1 | – | 1 | 1 | – | – | – | 1 |
| | 40 | 29 | 11 | 1 | 3 | – | 7 | 11 |
| ***Current assets*** | | | | | | | | |
| Trade receivables | 517 | – | 517 | – | 517 | – | – | 517 |
| Prepayments and other receivables | 125 | 86 | 39 | – | 39 | – | – | 39 |
| Derivative financial instruments | 44 | – | 44 | 44 | – | – | – | 44 |
| Cash and cash equivalents | 703 | – | 703 | – | 703 | – | – | 703 |
| | 1,389 | 86 | 1,303 | 44 | 1,259 | – | – | 1,303 |

| (US$ million) | As determined by IAS 39 | | | Categories in accordance with IAS 39 | | |
|---|---|---|---|---|---|---|
| | Total balance | Total out of scope | Total in scope | Fair value through profit or loss | Other financial liabilities | Fair value |
| **September 2016** | | | | | | |
| ***Non-current liabilities*** | | | | | | |
| Interest-bearing borrowings | 1,535 | – | 1,535 | – | 1,535 | 1,632 |
| Other non-current liabilities | 518 | 517 | 1 | – | – | 1 |
| | 2,053 | 517 | 1,536 | – | 1,535 | 1,633 |
| ***Current liabilities*** | | | | | | |
| Interest-bearing borrowings | 576 | – | 576 | – | 576 | 576 |
| Derivative financial instruments | 2 | – | 2 | 2 | – | 2 |
| Trade payables | 455 | – | 455 | – | 455 | 455 |
| Other payables and accruals | 384 | 220 | 164 | – | 164 | 164 |
| | 1,417 | 220 | 1,197 | 2 | 1,195 | 1,197 |

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 31. Financial instruments continued

**(b) Liquidity risk** continued

***Fair values*** 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.

| (US$ million) | **2017** Total fair value | **2017** Fair value hierarchy Level 1 | Level 2 | Level 3 | 2016 Total fair value | 2016 Fair value hierarchy Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|---|---|---|---|
| ***Non-current assets*** | | | | | | | | |
| Other non-current assets | **7** | **7** | **–** | **–** | 7 | 7 | – | – |
| Derivative financial instruments | **–** | **–** | **–** | **–** | 1 | – | 1 | – |
| | **7** | **7** | **–** | **–** | 8 | 7 | 1 | – |
| ***Current assets*** | | | | | | | | |
| Derivative financial instruments | **3** | **–** | **3** | **–** | 44 | – | 44 | – |
| | **3** | **–** | **3** | **–** | 44 | – | 44 | – |
| ***Non-current liabilities*** | | | | | | | | |
| Interest-bearing borrowings | | | | | | | | |
| Derivative financial instruments | **–** | **–** | **–** | **–** | – | – | – | – |
| Contingent consideration liability | **11** | **–** | **–** | **11** | – | – | – | – |
| | **11** | **–** | **–** | **11** | – | – | – | – |
| ***Current liabilities*** | | | | | | | | |
| Contingent consideration liability | **2** | **–** | **–** | **2** | – | – | – | – |
| Derivative financial instruments | **5** | **–** | **5** | **–** | 2 | – | 2 | – |
| | **7** | **–** | **5** | **2** | 2 | – | 2 | – |

**(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, 70% 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 17.

## 32. Related-party transactions

Transactions between group companies, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

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

| | Sales of goods | | Purchases of goods | | Amounts owed by related parties | | Amounts owed to related parties | |
|---|---|---|---|---|---|---|---|---|
| (US$ million) | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 |
| – proNARO GmbH | **–** | – | **117.3** | 125.8 | **–** | – | **–** | 1.2 |
| – Umkomaas Lignin Proprietary Limited | **5.2** | 4.8 | **–** | 0.1 | **0.7** | 0.5 | **–** | – |
| – Papierholz Austria GmbH | **–** | – | **82.9** | 82.5 | **–** | – | **5.0** | 4.8 |
| – The Boldt Company | **–** | – | **8.0** | – | **–** | – | **–** | – |
| | **5.2** | 4.8 | **208.2** | 208.4 | **0.7** | 0.5 | **5.0** | 6.0 |

The amounts outstanding at balance sheet date are unsecured and will be settled in cash. Guarantees given by the group are disclosed in note 27. No expense has been recognised in the period for bad or doubtful debts in respect of the amounts owed by related parties.

### Broad-based Black Economic Empowerment (BBBEE) transaction

Refer to notes 18 and 29 for details of the BBBEE transaction.

### Key management personnel

Key management personnel include our executive directors and prescribed officers. The total key management personnel emoluments amounted to US$8.5 million (2016: US$7.7 million). The details of key management personnel, including emoluments, interests in contracts and participation in the Sappi Limited share schemes are disclosed in notes 34 to 36.

### Shareholders

| Ordinary shares in issue | Number of shareholders | % | Number of shares[1] | % of shares in issue |
|---|---|---|---|---|
| 1 – 5,000 | 5,566 | 81.5 | 3,093,227 | 0.6 |
| 5,001 – 10,000 | 223 | 3.3 | 1,678,002 | 0.3 |
| 10,001 – 50,000 | 446 | 6.5 | 11,258,624 | 2.1 |
| 50,001 – 100,000 | 190 | 2.8 | 13,865,237 | 2.6 |
| 100,001 – 1,000,000 | 324 | 4.7 | 103,771,633 | 19.4 |
| Over 1,000,000 | 83 | 1.2 | 401,353,472 | 75.0 |
| | 6,832 | 100.0 | 535,020,195 | 100.0 |

[1] *The number of shares excludes 22,182,378 treasury shares held by the group.*

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 32. Related-party transactions continued

**Shareholder spread**

| Type of shareholder | % of shares in issue |
|---|---|
| Non-public | 0.3 |
| Sappi Limited directors and prescribed officers | 0.3 |
| Associates of group directors | – |
| Trustees of the company's share and retirement funding schemes | – |
| Share owners who, by virtue of any agreement, have the right to nominate board members | – |
| Share owners interested in 10% or more of the issued shares | – |
| Public (the number of public shareholders as at September 2017 was 6,821) | 99.7 |
| | 100.0 |

Sappi has a primary listing on the JSE Limited and a Level 1 ADR programme that trades in the over-the-counter market in the United States.

A large number of shares are held by nominee companies for beneficial shareholders. Pursuant to section 56(7) of the Companies Act 71 of 2008 of South Africa, the directors have investigated the beneficial ownership of shares in Sappi Limited, including those which are registered in the nominee holdings. These investigations revealed as of September 2017, the following are beneficial holders of more than 5% of the issued share capital of Sappi Limited:

| Beneficial holder | Shares | % |
|---|---|---|
| Public Investment Corporation | 82,034,389 | 15.3 |

Further, as a result of these investigations, the directors have ascertained that some of the shares registered in the names of the nominee holders are managed by various fund managers and that, as of September 2017, the following fund managers were responsible for managing 5% or more of the share capital of Sappi Limited:

| Fund manager | Shares | % |
|---|---|---|
| Public Investment Corporation | 74,737,258 | 14.0 |
| Prudential Investment Managers | 51,813,987 | 9.7 |
| BlackRock Inc | 32,311,957 | 6.0 |
| Old Mutual Plc | 28,814,593 | 5.4 |
| STANLIB Asset Management | 27,225,483 | 5.1 |

## 33. Events after balance sheet date

The directors declared a gross dividend of 15 US cents per share, payable in ZAR at an exchange rate of US$1 = ZAR14.37037 being ZAR215.55555 cents per share on 16 November 2017. See note 8 for further details.

On 05 December 2017, Sappi agreed to acquire the speciality paper business of Cham Paper Group Holding AG (CPG) for CHF146.5 million (approximately US$149 million). The transaction includes all brands and know-how, the Carmignano and Condino Mills in Italy, as well as their digital imaging business and facility situated in Cham, Switzerland. The acquisition will be financed from internal resources. We are working to obtain approval from the relevant competition authorities and trust that we can announce completion during the first calendar quarter 2018.

Other than the non-adjusting events as described above, there have been no reportable events that occurred between financial year-end and the date of authorisation for issue of these financial statements.

## 34. Directors' and prescribed officers' remuneration

### Non-executive directors

Directors are normally remunerated in the currency of the country in which they live or work from. Their remuneration is translated into US Dollar, the group's reporting currency, at the average exchange rate prevailing during the financial year. Directors' fees are established in local currencies to reflect market conditions in those countries.

Non-executive directors' fees reflect their services as directors and services on various sub-committees on which they serve. The quantum of committee fees depends on whether the director is an ordinary member or a chairman of the committee. Non-executive directors do not earn attendance fees; however, additional fees are paid for attendance at board meetings in excess of the five scheduled meetings per annum.

The Chairman of the Sappi Limited board receives a flat director's fee and does not earn committee fees.

Non-executive directors do not participate in any incentive schemes or plans of any kind.

In determining the fees for non-executive directors, due consideration is given to the fee practice of companies of similar size and complexity in the countries in which the directors are based.

The extreme volatility of currencies, in particular the Rand/US Dollar exchange rate in the past few years, caused distortions of the relative fees in US Dollar paid to individual directors.

Non-executive directors' fees are proposed by the Executive Committee, agreed by the Compensation Committee, recommended by the board and approved at the Annual General Meeting by the shareholders.

| | 2017 | | | |
|---|---|---|---|---|
| (US$) | Board fees | Committee fees | Travel allowance | Total |
| D Konar | 35,200 | 43,811 | 7,000 | 86,011 |
| B Radebe[1] | 15,156 | 3,969 | – | 19,125 |
| KR Osar | 79,360 | 41,800 | 10,500 | 131,660 |
| JD McKenzie | 49,751 | 19,053 | 7,000 | 75,804 |
| ANR Rudd | 395,427 | – | 14,000 | 409,427 |
| NP Mageza | 35,200 | 24,750 | 7,000 | 66,950 |
| R Thummer[2] | 78,745 | 27,781 | 14,000 | 120,526 |
| MV Moosa | 35,200 | 18,305 | 7,000 | 60,505 |
| MA Fallon | 67,177 | 62,446 | 14,000 | 143,623 |
| GPF Beurskens[1] | 27,384 | 22,570 | – | 49,954 |
| RJ DeKoch | 79,360 | 23,920 | 7,000 | 110,280 |
| RJAM Renders | 78,745 | 53,070 | 14,000 | 145,815 |
| B Mehlomakulu[3] | 20,043 | 5,557 | 7,000 | 32,600 |
| | 996,748 | 347,032 | 108,500 | 1,452,280 |

[1] *Retired from the board at the end of February 2017.*
[2] *Will retire from the board at the end of December 2017.*
[3] *Appointed to the board on 01 March 2017.*

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 34. Directors' and prescribed officers' remuneration continued

**Non-executive directors** continued

| | 2016 | | | |
|---|---|---|---|---|
| (US$) | Board fees | Committee fees | Travel allowance | Total |
| D Konar | 25,031 | 47,228 | 10,200 | 82,459 |
| B Radebe | 25,031 | 8,132 | 3,400 | 36,563 |
| KR Osar | 64,840 | 65,640 | 17,000 | 147,480 |
| JD McKenzie | 32,277 | 19,387 | 10,200 | 61,864 |
| DC Cronje[4] | 71,480 | – | – | 71,480 |
| ANR Rudd | 286,549 | 26,495 | 6,800 | 319,844 |
| NP Mageza | 25,031 | 21,128 | 10,200 | 56,359 |
| R Thummer | 65,603 | 27,722 | 6,800 | 100,125 |
| MV Moosa | 25,031 | 12,504 | 10,200 | 47,735 |
| MA Fallon | 61,973 | 64,373 | 6,800 | 133,146 |
| GPF Beurskens | 65,603 | 67,761 | 3,400 | 136,764 |
| RJ DeKoch | 64,840 | 23,455 | 13,600 | 101,895 |
| RJAM Renders | 65,603 | 16,047 | 6,800 | 88,450 |
| | 878,892 | 399,872 | 105,400 | 1,384,164 |

[4] *Retired as independent Chairman of the board at the end of February 2016.*

**Executive directors**

Our pay policy is to pay our executive directors a compensation package which is fair and equitable in comparison to their peers in the markets in which they live and work. They are generally paid in the currency of that country.

| | **2017** | | | | |
|---|---|---|---|---|---|
| (US$) | **Salary** | **Performance-related remuneration** | **Sums paid by way of expense allowance** | **Contributions paid under pension and medical aid schemes** | **Total** |
| SR Binnie[1] | **464,563** | **440,139** | **12,944** | **76,580** | **994,226** |
| GT Pearce[2] | **302,683** | **283,986** | **8,295** | **61,090** | **656,054** |
| | **767,246** | **724,125** | **21,239** | **137,670** | **1,650,280** |

[1] *SR Binnie received a 7.0% increase on the South African portion, followed during the year with a further 20.3% (70% of total salary), and a 1% increase on the off-shore portion of his salary, followed during the year with a further 20.3% (30% of total salary).*
[2] *GT Pearce received a 6.5% increase on the South African portion (70% of total salary), and a 1% increase on the off-shore portion of his salary (30% of total salary).*

| | 2016 | | | | |
|---|---|---|---|---|---|
| (US$) | Salary | Performance-related remuneration | Sums paid by way of expense allowance | Contributions paid under pension and medical aid schemes | Total |
| SR Binnie | 386,767 | 438,082 | 12,050 | 91,638 | 928,537 |
| GT Pearce | 269,960 | 300,613 | 8,249 | 69,630 | 648,452 |
| | 656,727 | 738,695 | 20,299 | 161,268 | 1,576,989 |

The remuneration figures shown above are affected by the translation into US Dollar.

Please see the compensation report in the Annual Integrated Report for further information.

## 34. Directors' and prescribed officers' remuneration continued

**Executive directors** continued

***Details of directors' service contracts***

The executive directors have service contracts with notice periods of 12 months or less. These notice periods are in line with international norms for executive directors.

None of the non-executive directors have service contracts with the company.

None of the directors have provisions for predetermined compensation on termination of their contracts exceeding 12 months' gross remuneration and benefits-in-kind.

**Prescribed officers**

As with our executive directors, our pay policy is to pay our prescribed officers a compensation package which is fair and equitable in comparison to their peers in the markets in which they live and work. They are generally paid in the currency of that country.

| (US$) | Salary | Bonuses and performance-related payments | Sums paid by way of expense allowance | Contributions paid under pension and medical aid schemes | Total |
|---|---|---|---|---|---|
| Prescribed officers remuneration – 2017 | **2,432,293** | **1,587,125** | **37,965** | **528,381** | **4,585,764** |
| Prescribed officers remuneration – 2016 | 2,280,020 | 1,846,458 | 37,734 | 517,276 | 4,681,488 |

# Notes to the Group Annual Financial Statements
continued

for the year ended September 2017

## 35. Directors' and prescribed officers' interests

The following table sets out each director's and prescribed officer's interests in shares and other securities in Sappi Limited. For the purposes of this table, each director's and prescribed officer's interests include shares that are owned either directly or indirectly as well as those shares in which directors and prescribed officers have vested obligations to purchase or to repay loans in terms of the Sappi Limited Share Incentive Trust.

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Direct interests** | **Indirect interests** | Direct interests | Indirect interests |
| Director | **Beneficial** | **Beneficial** | Beneficial | Beneficial |
| **Non-executive directors** | | | | |
| R Thummer | **–** | **–** | 7,542 | – |
| MV Moosa | **–** | **576,542** | – | 576,542 |
| MA Fallon | **5,000** | **–** | 5,000 | – |
| **Executive directors** | | | | |
| SR Binnie | **97,522** | **–** | 40,022 | – |
| GT Pearce | **49,412** | **–** | 30,162 | – |
| **Prescribed officers** | **842,295** | **–** | 562,823 | – |
| | **994,229** | **576,542** | 645,549 | 576,542 |

Subsequent to year-end and as per our SENS announcements to the date of this report, the directors and prescribed officers have acquired a net 2,745 Sappi shares.

## 36. Directors' and prescribed officers' participation in the Sappi Limited share schemes

**Changes in executive directors' and prescribed officers' share options and performance shares before financial year-end**

***Executive directors***

| | SR Binnie | | GT Pearce | | Executive directors | | Prescribed officers | |
|---|---|---|---|---|---|---|---|---|
| | Allocated price | Number of shares | Allocated price | Number of shares | **Total 2017 Number of shares** | Total 2016 Number of shares | **Total 2017 Number of shares** | Total 2016 Number of shares |
| **Outstanding at beginning of year** | | | | | | | | |
| Number of shares held | | 775,000 | | 243,000 | **1,018,000** | 800,100 | **2,261,713** | 2,166,464 |
| 'A' Ordinary shares | | – | | – | **–** | – | **18,213** | 18,213 |
| Share Option 32 – R52,57 | | – | | – | **–** | 6,600 | **–** | 7,700 |
| Performance shares 337 | | – | | – | **–** | 55,500 | **–** | 457,051 |
| Performance shares 38 | | 100,000 | | 35,000 | **135,000** | 135,000 | **498,500** | 498,500 |
| Performance shares 39 | | 310,000 | | 33,000 | **343,000** | 343,000 | **720,000** | 720,000 |
| Performance shares 40 | | 175,000 | | 85,000 | **260,000** | 260,000 | **465,000** | 465,000 |
| Performance shares 41 | | 190,000 | | 90,000 | **280,000** | – | **560,000** | – |
| **Offered and accepted during the year** | | | | | | | | |
| Performance shares 41 | | | | | | 280,000 | | 560,000 |
| Performance shares 42 | | 162,000 | | 75,000 | **237,000** | | **475,000** | |
| **Vested during the year** | | | | | | | | |
| Number of shares | | (100,000) | | (35,000) | **(135,000)** | (34,350) | **(498,500)** | (236,226) |
| **Returned, lapsed and forfeited during the year** | | | | | | | | |
| Number of shares | | – | | – | **–** | (27,750) | **–** | (228,525) |
| **Outstanding at end of year** | | | | | | | | |
| Number of shares | | 837,000 | | 283,000 | **1,120,000** | 1,018,000 | **2,238,213** | 2,261,713 |
| 'A' Ordinary shares | | – | | – | **–** | – | **18,213** | 18,213 |
| Performance shares 38 | | – | | – | **–** | 135,000 | **–** | 498,500 |
| Performance shares 39 | | 310,000 | | 33,000 | **343,000** | 343,000 | **720,000** | 720,000 |
| Performance shares 40 | | 175,000 | | 85,000 | **260,000** | 260,000 | **465,000** | 465,000 |
| Performance shares 41 | | 190,000 | | 90,000 | **280,000** | 280,000 | **560,000** | 560,000 |
| Performance shares 42 | | 162,000 | | 75,000 | **237,000** | – | **475,000** | – |

Performance shares are issued for ZARnil and vest after four years subject to performance criteria being achieved. Plan share issue 38 vested at ZAR82.06. The 'A' ordinary shares are issued for Nil and vesting conditions are described in note 28.

The total IFRS 2 charge in respect of key management personnel amounted to US$2.3 million (2016: US$1.5 million).

Vesting dates

| | |
|---|---|
| Performance shares 39 | 13 December 2017 |
| Performance shares 40 | 04 December 2018 |
| Performance shares 41 | 07 December 2019 |
| Performance shares 42 | 09 December 2020 |
| 'A' ordinary shares | 28 August 2019 |

# Notes to the Group Annual Financial Statements
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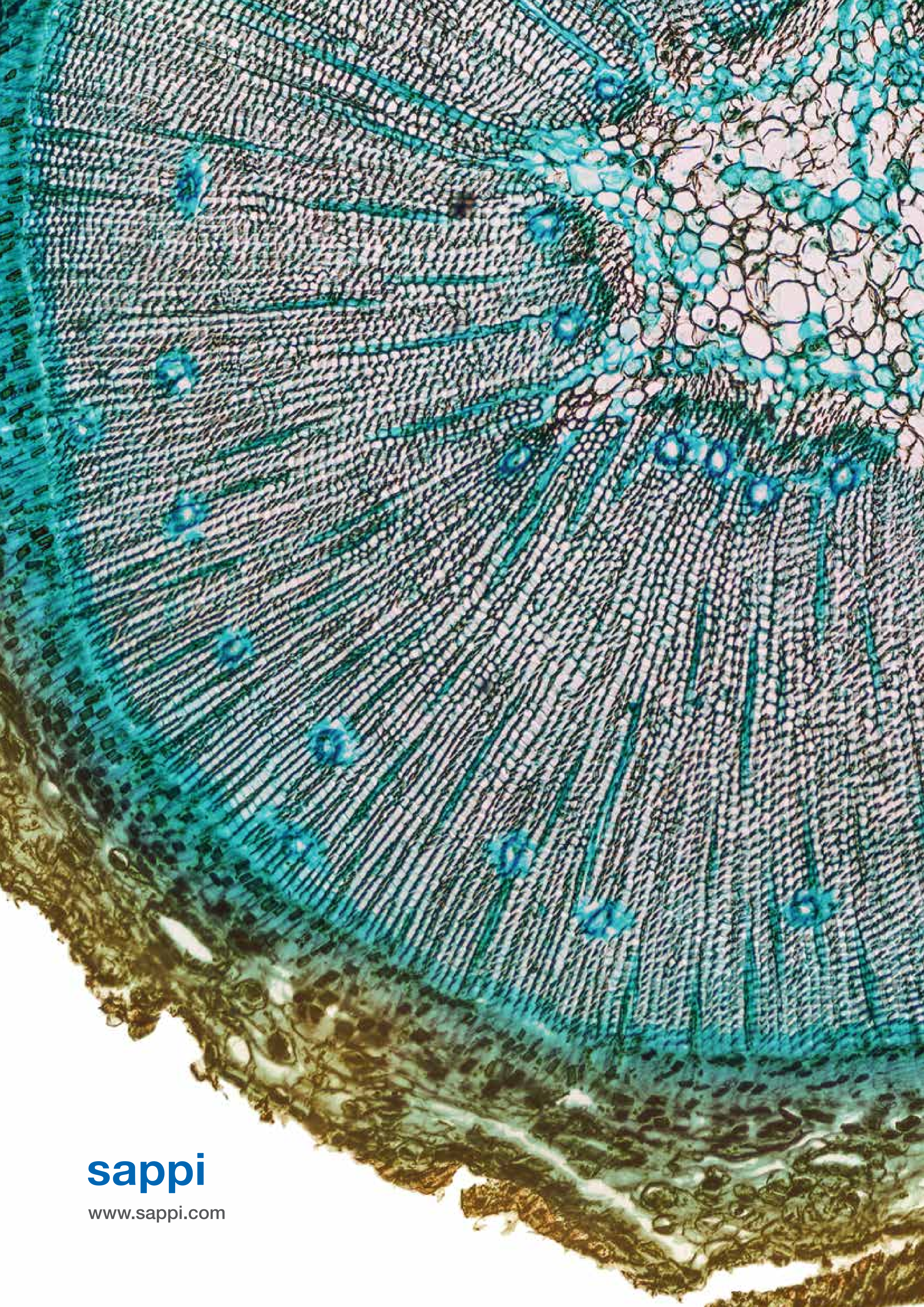
for the year ended September 2017

## 37. Investments

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

| Name of subsidiary | Country of incorporation | Principal activity | Effective holding (%) 2017 | Effective holding (%) 2016 |
|---|---|---|---|---|
| Elektra Purchase Nº 29 Limited | Ireland | Securitisation of receivables | – | – |
| Sappi Alfeld GmbH | Germany | Manufacture of paper and paper pulp | **100** | 100 |
| Sappi Austria Produktions GmbH and CoKG | Austria | Manufacture of paper and paper pulp | **100** | 100 |
| Sappi Cloquet LLC | United States of America | Manufacture of paper, paper pulp and dissolving wood pulp/ paper pulp | **100** | 100 |
| Sappi Deutschland GmbH | Germany | Sales | **100** | 100 |
| Sappi Ehingen GmbH | Germany | Manufacture of paper and paper pulp | **100** | 100 |
| Sappi Europe SA | Belgium | Sales | **100** | 100 |
| Sappi Finland Operations Oy and Sappi Finland I Oy | Finland | Manufacture of paper and paper pulp | **100** | 100 |
| Sappi International Holdings Proprietary Limited | South Africa | Treasury | **100** | 100 |
| Sappi International SA | Belgium | Treasury | **100** | 100 |
| Sappi Lanaken NV | Belgium | Manufacture of paper | **100** | 100 |
| Sappi Lanaken Press Paper NV | Belgium | Manufacture of paper and paper pulp | **100** | 100 |
| Sappi Maastricht BV | The Netherlands | Manufacture of paper | **100** | 100 |
| Sappi Papier Holding GmbH | Austria | Holding company/sales | **100** | 100 |
| Sappi Southern Africa Limited | South Africa | Production of paper and paper pulp, dissolving wood pulp and forestry | **100** | 100 |
| Sappi Stockstadt GmbH | Germany | Manufacture of paper and paper pulp | **100** | 100 |
| Sappisure Försäkrings AB | Sweden | Insurance | **100** | 100 |
| SD Warren Company | United States of America | Manufacture of paper and paper pulp | **100** | 100 |



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