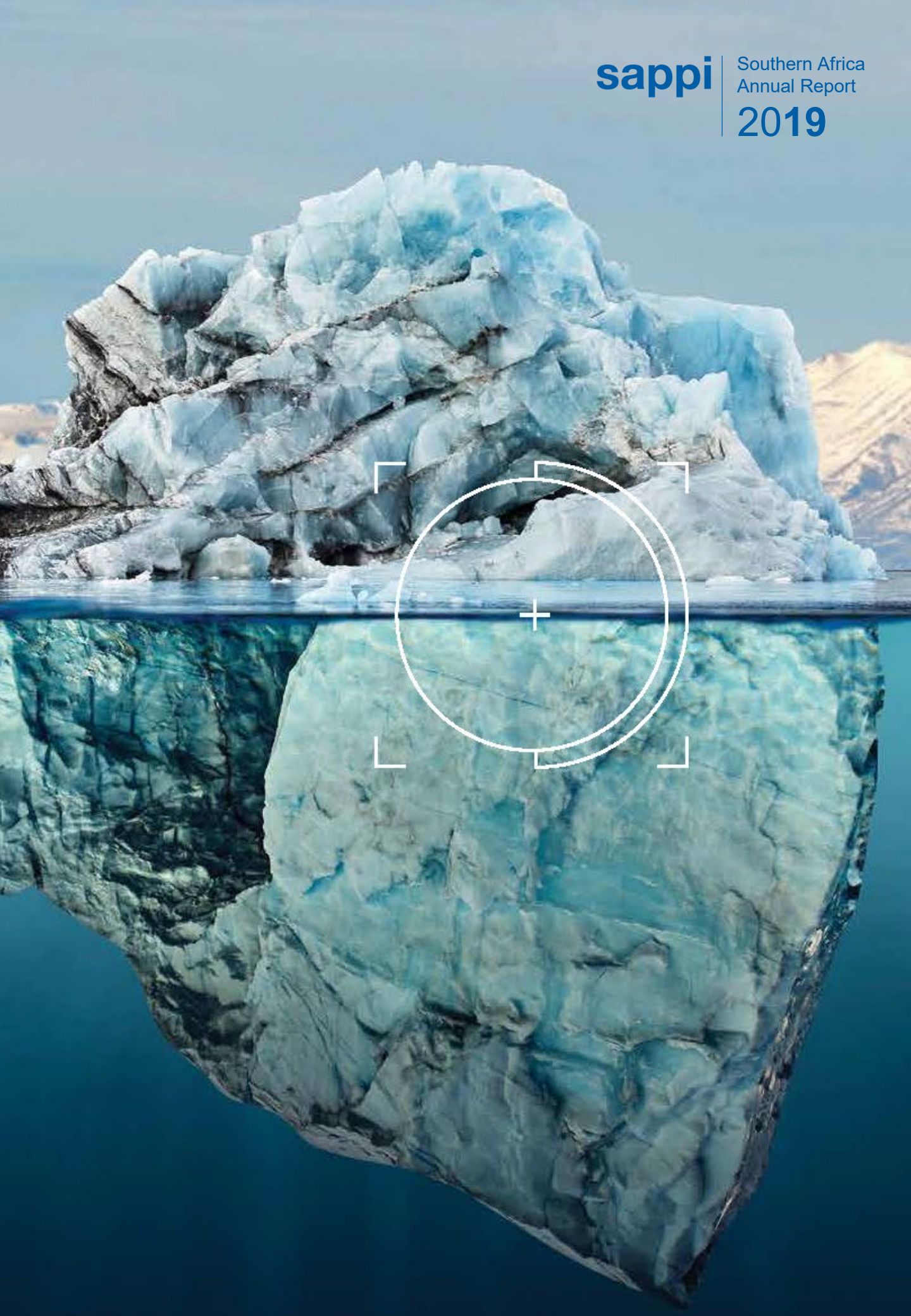
sappi

Southern Africa Annual Report 2019



Sappi Southern Africa Limited

(Incorporated in the Republic of South Africa)
(Registration Number: 1951/003180/06)

Group and company annual financial statements

for the year ended September 2019

Audited

Sappi Southern Africa Limited

(Registration Number: 1951/003180/06)

Group and company annual financial statements

for the year ended September 2019

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Group and company annual financial statements
for the year ended September 2019 (continued)

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The audited financial statements for the year ended September 2019 have been prepared by the corporate accounting staff of Sappi Limited headed by John Shaw, Group Financial Manager. This process was supervised by Pramy Moodley, Chief Financial Officer.

The financial statements have been audited in compliance with Section 30 of the Companies Act of South Africa.

Sappi Southern Africa Limited

Directors' approval

for the year ended September 2019

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

The directors acknowledge that they are ultimately responsible for the system of internal financial control established and are committed to maintaining a strong control environment. The directors are of the opinion that the system of internal control provides reasonable assurance that the financial records may be relied on for the preparation of the group and company 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 and company's budget and cash flow forecasts. This review, together with the group and company's financial position, existing borrowing facilities and cash on hand, have satisfied the directors that the group and company will continue as a going concern for the foreseeable future. The group and company, therefore, continue to adopt the going concern basis in the preparation of the group and company financial statements.

Approval of the group and company annual financial statements

The directors' report, group and company annual financial statements appear on pages 13 to 104 and were approved by the board of directors on 28 January 2020 and signed on its behalf by:

A Thiel
Chief Executive Officer
Authorised Director

P Moodley
Chief Financial Officer
Authorised Director

Group and 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 2019, all such returns as are required of a public company in terms of this Act and that such returns appear to be true, correct and up to date.

Sappi Limited
Secretaries

Per A Mahendranath
Group Company Secretary

28 January 2020

Sappi Southern Africa Limited

Directors' report

for the year ended September 2019

The directors submit their report for the year ended September 2019.

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

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

Sappi Southern Africa overview

The Sappi Group is one of the world's largest manufacturer of DWP and exports almost all of the 1 055 000 tons produced by Sappi Southern Africa at the Saiccor and Ngodwana Mills. DWP is a highly purified form of cellulose extracted from sustainably grown and responsibly managed trees using unique cellulose chemistry technology. When converted to viscose staple fibre (VSF), DWP is a natural substitute in many applications for cotton and polyester and this is used in the manufacture of a wide range of consumer products, including in textiles for fashion clothing and household linen. DWP can also be processed into products used in food and beverages, health and hygiene products, wrapping and packaging, pharmaceuticals and many more applications that touch our daily lives.

The South African paper business produces 690 000 tons of kraft linerboard, corrugating medium, newsprint, office paper and tissue paper which are largely sold regionally, where we have strong market positions in most of these products. We supply the agricultural sector with carton board to protect fresh produce as it is shipped from farms to tables locally and around the world. We also produce 530 000 tons of paper pulp and collect 135 000 tons of recycled waste paper. On a net basis we are approximately self-sufficient for our pulp requirements.

Sappi Southern Africa owns or leases 394,000 hectares (ha) with approximately 28 million tons of standing timber and 135,000 ha being used for other purposes such as conservation. Contracted supply covers almost 138,800 ha. Of the 241,000 ha planted at the end of FY2019, 60% was hardwood and 40% softwood, and of contracted supply, 93% is hardwood. These plantations provide approximately 59% of the wood requirements for the Southern Africa mills. Our aim is to produce low-cost wood with the required pulping characteristics and increase yield per hectare. We actively pursue this aim, particularly through genetic improvement of planting stock.

Markets and operations

Demand for DWP used in textiles, particularly for viscose and lyocell fibres, is both the largest and fastest growing sector. Based on the growth rate in the overall textile market, driven by factors such as population growth, rising urbanisation and a shift towards environmentally friendly natural fibres, we expect long term growth in demand of approximately 6% per annum for DWP.

Sappi Southern Africa's sales volumes in 2019 increased year on year by 5% mainly due to growth in DWP following the successful debottlenecking projects at Saiccor and Ngodwana Mill. Packaging and speciality volumes decreased due to lower demand in the local citrus market and the weak South African economy impacted other paper sales volumes.

The US Dollar spot prices for DWP decreased year on year by approximately 32% to the current level of US$638/ton. Market prices are influenced by VSF and other smaller textile dynamics as well as general macro-economic uncertainties pertaining to the ongoing US/China trade dispute and subsequent US$/RMB exchange rate fluctuations.

Sappi Southern Africa Limited

Directors' report

for the year ended September 2019 (continued)

Markets and operations *(continued)*

Sappi Southern Africa's sales for 2019 in ZAR terms increased year on year, ZAR19 836 million compared to 2018 (ZAR17 867 million). The average rate of the ZAR weakened by 10% to the US Dollar for the year, resulting in price increases in local currency. Variable cost per ton increased by 12% mainly due to increased wood and purchased pulp cost. Variable cost was also impacted by a ZAR20m charge for carbon tax which was introduced in the fourth fiscal quarter. Fixed costs were mainly impacted by above inflationary wage increases at 7% and the employment of additional personnel in anticipation of the increased capacity planned for Saiccor in 2020.

The net result of the above is an increase in ZAR annual operating profit of ZAR3 434 million (ZAR2 962 million in 2018).

We regard ownership of our plantations as a key strategic resource which gives us access to low cost fibre for our pulp production and ensures continuity of an important raw material input source. As we manage our plantations on a sustainable basis, the growth in plantations over the year was largely offset by fellings in the year. A positive fair value price adjustment of ZAR270 million was recorded in fiscal 2019 due mainly to the rolling forward of the higher average fair value rates offset by higher fuel and contractor costs.

We continued our efforts to improve safety across all our operations in South Africa. We remain committed to Project Zero with improved personal behaviour and making safe choices and continuous leadership engagement. Regrettably, we had four contractor fatalities during the year Our target is zero injuries and we believe we can achieve this with enhanced procedures, training, behaviour and entrenching a strong safety culture.

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

Going concern

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

Events after balance sheet date

Refer to note 22 – Contingent Liabilities and note 30 - Events after balance sheet date.

Outlook

Due to the current weak pricing in the DWP market and with paper markets impacted by the slowing South African economy, we expect EBITDA for financial year 2020 to be below that of 2019. The markets we operate in are expected to continue to be challenging in the coming year DWP pricing in particular will have a significant impact on earnings as this segment is a major contributor to our profits and cash flow generation. DWP pricing remains under significant pressure, having declined to an historic low. However underlying demand for DWP is still growing at rates consistent with our long-term forecasts. A recovery in DWP prices is likely to be prompted by a recovery in VSF prices which have been depressed by excess VSF capacity and a weak Chinese textile market.

The year ahead remains a challenge and we have reacted by reducing capital expenditure other than committed projects, reducing working capital and targeting cost reduction across the business.

Sappi Southern Africa Limited

Directors' report

for the year ended September 2019 (continued)

Reporting period

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

Share capital

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

Authorised

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

Issued

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

Financing

At year end, the average tenure of the company's debt is 2.9 years.

Sappi Southern Africa Limited currently has the following credit ratings:

– Global Credit Rating (GCR): South African national rating AA(za)/A1+ (za)/stable outlook (November 2019).

Net borrowings

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

Insurance

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

Asset insurance is renewed on a calendar year basis. The self-insured retention portion for any one property damage occurrence is EUR21 million with the annual aggregate set at EUR33 million. The self-insured retention is managed through the Sappi Captive insurer, SappiSure for property damage and business interruption insurance, cost-effective cover to full value is not readily available. A loss limit cover of EUR730 million, based on the maximum foreseeable loss, has been deemed to be adequate for the reasonable foreseeable loss for any single claim. In addition to the Property damage and business interruption policies there is a full program of policies to mitigate the losses stemming from events not covered by the main global policy.

During 2019, no incidents occurred that exceeded the Captive retention and resulted in a successful claim against the group and company's property damage or business interruption insurance policies.

Fixed assets

Capital expenditure of ZAR3 239 million was incurred during the year as per the cash flow statement. We successfully completed the Woodyard upgrade during the course of the year. Capital expenditure increased slightly in 2019 as we proceeded with the 110kt capacity increase of Dissolving Wood Pulp.

Litigation

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

Corporate Governance

Sappi is committed to high standards of Corporate Governance which form the foundation for long term sustainability of our Company and the creation of value for our stakeholders. Good governance at Sappi contributes to living our values through enhanced accountability, a transparent and ethical culture, strong risk management, a focus on performance, legitimacy and effective control of the business.

Sappi endorses the corporate outcomes of ethical cultures, good performance, effective control and legitimacy promoted by the King IV Report on Corporate Governance for South Africa (released November 2019).

Sappi Southern Africa Limited

Directors' report

for the year ended September 2019 (continued)

Audit and risk committee

The Sappi Southern Africa Limited group of companies (Group) is a major subsidiary of Sappi Limited (Sappi), a company that maintains its listing on the JSE Limited. Sappi complies in all material respects with the JSE listings requirements, regulations and codes. The Sappi Southern Africa Limited Audit Committee operates as a function of the Sappi Limited Audit Committee. The committee, in terms of the Companies Act of South Africa, and King code has the responsibility for reviewing the effectiveness of the group and company's system of internal controls and risk management system. An internal audit function is responsible for advising the Board of Directors on the effectiveness of the group and company's risk management system. For further information on Sappi's application of the King Code please refer to the Sappi Ltd 2019 Integrated Annual Report.

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

Company secretary

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

Subsidiary companies

Details of the company's significant subsidiaries are given in note 31.

Registered office

108 Oxford Road
Houghton Estate
2198

Secretaries

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South Africa
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Telefax +27 (0) 11 339 1881
e-Mail Ami.Mahendranath@sappi.com

Sappi Southern Africa Limited

Directors' report

for the year ended September 2019 (continued)

Auditors

KPMG Inc.

Holding company

Sappi Limited

Directors

Steven Binnie *Chief Executive Officer* *Sappi Limited* *and* *Executive Director* *Sappi Southern Africa Limited*	**Qualifications:** Bcom, B Acc, CA(SA), MBA **Nationality:** British **Appointed:** 1 September 2012 **Skills and experience:** Mr Binnie was appointed Chief Executive Officer of Sappi Limited in July 2014 and is and Executive Director of Sappi Southern Africa Limited. He brings extensive experience in financial management, leadership, corporate activity and strategy to the role.
Glen Pearce *Chief Financial Officer* *Sappi Limited* *and* *Executive Director* *Sappi Southern Africa Limited*	**Qualifications:** BCom, BCom (Hons), CA(SA) **Nationality:** South African **Appointed:** 1 July 2014 **Skills and experience:** Mr Pearce joined Sappi Limited in June 1997 and was promoted to Chief Financial Officer and executive director of Sappi Limited in July 2014. He was also appointed as Executive Director of Sappi Southern Africa Limited at the same time. Mr Pearce has extensive financial management experience, both locally and abroad.
Alex Thiel *Chief Executive Officer* *Sappi Southern Africa Limited*	**Qualifications:** BSc (Mechanical Engineering), MBA (Financial Management and Information Technology) **Nationality:** South African **Appointed:** 1 December 2010 **Skills and experience:** Mr Thiel joined Sappi in December 1989 and was appointed Chief Executive Officer of Sappi Southern Africa Limited in December 2010. His experience and expertise includes marketing, logistics, procurement, strategy and operations across Europe and Southern Africa. .
Pramy Moodley *Chief Financial Officer* *Sappi Southern Africa Limited*	**Qualifications:** B Acc, CA(SA) **Nationality:** South African **Appointed:** 1 January 2017 **Skills and experience:** Ms Moodley joined Sappi Southern Africa Limited in June 2002 and subsequently held various finance roles before being promoted to Chief Financial Officer and executive director of Sappi Southern Africa Ltd in January 2017.

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85 Empire Road, Parktown, 2193,
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Independent Auditor's Report

To the shareholders of Sappi Southern Africa Limited

Report on the audit of the consolidated and separate financial statements

Opinion

We have audited the consolidated and separate financial statements of Sappi Southern Africa Limited (the group and company) set out on pages 13 to 104, which comprise the group and company balance sheets as at September 2019, and the group and company income statements, group and company statements of comprehensive income, the group and company statements of changes in equity and the group and company statements of cash flows for the year then ended, and notes to the group and company financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated and separate financial statements present fairly, in all material respects, the consolidated and separate financial position of Sappi Southern Africa Limited as at September 2019, and its consolidated and separate financial performance and consolidated and separate cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the Companies Act of South Africa.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated and separate financial statements* section of our report. We are independent of the group and company in accordance with the sections 290 and 291 of the Independent Regulatory Board for Auditors' *Code of Professional Conduct for Registered Auditors (Revised January 2018),* parts 1 and 3 of the Independent Regulatory Board for Auditors' *Code of Professional Conduct for Registered Auditors (Revised November 2018)* (together the IRBA Codes) and other independence requirements applicable to performing audits of financial statements in South Africa. We have fulfilled our other ethical responsibilities, as applicable, in accordance with the IRBA Codes and in accordance with other ethical requirements applicable to performing audits in South Africa. The IRBA Codes are consistent with the corresponding sections of the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* and the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* respectively. 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 and separate financial statements of the current period. These matters were addressed in the context of our audit of the consolidated and separate financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

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

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

Registration number 1999/021543/21

Chairman Wiseman Nkuhlu

Chief Executive Officer Ignatius Sehoole

Directors Full list on website

The company's principal place of business is at KPMG Crescent, 85 Empire Road, Parktown.

KPMG

Valuation of plantations Refer to note 2.3.4 for the accounting policies applied and note 7 to the group and company financial statements	
Key audit matter	How the matter was addressed in our audit
Plantations are valued in terms of IAS 41, *Agriculture* (IAS 41) and are stated at fair value less cost to sell at the harvesting stage, using the income approach, and is a level 3 measure in terms of IFRS 13, *Fair Value Measurement (IFRS 13)*. The valuation of plantations requires complex measurements and involves estimation uncertainty. The key inputs and assumptions involving significant estimation, judgement and having the most significant impact on the fair value of the plantations are: • Volume and growth estimations (standing tons); and Discount rate. Given the complexity and the significant amount of estimation and judgement involved in the determination of fair value of the plantations, this matter was considered a key audit matter in our audit of the group and company.	Our audit procedures related to the valuation of plantations included: • Critically evaluating the fair value methodology, key measurements and assumptions applied by management in determining the fair value of the plantations against the criteria in terms of IAS 41 and IFRS 13. This was performed by the audit team, by applying their knowledge of the industry to assess the appropriateness of the valuations. • Challenging the consistency and appropriateness of the underlying measurements and assumptions used by comparing to external observable data, where possible, and considering management's historical accuracy in determining these measurements and estimations. • Assessing the reasonableness of the group's fair value estimates, and the related sensitivity disclosures, by performing our own sensitivity analysis of the plantation valuations. • We considered the adequacy and appropriateness of the group and company's disclosures in respect of the valuation of plantations in accordance with IAS 41 and IFRS 13.

Other information

The directors are responsible for the other information. The other information comprises the information included in the document titled "Sappi Southern Africa Limited Group and company annual financial statements for the year ended September 2019", which includes the Directors' Report and the Group and company secretary's certificate as required by the Companies Act of South Africa. The other information does not include the consolidated and separate financial statements and our auditor's report thereon.

Our opinion on the consolidated and separate 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 and separate 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 and separate financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors for the consolidated and separate financial statements

The directors are responsible for the preparation and fair presentation of the consolidated and separate 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 and separate financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated and separate financial statements, the directors are responsible for assessing the group and company'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 and/or company or to cease operations, or have no realistic alternative but to do so.

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

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

KPMG

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

- Identify and assess the risks of material misstatement of the consolidated and separate 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 and company'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 director's 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 and company'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 and separate 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 and/or company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated and separate financial statements, including the disclosures, and whether the consolidated and separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- 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 and separate financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements
In terms of the IRBA Rule published in Government Gazette Number 39475 dated 4 December 2015, we report that KPMG Inc. has been the auditor of Sappi Southern Africa Limited for three years.

KPMG Inc.

Per Safeera Loonat
Chartered Accountant (SA)
Registered Auditor
Director
28 January 2020

Sappi Southern Africa Limited

Group and company income statements

for the year ended September 2019

		Group		Company	
		2019	2018	**2019**	2018
	Note	**ZAR'millions**	ZAR'millions	**ZAR'millions**	ZAR'millions
Revenue		**19 836**	17 867	**19 836**	17 867
Cost of sales	*3.1*	**15 522**	14 040	**15 521**	14 040
Gross profit		**4 314**	3 827	**4 315**	3 827
Selling, general and administrative expenses	*3.1*	**705**	578	**705**	703
Equity accounted investee, profits	*9*	**(46)**	(44)	**(46)**	(44)
Dividends received		**–**	–	**(156)**	(211)
Operating profit	*3*	**3 655**	3 293	**3 812**	3 379
Net finance (income)/costs	*4*	**113**	(85)	**113**	(85)
Finance costs		**150**	128	**150**	128
Finance income		**(68)**	(180)	**(68)**	(180)
Net foreign exchange losses/ (gains)		**31**	(33)	**31**	(33)
Profit before taxation		**3 542**	3 378	**3 699**	3 464
Taxation charge	*5*	**1 008**	1 202	**1 008**	1 172
Profit for the year		**2 534**	2 176	**2 691**	2 292

Sappi Southern Africa Limited

Group and company statements of comprehensive income

for the year ended September 2019

		Group		Company	
		2019	2018	**2019**	2018
	Note	**ZAR'millions**	ZAR'millions	**ZAR'millions**	ZAR'millions
Profit for the year		**2 534**	2 176	**2 691**	2 292
Other comprehensive (loss)/ income, net of tax	*14*	**(182)**	102	**(182)**	102
Items that will not be reclassified subsequently to profit or loss	*14*	**(103)**	14	**(103)**	14
Actuarial (losses)/gains on post-employment benefit funds		**(143)**	19	**(143)**	19
Tax on above item		**40**	(5)	**40**	(5)
Items that may be reclassified subsequently to profit or loss	*14*	**(79)**	88	**(79)**	88
Movement in hedging reserves		**(130)**	122	**(130)**	122
Tax on above item		**51**	(34)	**51**	(34)
Total comprehensive income for the year		**2 352**	2 278	**2 509**	2 394

Sappi Southern Africa Limited

Group and company balance sheets

as at September 2019

		Group		Company	
		2019	2018	**2019**	2018
	Note	**ZAR'millions**	ZAR'millions	**ZAR'millions**	ZAR'millions
Assets					
Non-current assets		**28 432**	24 660	**28 431**	24 659
Property, plant and equipment	*6*	**15 565**	13 080	**15 571**	13 086
Plantations	*7*	**6 830**	6 595	**6 830**	6 595
Equity accounted investee	*9*	**158**	161	**158**	161
Other non-current assets	*10*	**329**	393	**322**	386
Amounts owing by related parties	*28*	**5 550**	4 377	**5 550**	4 377
Derivative financial instruments	*26*	**–**	54	**–**	54
Current assets		**6 930**	5 913	**6 930**	5 913
Inventories	*11*	**2 083**	2 011	**2 083**	2 011
Trade and other receivables	*12*	**645**	610	**645**	610
Derivative financial instruments	*26*	**24**	123	**24**	123
Amounts owing by related parties	*28*	**2 335**	2 155	**2 335**	2 155
Cash and cash equivalents		**1 843**	1 014	**1 843**	1 014
Total assets		**35 362**	30 573	**35 361**	30 572
Equity and liabilities					
Shareholders' equity		**23 449**	21 096	**23 447**	20 937
Ordinary share capital and share premium	*13*	**221**	221	**221**	221
Non-distributable reserves	*15*	**158**	157	**156**	155
Hedging reserves		**(37)**	93	**(36)**	94
Retained earnings		**23 107**	20 625	**23 106**	20 467
Non-current liabilities		**5 970**	5 395	**5 970**	5 395
Interest-bearing borrowings	*17*	**1 498**	1 145	**1 498**	1 145
Derivative financial instruments	*26*	**32**	–	**32**	–
Deferred tax liabilities	*8*	**4 149**	3 979	**4 149**	3 979
Other non-current liabilities	*18*	**291**	271	**291**	271
Current liabilities		**5 943**	4 082	**5 944**	4 240
Interest-bearing borrowings	*17*	**1 144**	–	**1 144**	–
Trade and other payables	*26*	**33**	80	**33**	80
Trade and other payables	*16*	**4 251**	3 675	**4 251**	3 674
Taxation payable	*19.4*	**362**	109	**362**	109
Amounts owing to related parties	*28*	**153**	218	**154**	377
Total equity and liabilities		**35 362**	30 573	**35 361**	30 572

Sappi Southern Africa Limited

Group and company statements of cash flows

for the year ended September 2019

	Note	Group 2019 ZAR'millions	Group 2018 ZAR'millions	Company 2019 ZAR'millions	Company 2018 ZAR'millions
Cash retained from operating activities		**3 744**	2 745	**3 743**	2 757
Cash generated from operations	*19.1*	**4 343**	3 688	**4 342**	3 672
– increase in working capital	*19.2*	**(79)**	(293)	**(79)**	(296)
Cash generated from operating activities		**4 264**	3 395	**4 263**	3 376
– Finance costs paid	*19.3*	**(93)**	(79)	**(93)**	(79)
– Finance income received		**68**	178	**68**	178
– Taxation paid	*19.4*	**(494)**	(750)	**(494)**	(719)
Cash utilised in investing activities		**(4 412)**	(4 154)	**(4 411)**	(4 166)
Investment to maintain operations		**(2 121)**	(1 327)	**(2 121)**	(1 326)
Investment to expand operations		**(1 118)**	(1 935)	**(1 118)**	(1 935)
Proceeds on disposal of property, plant and equipment	*19.5*	**25**	144	**25**	13
Increase in amounts owing by related parties		**(1 183)**	(1 066)	**(1 338)**	(1 160)
Dividends received		**–**	–	**156**	211
Other decrease in non-current assets		**(15)**	30	**(15)**	31
Cash effects of financing activities		**1 497**	(500)	**1 497**	(500)
Repayment of interest-bearing borrowings	*19.6*	**(3)**	(500)	**(3)**	(500)
Increase in interest-bearing borrowings		**1 500**	–	**1 500**	–
Net movement in cash and cash equivalents		**829**	(1 909)	**829**	(1 909)
Cash and cash equivalents at beginning of year		**1 014**	2 923	**1 014**	2 923
Cash and cash equivalents at end of year		**1 843**	1 014	**1 843**	1 014

Sappi Southern Africa Limited

Group and company statements of changes in equity

for the year ended September 2019

Group	*Note*	Ordinary share capital ZAR'millions	Share premium ZAR'millions	Ordinary share capital and share premium ZAR'millions	Non-distributable reserves ZAR'millions	Hedging reserves ZAR'millions	Retained earnings ZAR'millions	Total equity ZAR'millions
Balance at 30 September 2017		12	209	221	152	5	18 435	18 813
Share-based payments		–	–	–	50	–	–	50
Sappi Limited Share Incentive Trust		–	–	–	(45)	–	–	(45)
Profit for the year		–	–	–	–	–	2 176	2 176
Other comprehensive income		–	–	–	–	88	14	102
Balance at 30 September 2018	*13*	12	209	221	157	93	20 625	21 096
IFRS 9 adoption	*2.4.1*	**–**	**–**	**–**	**–**	**(51)**	**51**	**–**
Share-based payments		**–**	**–**	**–**	**41**	**–**	**–**	**41**
Sappi Limited Share Incentive Trust		**–**	**–**	**–**	**(40)**	**–**	**–**	**(40)**
Profit for the year		**–**	**–**	**–**	**–**	**–**	**2 534**	**2 534**
Other comprehensive loss	*14*	**–**	**–**	**–**	**–**	**(79)**	**(103)**	**(182)**
Balance at September 2019		**12**	**209**	**221**	**158**	**(37)**	**23 107**	**23 449**

Sappi Southern Africa Limited

Group and company statements of changes in equity

for the year ended September 2019

Company	*Note*	Ordinary share capital ZAR'millions	Share premium ZAR'millions	Ordinary share capital and share premium ZAR'millions	Non-distributable reserves ZAR'millions	Hedging reserves ZAR'millions	Retained earnings ZAR'millions	Total equity ZAR'millions
Balance at 30 September 2017		12	209	221	150	6	18 161	18 538
Share-based payments		–	–	–	50	–	–	50
Sappi Limited Share Incentive Trust		–	–	–	(45)	–	–	(45)
Profit for the year		–	–	–	–	–	2 292	2 292
Other comprehensive income		–	–	–	–	88	14	102
Balance at 30 September 2018	*13*	12	209	221	155	94	20 467	20 937
IFRS 9 adoption		**–**	**–**	**–**	**–**	**(51)**	**51**	**–**
Share-based payments		**–**	**–**	**–**	**41**	**–**	**–**	**41**
Sappi Limited Share Incentive Trust		**–**	**–**	**–**	**(40)**	**–**	**–**	**(40)**
Profit for the year		**–**	**–**	**–**	**–**	**–**	**2 691**	**2 691**
Other comprehensive loss	*14*	**–**	**–**	**–**	**–**	**(79)**	**(103)**	**(182)**
Balance at September 2019		**12**	**209**	**221**	**156**	**(36)**	**23 106**	**23 447**

Sappi Southern Africa Limited

Notes to the group and company financial statements

for the year ended September 2019

1. Basis of preparation

The group and company financial statements of Sappi Southern Africa Limited (the 'Company') as at and for the year ended September 2019 comprise the company and its subsidiaries (together referred to as the 'Group' and individually as 'Group entities' or 'Group entity') as well as the group's interests in joint ventures.

The group and company annual financial statements were approved by the board of directors on 28 January 2020.

The group and company financial statements (the group and company Annual Financial Statements) have been prepared in accordance with:

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

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

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

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

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

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

The preparation of the group and company Annual Financial Statements was supervised by P Moodley CA(SA).

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

- 1 October 2018 to 29 September 2019 (52 weeks)
- 2 October 2017 to 30 September 2018 (52 weeks)

The group and company Annual Financial Statements are prepared on the going concern basis.

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

2. Accounting policies

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

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

2.1 Significant accounting policy elections

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

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

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

2.2 Summary of accounting policies

2.2.1 Foreign currencies

Transactions and balances
Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the 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.

2.2.2 Group and company accounting

(i) Subsidiaries

An entity is consolidated when the group and company 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 and company's results from acquisition date until disposal date.

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

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.2 Group and company accounting *(continued)*

(ii) Equity accounted investee

The financial results of the joint ventures are incorporated in the group and company'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 and company'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 or company, from their unaudited management accounts that correspond to the group and company'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 and company 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 (in the current year IFRS 9 has been adopted, refer to note 2.4 for the policy of adoption for this standard).

Policy applicable after 1 October 2018

(i) Initial recognition

Financial instruments are recognised on the balance sheet when the group and company 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

A financial asset (unless it is a trade receivable without a significant financing component) or a financial liability is initially measured at fair value plus, for an item not at fair value through profit or loss (FVTPL), transaction costs that are directly attributable to its acquisition or issue. A trade receivable without a significant financing component is initially measured at the transaction price.

(iii) Classification and subsequent measurement

Financial assets

On initial recognition, a financial asset is classified and measured at: amortised cost, fair value through other comprehensive income (FVOCI) - debt investment, FVOCI - equity instrument or FVTPL. Financial assets are not reclassified subsequent to their initial recognition unless the group and company changes its business model for managing financial assets, in which case all affected financial assets are reclassified on the first day of the first reporting period following the change in the business model. A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.3 Financial instruments (in the current year IFRS 9 has been adopted, refer to note 2.4 for the policy of adoption for this standard) *(continued)*

Policy applicable after 1 October 2018 *(continued)*

(iii) Classification and subsequent measurement (continued)

A debt investment is measured at FVOCI if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the group and company may irrevocably elect to present subsequent changes in the investment's fair value in OCI. This election is made on an investment-by-investment basis.

All financial assets not classified as measured at amortised cost or FVOCI as described above are measured at FVTPL. This includes all derivative financial assets. On initial recognition, the group and company may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Financial assets – Business model assessment

The group and company makes an assessment of the objective of the business model in which a financial asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. These include whether management's strategy focuses on earning contractual interest income, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of any related liabilities or expected cash outflows or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the group and company's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales of financial assets in prior periods, the reasons for such sales and expectations about future sales activity.

The group and company's business model is to hold financial assets to collect contractual cash flows.

Transfers of financial assets to third parties in transactions that do not qualify for derecognition are not considered sales for this purpose, consistent with the group and company's continuing recognition of the assets. Financial assets that are held for trading or are managed and whose performance is evaluated on a fair value basis are measured at FVTPL.

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.3 Financial instruments (in the current year IFRS 9 has been adopted, refer to note 2.4 for the policy of adoption for this standard) *(continued)*

Policy applicable after 1 October 2018 *(continued)*

(iii) Classification and subsequent measurement (continued)

Financial assets – Assessment whether contractual cash flows are solely payments of principal interest

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the group and company considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making this assessment, the group and company considers:

- contingent events that would change the amount or timing of cash flows;
- terms that may adjust the contractual coupon rate, including variable-rate features;
- prepayment and extension features; and
- terms that limit the group and company's claim to cash flows from specified assets (e.g. non-recourse features).

A prepayment feature is consistent with the solely payments of principal and interest criterion if the prepayment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable additional compensation for early termination of the contract. Additionally, for a financial asset acquired at a discount or premium to its contractual par-amount, a feature that permits or requires prepayment at an amount that substantially represents the contractual par amount plus accrued (but unpaid) contractual interest (which may also include reasonable additional compensation for early termination) is treated as consistent with this criterion if the fair value of the prepayment feature is insignificant at initial recognition.

Financial assets – subsequent measurement and gains and losses

– Financial assets at FVTPL

These assets are subsequently measured at fair value. Net gains and losses, including any interest or dividend income, are recognised in profit or loss.

– Financial assets at amortised cost

These assets are subsequently measured at amortised cost using the effective interest method. The amortised cost is reduced by impairment losses. Interest income, foreign exchange gains and losses and impairment are recognised in profit or loss. Any gain or loss on derecognition is recognised in profit or loss.

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.3 Financial instruments (in the current year IFRS 9 has been adopted, refer to note 2.4 for the policy of adoption for this standard) *(continued)*

Policy applicable after 1 October 2018 *(continued)*

(iii) Classification and subsequent measurement (continued)

Financial assets – subsequent measurement and gains and losses *(continued)*

– Debt investments at FVOCI

These assets are subsequently measured at fair value. Interest income calculated using the effective interest method, foreign exchange gains and losses and impairment are recognised in profit or loss. Other net gains and losses are recognised in OCI. On derecognition, gains and losses accumulated in OCI are reclassified to profit or loss.

– Equity investments at FVOCI

These assets are subsequently measured at fair value. Dividends are recognised as income in profit or loss unless the dividend clearly represents a recovery of part of the cost of the investment. Other net gains and losses are recognised in OCI and are never reclassified to profit or loss.

Financial liabilities

Financial liabilities are classified as measured at amortised cost or FVTPL. A financial liability is classified as at FVTPL if it is classified as held-for-trading, it is a derivative or it is designated as such on initial recognition. Financial liabilities at FVTPL are measured at fair value and net gains and losses, including any interest expense, are recognised in profit or loss. Other financial liabilities are subsequently measured at amortised cost using the effective interest method. Interest expense and foreign exchange gains and losses are recognised in profit or loss. Any gain or loss on derecognition is also recognised in profit or loss.

Policy applicable prior to 1 October 2018

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

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

– Financial liabilities at amortised cost

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

– Loans and receivables

Loans and receivables were carried at amortised cost.

– Available-for-sale financial assets

Available-for-sale financial assets were 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, were recognised in profit or loss.

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.3 Financial instruments (in the current year IFRS 9 has been adopted, refer to note 2.4 for the policy of adoption for this standard) *(continued)*

Policy applicable prior to 1 October 2018 *(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 and company derecognises a financial asset when the rights to receive cash flows from the financial asset have expired or have been transferred and the group and company has transferred substantially all risks and rewards of ownership of the financial asset.

A financial liability is derecognised when and only when the liability is extinguished, i.e. when the obligation specified in the contract is discharged, cancelled or has expired. The group and company also derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different, in which case a new financial liability based on the modified terms is recognised at fair value. The difference in the respective carrying amounts is recognised in profit or loss for the period.

(vi) Impairment of financial assets

The group and company measures loss allowances at an amount equal to lifetime expected credit losses using a simplified approach. When determining whether the credit risk of a financial asset has increased significantly since initial recognition and when estimating expected credit losses, the group and company considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the group and company's historical experience and informed credit assessment and including forward-looking information. Forward looking information incorporates actual and expected significant changes in the political, regulatory and technological environment of the debtor and its business activities

Impairment losses are calculated taking into account the life time expected credit losses of trade and other receivables. The group and company's trade and other receivables are managed on a collective basis irrespective of the nature of its customers. The group and company does not have a history of significant trade receivables write-offs as the contractual terms entered with the customers help ensure that these balances are recoverable.

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.3 Financial instruments (in the current year IFRS 9 has been adopted, refer to note 2.4 for the policy of adoption for this standard) *(continued)*

(vi) Impairment of financial assets (continued)

Policy applicable after 1 October 2018

The group and company establishes an allowance for impairment that represents its estimate of credit losses in respect of trade and other receivables. The main component of this allowance is a specific loss component that relates to individual significant exposures and a collective loss component in respect of losses that may be incurred but have not yet been identified. The collective loss allowances are determined based on historical write-offs data over the last five years. This takes into account past circumstances which resulted in trade and other receivable balances that were not recovered. Individual significant exposures refer to customers that are under business rescue, in liquidation or unable to pay their obligations. These customers are credit impaired irrespective of their aging. This takes into account forward looking circumstances. Five years is considered to be a reasonable timeframe on which to calculate a loss rate given the nature of the group and company's operations and the contractual terms agreed to with its customers.

Policy applicable prior to 1 October 2018

– Loans and receivables

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

– Available-for-sale financial assets

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

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

(vii) Finance income and finance costs

Finance income and finance costs are recognised in profit or loss using the effective interest 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.

(viii) Offsetting

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the group and company currently has a legally enforceable right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

Policy applicable prior to 1 October 2018 *(continued)*

2.2.4 Intangible assets

(i) Research activities

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

2.2.5 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 inter-changeable	Specific identification inventory valuation basis.

2.2.6 Leases

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 and company's benefit.

2.2.7 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 and company'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. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.8 Revenue (in the current year IFRS 15 has been adopted refer to note 2.4 for the policy of adoption for this standard)

Policy applicable after 1 October 2018

Revenue is recognised when a customer obtains control of the goods. Revenue is recognised at a point in time, with no deferral of revenue. Control of goods passes to the customer when the performance obligations are satisfied. Sappi primarily has one performance obligation, which is the delivery of the goods to the customer. Control is dependent on shipping in terms where goods are sold to customers overseas. Depending on the shipping terms used, shipping and handlings activities may be a separate performance obligation where these activities are performed after revenue is recognised from the sale of the goods. In these instances, revenue is recognised from the shipping and handling activities when these activities are fulfilled, which is at the same time revenue is recognised from the sale of goods. Sappi acts as an agent in the fulfilment of these shipping and handling performance obligations, and as such recognises revenue from this performance obligation net of the costs incurred to fulfil it. When shipping and handling activities are not a separate performance obligation, these costs are included in cost of sales.

Policy applicable prior to 1 October 2018

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 and company's customers’ destinations, are included in cost of sales.

2.2.9 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. Cash and cash equivalents are measured at amortised cost.

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

Policy applicable prior to 1 October 2018 *(continued)*

2.2.10 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 and company as consideration for those equity instruments will be received over the vesting period. These benefits are accounted for in profit or loss as they are received with a corresponding increase in equity. Share-based payment expenses are adjusted to reflect the number of awards for which the related service and non-market performance conditions are expected to be met.

(ii) Measurement of fair value of equity instruments granted

The equity instruments granted by the group and company 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 and company 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 and company'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 and company's share price, employee turnover rate, and dividend pay-out rates.

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

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.11 Derivatives and hedge accounting (in the current year IFRS 9 has been adopted refer to note 2.4 for the policy of adoption for this standard)

Policy applicable after 1 October 2018

Derivatives are initially measured at fair value. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are generally recognised in profit or loss. For the purpose of hedge accounting, hedges are classified as follows:

(i) Fair value hedges

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

(ii) Cash flow hedges

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

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

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

(iii) Discontinuance of hedge accounting

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

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

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

2. Accounting policies *(continued)*

2.2 Summary of accounting policies *(continued)*

2.2.11 Derivatives and hedge accounting (in the current year IFRS 9 has been adopted refer to note 2.4 for the policy of adoption for this standard) *(continued)*

(iii) Discontinuance of hedge accounting (continued)

Policy applicable prior to 1 October 2018

The accounting policy in the comparative information presented for 2018 is similar to that applied for 2019. The only changes as a result of the application of IFRS 9 was that changes in the fair value of the forward element of forward exchange contracts is recorded as a cost of hedging reserve as a separate component of OCI, whereby under IAS 39 it was recognised immediately in profit or loss.

2.2.12 Provisions

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

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

Restructuring provisions are recognised when the group and company 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.

2.2.13 Short-term employee benefits

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

2.2.14 Share capital

Share capital comprises ordinary shares and are classified as equity. Issued ordinary shares are measured at the fair value of the proceeds received less any directly attributable issue costs. An amount equal to the par value of the shares issued is presented as share capital. The amount by which the fair value exceeds par value is presented as share premium. Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity. Income tax relating to transaction costs of an equity transaction is accounted for in accordance with IAS 12. Treasury shares are excluded from equity.

2. Accounting policies *(continued)*

2.3 Critical accounting policies and key sources of estimation uncertainty

2.3.1 Impairment of assets other than goodwill and financial instruments

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

In assessing assets for impairment, the group and company 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 cash-generating unit (CGU) to which the asset belongs. Additionally, assets are also assessed against their fair value less costs of disposal.

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

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

2.3.2 Property, plant and equipment

Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Cost includes, where specifically required in terms of legislative requirements or where a constructive obligation exists, the estimated cost of dismantling and removing the assets, professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the group and company'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.

2. Accounting policies *(continued)*

2.3 Critical accounting policies and key sources of estimation uncertainty *(continued)*

2.3.2 Property, plant and equipment *(continued)*

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

(ii) Deferred taxation

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

2. Accounting policies *(continued)*

2.3 Critical accounting policies and key sources of estimation uncertainty *(continued)*

2.3.3 Taxation *(continued)*

(ii) Deferred taxation (continued)

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 and company intends to settle its current tax assets and liabilities on a net basis.

Before recognising a deferred tax asset, the group and company 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 and company considers profit forecasts, including the effect of exchange rate fluctuations on sales, external market conditions and restructuring plans.

(iii) Dividend withholding tax

Dividend withholding tax is payable on dividends distributed to certain shareholders. This tax is not attributable to the company paying the dividend but is withheld 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 Plantations

Plantations are stated at fair value less costs to sell at the harvesting stage and is a Level 3 measure in terms of the fair value measurement hierarchy as established by IFRS 13 Fair Value Measurement. The group and company 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 inputs are market prices, costs to sell, discount rates, and volume and growth estimations. Of these key inputs, discount rates and the volume and growth estimations are key assumptions that have significant estimation and judgement.

All changes in fair value are recognised in profit or loss in the period in which they arise.

The impact that changes in market prices, costs to sell, discount rates, and volume and growth assumptions may have on the calculated fair value on plantations is disclosed in note 7.

2. Accounting policies *(continued)*

2.3 Critical accounting policies and key sources of estimation uncertainty *(continued)*

2.3.4 Plantations *(continued)*

– Market prices and costs to sell

The fair value is derived by using the prices explained below less costs to sell. Costs to sell includes all costs associated with getting the harvested agricultural produce to the market, including harvesting, loading, transport and allocated fixed overheads. The group and company uses a twelve-quarter rolling historical average fair value to value all immature timber and mature timber which is to be felled more than twelve 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 for reasonability when estimating fair value.

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

– Discount rate

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

– Volume and growth estimations

The group and company focuses on good husbandry techniques which include ensuring that the rotation of plantations is met with adequate planting activities for future harvesting. The age threshold used for quantifying immature timber is dependent on the rotation period of the specific timber genus which varies between 5 and 18 years. In the Southern African region, softwood less than 8 years and hardwood less than 5 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 includes harvesting (fellings) and damages. The fair value of timber felled is determined on the actual method while damages is calculated on the average method. Damages are written off against standing timber to record loss or damage caused by fire, storms, disease and stunted growth. Harvesting (fellings) depletion costs are accounted for as actual tonnes multiplied by the actual fair value. Damages depletion costs are accounted for as actual damaged tonnes multiplied by the actual twelve quarter rolling historical average price. Damaged tonnes are calculated using the projected growth to rotation age and are extrapolated to current age on a straight- line basis.

The group and company has projected growth estimation over a period of 5 to 18 years per rotation. In deriving this estimate, the group and company 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 and company's growth estimation. Periodic adjustments are made to existing models for new genetic material.

The associated costs for managing plantations are recognised as silviculture costs in cost of sales (see note 3.1).

2. Accounting policies *(continued)*

2.3 Critical accounting policies and key sources of estimation uncertainty *(continued)*

2.3.5 Post-employment benefits

Defined benefit and defined contribution plans have been established for eligible employees of the group and company, 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 and company's policy is to recognise actuarial gains or losses, which can arise from differences between expected and actual outcomes or changes in actuarial assumptions, in OCI. Any increase in the present value of plan liabilities expected to arise due to current service costs is charged to profit or loss.

Gains or losses on the curtailment or settlement of a defined benefit plan are recognised in profit or loss when the group and company 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 and company, 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 23 for the key estimates, assumptions and other information on post-employment benefits.

2. Accounting policies *(continued)*

2.4 Adoption of accounting standards in the current year

The group and company adopted IFRS 9 (refer to 2.4.1) and IFRS 15 (refer to 2.4.2) from 1 October 2018. The following standards, interpretations, amendments and improvements to standards were also effective and adopted in the current fiscal year, all of which had no material impact on the group and company's reported results or financial position:

- IFRS 2 – Classification and Measurement of share-based Payment Transactions
- IFRIC 22 – Foreign Currency Transactions and Advance Consideration
- Annual Improvements 2014-2016 Cycle

2.4.1 IFRS 9 Financial instruments

IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement. Additionally, the entity has adopted consequential amendments to IFRS 7 Financial Instruments: Disclosures that are applied to disclosures for 2019, but have not been generally applied to comparative information.

(i) Classification and measurement of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, FVOCI and FVTPL. The classification of financial assets under IFRS 9 is generally based on the business model in which a financial asset is managed and its contractual cash flow characteristics. IFRS 9 eliminates the previous IAS 39 categories of held to maturity, loans and receivables and available for sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never separated. Instead, the hybrid financial instrument as a whole is assessed for classification.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification and measurement of financial liabilities. The adoption of IFRS 9 has not had a significant effect on the group and company’s accounting policies related to financial liabilities and derivative financial instruments. The only adjustment was ZAR51 million that was reclassified from Cash flow hedge reserves to retained income. (refer to derivatives that are used as hedging instruments, see (2.4.1.3)).

2. Accounting policies *(continued)*

2.4 Adoption of accounting standards in the current year *(continued)*

2.4.1 IFRS 9 Financial instruments *(continued)*

(i) Classification and measurement of financial assets and financial liabilities (continued)

The changes in classification and measurement from IAS 39 to IFRS 9 are as follows:

1 October 2018	**Total balance**	**Total in scope**	**Categories in accordance with IAS 39**			**Categories in accordance with IFRS 9**		
	R'millions	**R'millions**	**Fair value through profit or loss R'millions**	**Loans and receivables R'millions**	**Available for sale R'millions**	**Fair value through profit or loss R'millions**	**Amortised cost R'millions**	**Fair value through OCI R'millions**
Non-current assets								
Derivative financial instruments	54	54	54	–	–	54	–	–
Amounts owing by related parties	4 377	4 377	–	4 377	–	–	4 377	–
	4 431	4 431	54	4 377	–	54	4 377	–
Current assets								
Trade and other receivables	610	304	–	304	–	–	304	–
Derivative financial instruments	123	123	123	–	–	123	–	–
Amounts owing by related parties	2 155	2 155		2 155	–	–	2 155	–
Cash and cash equivalents	1 014	1 014	–	1 014	–	–	1 014	–
	3 902	3 596	123	3 473	–	123	3 473	–

2. Accounting policies *(continued)*

2.4 Adoption of accounting standards in the current year *(continued)*

2.4.1 IFRS 9 Financial instruments *(continued)*

(ii) Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' (ECL) model. The new impairment model applies to financial assets measured at amortised cost and debt investments at FVOCI, but not to investments in equity instruments. Under IFRS 9, credit losses are recognised earlier than under IAS 39. The group and company has determined that the application of IFRS 9's impairment requirements at 1 October 2018 results in no significant increase in an impairment allowance.

(iii) Hedge accounting

The group and company has elected to adopt the new general hedge accounting model in IFRS 9. This requires the group and company to ensure that hedge accounting relationships are aligned with its risk management objectives and strategy and to apply a more qualitative and forward-looking approach to assessing hedge effectiveness. The group and company uses forward foreign exchange contracts to hedge the variability in cash flows arising from changes in foreign exchange rates relating to foreign currency borrowings, sales and capital expenditure. The effective portion of changes in fair value of hedging instruments is accumulated in a cash flow hedge reserve as a separate component of equity. Under IAS 39, the change in fair value of the forward element of the forward exchange contracts ('forward points') was recognised immediately in profit or loss. However, under IFRS 9 the forward points are separately accounted for as a cost of hedging; they are recognised in OCI and accumulated in a cost of hedging reserve as a separate component within equity. Under IAS 39, for all cash flow hedges the amounts accumulated in the cash flow hedge reserve were reclassified to profit or loss as a reclassification adjustment in the same period as the hedged expected cash flows affected profit or loss. However, under IFRS 9, for cash flow hedges of foreign currency risk associated with forecast PPE purchases, the amounts accumulated in the cash flow hedge reserve are instead included directly in the initial cost of the PPE item when it is recognised. The same approach also applies under IFRS 9 to the amounts accumulated in the cost of hedging reserve.

2.4.2 IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaced IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations. Under IFRS 15, revenue is recognised when a customer obtains control of the goods or services. Determining the timing of the transfer of control at a point in time or over time requires judgement.

IFRS 15 provides a single, principles based five-step model to be applied to all contracts with customers. The group and company has reviewed the significant customer contracts, and the adoption of IFRS 15 does not have a material impact on the recognition and measurement of revenue when compared to that of the application of IAS18.

2. Accounting policies *(continued)*

2.4 Adoption of accounting standards in the current year *(continued)*

2.4.2 IFRS 15 Revenue from Contracts with Customers *(continued)*

Under IAS 18 Sappi derived revenue from contracts with customers from one revenue stream being the sale of goods. For the majority of local and regional sales, transfer occurred at the point of off-loading the shipment into the customer warehouse whereas for the majority of export sales, transfer occurred when the goods have been loaded into the relevant carrier unless the contract of sale specified different terms.

Revenue was 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 and company's customer destination, were included in cost of sales. Under IFRS 15 revenue is recognised when a customer obtains control of the goods. There has not been a material change in timing of revenue recognition with revenue being recognised at a point in time, with no deferral of revenue. As a result, there has not been an impact in retained earnings on transition to IFRS 15.

The application of IFRS 15 has had the effect on the group and company to the extent that there have been instances where revenue has been recognised prior to the shipping of the goods, where the shipping of the goods is still the responsibility of Sappi. This has created a separate performance obligation, where Sappi is acting as an agent for the fulfilment of the shipping activities. As there is no margin earned on the shipping of the goods, the net revenue recognised for the shipping is nil. This has resulted in revenue been recognised at a lower value net of the shipping costs, and operating expenses also reducing by the corresponding value as a result of the re allocation of the shipping costs from operating costs to sales. Sappi has adopted IFRS 15 using the cumulative effect method without practical expedients applied with the effect of initially applying this standard recognised at the date of initial application (i.e. 1 October 2018). Accordingly, the information presented for 2018 has not been restated.

Additionally, the disclosure requirements in IFRS 15 have not generally been applied to comparative information.

2. Accounting policies *(continued)*

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 and company. The impact of these standards is still being evaluated by the group and company. The effective date denotes the fiscal year end in which it will be adopted.

- IFRS 9 Financial Instruments – Prepayment Features with Negative Compensation – September 2020
- IFRS 16 Leases

Management have substantially completed their assessment of IFRS 16 Leases which it will adopt from its mandatory adoption date of September 2019 being the beginning of the 2020 financial year. IFRS 16 introduces a single on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. The group and company intends to apply the modified retrospective transition approach and will not restate comparative amounts. The group and company expects to recognise right-of-use assets measured at the amount of the lease liability on adoption between the range of ZAR380 million and ZAR400 million. The group and company's leasing activities mainly relate to the lease of premises, vehicles and equipment.

Sappi is planning to elect the following practical expedients as allowed by IFRS 16:

- relying on previous assessments on whether leases are onerous as an alternative to performing an impairment review: there were no onerous contracts as at 29 September 2019
- accounting for operating leases with a remaining lease term of less than 12 months as at the adoption date as short-term leases
- excluding initial direct costs for the measurement of the right-of-use asset at the adoption date
- using hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

The group and company has also elected not to reassess whether a contract is, or contains a lease at the date of initial application. Instead, for contracts entered into before the transition date the group and company relied on its assessment made applying IAS 17 and IFRIC 4 Determining whether an Arrangement contains a Lease.

- IFRIC 23: Uncertainty over Income Tax Treatments – September 2020
- IAS 19: Plan Amendment, Curtailment or Settlement – September 2020
- IAS 28: Long-term Interests in Associates and Joint Ventures September 2020
- IFRS 3: amendment definition of a business – September 2020
- IAS 1 & 8: amendments to the definition of material – September 2020
- Annual Improvements 2015-2017 Cycle: Amendments to IFRS 1 and IAS 28 – September 2020

3. Operating profit

3.1 Cost of sales and selling, general and administration

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

	2019		2018	
	Cost of sales ZAR'millions	**Selling, general and administrative expenses ZAR'millions**	Cost of sales ZAR'millions	Selling, general and administrative expenses ZAR'millions
Group				
Raw materials, energy and other direct input costs	**9 632**	**–**	8 593	–
Plantation price fair value adjustment	**(307)**	**–**	(386)	–
Employment costs	**2 141**	**504**	2 000	466
Depreciation	**1 000**	**28**	839	35
Delivery charges	**990**	**–**	1 062	–
Maintenance	**956**	**–**	924	–
Other overheads	**1 110**	**–**	1 008	–
Marketing and selling expenses	**–**	**21**	–	22
Administrative and general expenses	**–**	**152**	–	55
	15 522	**705**	14 040	578
Company				
Raw materials, energy and other direct input costs	**9 631**	**–**	8 593	–
Plantation price fair value adjustment	**(307)**	**–**	(386)	–
Employment costs	**2 141**	**504**	2 000	466
Depreciation	**1 000**	**28**	839	35
Delivery charges	**990**	**–**	1 062	–
Maintenance	**956**	**–**	924	–
Other overheads	**1 110**	**–**	1 008	131
Marketing and selling expenses	**–**	**21**	–	22
Administrative and general expenses	**–**	**152**	–	49
	15 521	**705**	14 040	703

Sappi Southern Africa Limited

Notes to the group and company financial statements

for the year ended September 2019 (continued)

3. Operating profit *(continued)*

3.1 Cost of sales and selling, general and administration *(continued)*

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Fair value gains on plantations (note 7)				
Changes in volumes				
– Fellings (note 19.1)	**1 017**	861	**1 017**	861
– Growth	**(1 054)**	(895)	**(1 054)**	(895)
	(37)	(34)	**(37)**	(34)
Plantation price fair value adjustment	**(270)**	(352)	**(270)**	(352)
	(307)	(386)	**(307)**	(386)
Silviculture costs (included within cost of sales)	**967**	856	**967**	856
Leasing charges for				
– Premises	**67**	58	**67**	58
– Plant and equipment	**6**	5	**6**	5
– Vehicles	**30**	31	**30**	31
– Office equipment	**27**	25	**27**	25
Cost on derecognition of trade receivables (debtor securitisation costs)	**104**	94	**104**	94
Audit and related services	**12**	12	**12**	12
Research and development costs	**141**	144	**141**	144

3.2 Employee costs

Employment costs consist of	**2 645**	2 466	**2 645**	2 466
Wages and salaries	**1 870**	1 723	**1 870**	1 723
Defined contribution plan expense (refer to note 23)	**156**	140	**156**	140
Defined benefit pension plan expense (refer to note 23)	**59**	68	**59**	68
Other defined benefit subsidy expense (refer to note 24)	**8**	8	**8**	8
Other medical contributions and allowances	**178**	167	**178**	167
Overtime	**151**	138	**151**	138
Share-based payment expense	**39**	36	**39**	36
Other [1]	**184**	186	**184**	186

[1] Mainly consists of training, hired labour, housing costs and catering.

3. Operating profit *(continued)*

3.3 Other expenses/(income)

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
(Profit)/loss on disposal of property, plant and equipment (note 19.5)	**(12)**	(53)	**(12)**	58
Insurance recoveries	**(20)**	(7)	**(20)**	(7)
(Reversals)/impairment of property, plant and equipment	**(108)**	2	**(108)**	2
Broad-based Black Economic Empowerment (BBBEE) charge	**2**	13	**2**	13
Write-off/(reversal) of other assets	**3**	(38)	**3**	(38)

4. Net finance (income)/costs

Interest and other finance costs on liabilities carried at amortised cost	**145**	123	**145**	123
– Interest on bank overdrafts	**4**	3	**4**	3
– Finance costs capitalised (note 6)	**(23)**	–	**(23)**	–
– Interest on redeemable bonds and other loans	**164**	120	**164**	120
Net interest on employee defined benefit liabilities (note 23 and 24)	**5**	5	**5**	5
Finance income received on assets carried at amortised cost	**(68)**	(180)	**(68)**	(180)
– Interest income on cash and cash equivalents	**(68)**	(178)	**(68)**	(177)
– Interest income on other loans and investments	**–**	(2)	**–**	(3)
Net foreign exchange (gains)/losses	**31**	(33)	**31**	(33)
Net finance (income)/costs	**113**	(85)	**113**	(85)

Sappi Southern Africa Limited

Notes to the group and company financial statements

for the year ended September 2019 (continued)

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
5. Taxation charge				
Current taxation	**758**	893	**758**	863
– Current year	**745**	606	**745**	576
– Prior year under provision	**13**	287	**13**	287
Deferred taxation (note 8)	**250**	309	**250**	309
– Current year	**268**	309	**268**	309
– Prior year over provision	**(18)**	–	**(18)**	–
	1 008	1 202	**1 008**	1 172

In addition to income taxation charges to profit and loss, current taxation relief of ZAR10.8 million (2018: ZAR6.7 million charge) and deferred taxation charge/benefit of ZAR80.0 million (2018: ZAR32.8 million charge) has been recognised directly in other comprehensive income (refer note 8).

	Group		Company	
	2019 %	2018 %	**2019 %**	2018 %
Reconciliation of the tax rate				
Statutory tax rate	**28.0**	28.0	**28.0**	28.0
Non-taxable income [1]	**0.6**	(0.9)	**0.6**	(0.8)
Prior year adjustments	**(0.2)**	8.5	**(0.2)**	8.8
Effective taxation rate for the year	**28.4**	35.6	**28.4**	36.0

[1] This mainly includes dividends, special allowances and items of a capital nature.

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
6. Property, plant and equipment				
Land and buildings [1]				
– At cost	**3 060**	3 160	**3 090**	3 190
– Accumulated depreciation and impairments	**(1 042)**	(1 168)	**(1 066)**	(1 192)
	2 018	1 992	**2 024**	1 998
Plant and equipment [2]				
– At cost	**23 148**	21 709	**23 148**	21 709
– Accumulated depreciation and impairments	**(9 601)**	(10 621)	**(9 601)**	(10 621)
	13 547	11 088	**13 547**	11 088

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
6. Property, plant and equipment *(continued)*				
Aggregate cost	**26 208**	24 869	**26 238**	24 899
Aggregate accumulated depreciation and impairments	**(10 643)**	(11 789)	**(10 667)**	(11 813)
Aggregate book value [3]	**15 565**	13 080	**15 571**	13 086

(1) Details of land and buildings are available at the registered offices of the respective companies who own the assets.
(2) Plant and equipment includes vehicles and furniture, the book value of which is immaterial and does not warrant disclosure as a separate class of assets.
(3) Plant and equipment includes an amount of ZAR3 301.9 million (2018: ZAR1 823.7 million) relating to assets under construction.

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

Group	**Land and buildings ZAR'millions**	**Plant and equipment ZAR'millions**	**Total ZAR'millions**
Carrying amount at September 2017	1 999	8 635	10 634
Additions	123	3 309	3 432
Disposals	(24)	(86)	(110)
Depreciation	(104)	(770)	(874)
Impairments (administration building)	(2)	–	(2)
Carrying amount at September 2018	1 992	11 088	13 080
Additions	**218**	**3 287**	**3 505**
Finance costs capitalised (note 4)	**–**	**23**	**23**
Disposals and scrappings	**(78)**	**(45)**	**(123)**
Depreciation	**(114)**	**(914)**	**(1 028)**
Impairments	**–**	**–**	**–**
Impairment reversals (note 3.3)	**–**	**108**	**108**
Net book value at September 2019	**2 018**	**13 547**	**15 565**

6. **Property, plant and equipment** *(continued)*	**Land and buildings ZAR'millions**	**Plant and equipment ZAR'millions**	**Total ZAR'millions**
Company			
Carrying amount at September 2017	1 994	8 635	10 629
Additions	123	3 309	3 432
Disposals	(13)	(86)	(99)
Depreciation	(104)	(770)	(874)
Impairments reversals	(2)	–	(2)
Carrying amount at September 2018	1 998	11 088	13 086
Additions	**218**	**3 287**	**3 505**
Finance costs capitalised (note 4)	**–**	**23**	**23**
Disposals and scrappings	**(77)**	**(45)**	**(122)**
Depreciation	**(114)**	**(914)**	**(1 028)**
Impairments	**(1)**	**–**	**(1)**
Impairment reversals (note 3.3) [1]	**–**	**108**	**108**
Net book value at September 2019	**2 024**	**13 547**	**15 571**

[1] The impairment reversal of ZAR108 million relates to the Tugela mill of ZAR95 million and Stanger mill of ZAR13 million due to an impairment reversal in demand for release paper products and the related impact on profitability (included in Packaging and Specialities segment, note 32). A pre-tax discount rate of 11.8% and a terminal growth rate of 6.8% were used. These amounts are recorded in other operating expenses.

	Group		**Company**	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
7. **Plantations**				
Fair value of plantations at the beginning of the year	**6 595**	6 206	**6 595**	6 206
Additions	**32**	–	**32**	–
Disposals	**–**	(1)	**–**	(1)
Fire, flood, storms and related events	**(58)**	(6)	**(58)**	(6)
In-field inventory	**(46)**	10	**(46)**	10
Gains arising from growth (note 3.1)	**1 054**	895	**1 054**	895
Gain arising from fair value price changes (note 3.1)	**270**	352	**270**	352
Harvesting - agriculture produce (fellings)	**(1 017)**	(861)	**(1 017)**	(861)
Fair value of plantations at end of year	**6 830**	6 595	**6 830**	6 595

7. Plantations *(continued)*

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

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

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

The group and company is exposed to financial risks arising from climatic changes, disease and other natural risks such as fire, flooding a 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 12.35% (2018:11.04%). The group and company currently values approximately 28 million tons (2018:28 million tons) of timber using selling prices and delivery costs that are benchmarked against industry norms. The average annual growth is measured at approximately 18 tons (2018: 16 tons) of timber per hectare while immature timber comprises approximately 107,000 hectares (2018: 107 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 and company has calculated the sensitivity of a change in each of these assumptions as tabled below:

	2019 **ZAR'millions**	2018 ZAR'millions
Market price changes		
1% increase in market prices	**33**	29
1% decrease in market prices	**(33)**	(29)
Discount rate (for immature timber)		
1% increase in rate	**(36)**	(37)
1% decrease in rate	**36**	37

7. **Plantations** *(continued)*	**2019 ZAR'millions**	2018 ZAR'millions
Volume assumption		
1% increase in estimate of volume	**65**	63
1% decrease in estimate of volume	**(65)**	(63)
Costs to sell		
1% increase in costs to sell	**(27)**	(24)
1% decrease in costs to sell	**27**	24
Growth assumptions		
1% increase in rate of growth	**18**	16
1% decrease in rate of growth	**(18)**	(16)

8. **Deferred tax liabilities**	**2019**		2018	
	Assets ZAR'millions	**Liabilities ZAR'millions**	Assets ZAR'millions	Liabilities ZAR'millions
Group				
Other non-current liabilities	**–**	**(36)**	**–**	46
Accrued and other liabilities	**–**	**(127)**	**–**	(139)
Property, plant and equipment	**–**	**2 384**	**–**	2 214
Plantations	**–**	**1 928**	**–**	1 858
	–	**4 149**	**–**	3 979
Company				
Other non-current liabilities	**–**	**(36)**	**–**	46
Accrued and other liabilities	**–**	**(127)**	**–**	(139)
Property, plant and equipment	**–**	**2 384**	**–**	2 214
Plantations	**–**	**1 928**	**–**	1 858
	–	**4 149**	**–**	3 979

	Group		**Company**	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Reconciliation of deferred tax				
Deferred tax balances at beginning of year	**3 979**	3 637	**3 979**	3 637
– Deferred tax assets	**–**	–	**–**	–
– Deferred tax liabilities	**3 979**	3 637	**3 979**	3 637

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
8. Deferred tax liabilities *(continued)*				
Reconciliation of deferred tax *(continued)*				
Deferred tax charge for the year (refer to note 5)	**250**	309	**250**	309
– Other non-current assets	**(2)**	(3)	**(2)**	(3)
– Accrued and other liabilities	**12**	3	**12**	3
– Property, plant and equipment	**170**	204	**170**	204
– Plantations	**70**	105	**70**	105
Amounts recorded directly in other comprehensive income	**(80)**	33	**(80)**	33
Deferred tax balances at end of year	**4 149**	3 979	**4 149**	3 979
– Deferred tax assets	**–**	–	**–**	–
– Deferred tax liabilities	**4 149**	3 979	**4 149**	3 979

9. Equity accounted investee

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 development, production and sale of products based on lignosulphonate in order to build a sustainable lignin business. The financial statements the 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 International Financial Reporting Standards are used to account for joint venture's income to Sappi's year-end.

9. Equity accounted investee *(continued)*

Umkomaas Lignin Proprietary Limited *(continued)*

Carrying amount of equity accounted investee:

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Cost of investment in joint venture	**2**	2	**2**	2
Share of post-acquisition profits	**86**	89	**86**	89
– Opening balance	**89**	122	**89**	122
– Current year profit (note 19.1)	**46**	44	**46**	44
– Additions equity	**–**	–	**–**	–
– Dividend received (note 28)	**(49)**	(77)	**(49)**	(77)
Loan – converted to share capital	**70**	70	**70**	70
Investment in joint venture	**158**	161	**158**	161

Dividends received from joint ventures for the 2019 financial year were ZAR49.2 million (2018: ZAR77.5 million).

Summarised financial information of Umkomaas Lignin Proprietary Limited:

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Balance Sheet summary				
Current assets	**257**	272	**257**	272
Non-current assets	**248**	254	**248**	254
Current liabilities	**(111)**	(100)	**(111)**	(100)
Non-current liabilities	**(79)**	(104)	**(79)**	(104)
The above assets and liabilities include the following:				
Cash and cash equivalents	**40**	72	**40**	72
Current financial liabilities (excluding trade and other payables, and provisions)	**(58)**	(100)	**(58)**	(100)
Non-current financial liabilities (excluding trade and other payables, and provisions)	**(45)**	(104)	**(45)**	(104)

9. Equity accounted investee *(continued)*

Umkomaas Lignin Proprietary Limited *(continued)*

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Income Statement summary				
Sales	**(635)**	(645)	**(635)**	(645)
Depreciation and amortisation	**24**	27	**24**	27
Finance costs	**5**	7	**5**	7
Finance income	**(5)**	(4)	**(5)**	(4)
Taxation charge	**29**	30	**29**	30
Profit from continuing operations	**(93)**	(89)	**(93)**	(89)
Other comprehensive income	**–**	–	**–**	–
Total comprehensive income	**(93)**	(89)	**(93)**	(89)

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

	Group		Company	
	2019	2018	**2019**	2018
Net assets of the joint venture	**315**	322	**315**	322
Proportion of the ownership interest	**50%**	50%	**50%**	50%
Carrying amount of the interest in the joint venture	**158**	161	**158**	161

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
10. Other non-current assets				
Advances to tree growers	**48**	45	**48**	45
Licence fee	**1**	1	**1**	1
Defined benefit pension plan assets (refer to note 23)	**128**	256	**128**	256
Unlisted investment	**21**	15	**15**	15
Investment in Ngodwana energy (refer to note 28)	**23**	23	**23**	23
Shareholder loan (refer to note 28)	**103**	45	**103**	45
Other	**5**	8	**4**	1
	329	393	**322**	386

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
11. Inventories				
Raw materials	**590**	451	**590**	451
Work in progress	**65**	65	**65**	65
Finished goods	**931**	1 102	**931**	1 102
Consumable stores and spares	**497**	393	**497**	393
	2 083	2 011	**2 083**	2 011

The charge to the income statement relating to the write-down of inventories to net realisable value amounted to ZAR27.8 million (2018: ZAR22.2 million).

The cost of inventories recognised as an expense and included in cost of sales amounted to ZAR14 895.7 million (2018: ZAR13 356.2 million).

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
12. Trade and other receivables				
Trade receivable	**169**	120	**169**	120
Allowance for credit losses	**–**	(4)	**–**	(4)
Trade receivable, net	**169**	116	**169**	116
Value Added Tax	**194**	281	**194**	281
Prepaid insurance	**29**	23	**29**	23
Prepayments and other receivables	**253**	190	**253**	190
	645	610	**645**	610

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. Trade receivables (including securitised trade receivables) represent 9.5% (2018: 6.3%) of turnover.

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
12. Trade and other receivables *(continued)*				
12.1 Reconciliation of the allowance for credit losses				
Balance at beginning of year	**4**	–	**4**	–
Raised during the year	**–**	4	**–**	4
Released during the year	**(4)**	–	**(4)**	–
Balance at end of year	**–**	4	**–**	4

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

12.2 Analysis of amounts past due

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

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Less than 7 days overdue	**–**	–	**–**	–
Between 7 and 30 days overdue	**1**	–	**–**	–
Between 30 and 60 days overdue	**–**	–	**–**	–
More than 60 days overdue	**–**	1	**–**	4
	1	1	**–**	4

The group and company holds collateral of ZAR47.5 million (2018: ZAR72.6 million) against trade receivables past contractual repayment terms. The group and company holds collateral of ZARnil (2018: ZAR1.4 million) against past due trade receivables.

12.3 Fair value

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

12. Trade and other receivables *(continued)*

12.4 Off-balance sheet structures (securitisation)

Sappi sells the majority of its ZAR receivables to Rand Merchant Bank Limited, a division of First Rand 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, the group and company would discontinue further sales of trade receivables and would not incur any losses in respect of trade receivables previously sold in excess of the 15% mentioned above. There are a number of events which may trigger termination of the facility, among others, an amount of defaults above a specified level, terms and conditions of the agreement not being met, or breaches of various credit insurance ratios. The impact on liquidity varies according to the terms of the agreement; generally, however, future trade receivables would be recorded on-balance sheet until a replacement agreement is entered into.

Details of the securitisation programme for group and company at the end of the 2019 and 2018 financial years are disclosed in the table below:

Bank	**Value**	**Facility**	**Discount charges**
2019			
Rand Merchant Bank Limited	**ZAR1,723 million**	**Unlimited [1]**	**Linked to 3-month JIBAR**
2018			
Rand Merchant Bank Limited	ZAR1,004 million	Unlimited [1]	Linked to 3-month JIBAR

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

Refer to note 27 for further details on credit risks.

12. Trade and other receivables *(continued)*

12.5 Concentration of credit risk

A significant portion of the group and company's sales and trade receivable are from a small number of customers. None of the group and company's significant customers represented more than 10% of our sales and trade receivables during the years ended September 2019 and September 2018.

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

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

At balance sheet date, the carrying amount of ZAR645 million (2018: ZAR610 million) represents the group and company's maximum credit risk exposure from trade and other receivables. At balance sheet date, no provision or impairment was required to any of the group and company's customers with balances equal to or greater than ZAR75 million.

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

	Group		Company	
Threshold	**Number of customers**	**ZAR'millions**	Number of customers	ZAR'millions
Less than ZAR75 million	**67**	**152**	79	110

	Group		**Company**	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
13. Ordinary share capital and share premium				
Authorised share capital				
6 052 500 Ordinary shares of R2 each	**12**	12	**12**	12
19 520 Class A cumulative preference shares[(1)(2)]	**–**	–	**–**	–
221 107 Class B cumulative preference shares[(1)(2)]	**–**	–	**–**	–
831 Class C cumulative preference shares[(1)(2)]	**–**	–	**–**	–
123 321 Class D cumulative preference shares[(1)(2)]	**–**	–	**–**	–
	12	12	**12**	12

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
13. Ordinary share capital and share premium *(continued)*				
Issued share capital				
6 015 769 (2018: 6 015 769) Ordinary shares of R2 each	**12**	12	**12**	12
19 520 (2018: 19 520) Class A cumulative preference shares of R0.01 each [(1)(2)(3)]	**–**	–	**–**	–
219 760 (2018: 219 760) Class B cumulative preference shares of R0.01 each [(1)(2)(3)]	**–**	–	**–**	–
831 (2018: 831) Class C cumulative preference shares of R0.01 each [(1)(2)(3)]	**–**	–	**–**	–
120 018 (2018: 119 183) Class D cumulative preference shares of R0.01 each [(1)(2)(3)]	**–**	–	**–**	–
Sappi Property Company (Pty) Limited [(2)(3)]	**–**	–	**–**	–
	12	12	**12**	12
Share premium	**209**	209	**209**	209
Share premium on preference shares issued	**–**	–	**223**	223
362 532 Investment in Sappi Property Company Proprietary Limited [(1)(2)]	**–**	–	**(223)**	(223)
Ordinary share capital and share premium	**221**	221	**221**	221

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

(2) The Class "A","B","C" and "D" preference shares were issued to Sappi Property Company Proprietary Limited (SPC) for no cash consideration on 30 June 2008. SSA subsequently acquired all the ordinary shares of SPC on 11 June 2010. Sappi Southern Africa Limited holds 362 532 (2018: 362 650) preference shares in SPC. A legal right to off-set these preference shares exists.

(3) Issued at nominal value

13. Ordinary share capital and share premium *(continued)*

Capital risk management

The capital structure of the group and company consists of:

- issued share capital and share premium and accumulated profits disclosed above and in the statements of changes in equity respectively,
- debt, which includes interest-bearing borrowings as disclosed in note 17, and
- cash and cash equivalents.

The objectives of the group and company in managing capital are:

- to safeguard the group and company'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 and company 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 and company has entered into a number of debt facilities which contain certain terms and conditions in respect of capital management.

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

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

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

14. Other comprehensive (loss)/income

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Items that will not be reclassified subsequently to profit or loss	**(103)**	14	**(103)**	14
Actuarial (losses)/gains on post-employment benefit funds (refer to notes 23 and 24)	**(143)**	19	**(143)**	19
Deferred tax	**40**	(5)	**40**	(5)
Items that will not be reclassified subsequently to profit or loss	**(79)**	88	**(79)**	88
Hedging reserves gains during the year	**63**	102	**63**	102
Reclassified to profit or loss	**(6)**	23	**(6)**	23
Reclassified to property, plant and equipment	**(187)**	(3)	**(187)**	(3)
Deferred tax	**51**	(34)	**51**	(34)
Other comprehensive (loss)/income	**(182)**	102	**(182)**	102
Profit for the year	**2 534**	2 176	**2 691**	2 292
Total comprehensive income for the year	**2 352**	2 278	**2 509**	2 394

15. Non-distributable reserves

Share-based payment reserve	**(58)**	(57)	**(60)**	(59)
Share-based payment reserve – BBBEE	**216**	214	**216**	214
	158	157	**156**	155

16. Trade and other payables

Trade payables	**2 606**	2 531	**2 606**	2 531
Employee related liabilities	**340**	339	**340**	339
Capital expenditure accruals	**458**	161	**458**	161
Accrued interest	**78**	42	**78**	42
Rebates	**352**	295	**352**	295
Other payables	**417**	307	**417**	306
Trade and other payables	**4 251**	3 675	**4 251**	3 674

17. Interest-bearing borrowings

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Unsecured borrowings	**2 642**	1 145	**2 642**	1 145
Less: Current portion included in current liabilities	**(1 144)**	–	**(1 144)**	–
Total non-current interest-bearing borrowings	**1 498**	1 145	**1 498**	1 145
The repayment profile of the interest-bearing borrowings is as follows:				
Payable in the year ended September:				
2019	**–**	–	**–**	–
2020	**1 144**	1 145	**1 144**	1 145
2021	**(1)**	–	**(1)**	–
2022	**(1)**	–	**(1)**	–
2023	**–**	–	**–**	–
2024 (September 2018: Thereafter)	**1 500**	–	**1 500**	–
	2 642	1 145	**2 642**	1 145

17. Interest-bearing borrowings *(continued)*

Capitalised lease liabilities

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

Set out below are details of the more significant interest-bearing borrowings in the group and company as at September 2019:

	Currency	Interest rate	Principal amount outstanding ZAR'millions	Balance sheet amount ZAR'millions	Security/ cession	Expiry
Redeemable bonds						
Public bond	**ZAR**	**Fixed [1]**	**745**	**745**	**Unsecured**	**April 2020**
Unsecured bank term loans						
GroCapital Financial Services	**ZAR**	**Variable**	**400**	**400**	**Unsecured**	**May 2020**
Nedbank	**ZAR**	**Fixed [1]**	**1 500**	**1 498**	**Unsecured**	**May 2024**

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

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

17. Interest-bearing borrowings *(continued)*

Other restrictions

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

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

During the 2019 and 2018 financial years, the group and company was in compliance with the financial covenants relating to all loans payable. Compliance with applicable covenants are monitored on an ongoing basis. If a possible breach of a financial covenant were to be expected, negotiations would commence with the applicable institutions before such breach occurs.

Unutilised facilities

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

	Currency	Interest rate	**2019 ZAR'millions**	2018 ZAR'millions
Unutilised committed facilities				
Syndicate loan/revolving credit facility [1]	ZAR	Variable (JIBAR)	**1 000**	1 000
Unutilised uncommitted facilities				
Cash management overdraft facility/short-term banking facilities	ZAR	Variable (ZAR bank prime rate)	**575**	275
Total unutilised facilities (committed and uncommitted) excluding cash			**1 575**	1 275

[1] Syndicated loans with a consortium of banks with revolving facilities available of ZAR1 billion. The ZAR1 billion facility is an evergreen facility with a 15 month notice period and is subject to financial covenants relating to the financial position of Sappi Southern Africa Limited. During the year, the group and company paid an amount of ZAR4.5 million (2018: ZAR4.4 million) thousand) in respect of this facility.

Fair value

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

		Group		Company	
		2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
18.	**Other non-current liabilities**				
	Post-employment benefits – post-retirement healthcare subsidy other than pension liability (refer to note 24)	**291**	271	**291**	271
19.	**Notes to the statements of cash flows**				
19.1	**Cash generated from operations**				
	Profit for the year	**2 534**	2 176	**2 691**	2 292
	Adjustment for:				
	– Depreciation (note 6)	**1 028**	874	**1 028**	874
	– Fellings (note 3.1)	**1 017**	861	**1 017**	861
	– Impairment reversals of property, plant and equipment (note 3.3)	**(108)**	–	**(108)**	–
	– Taxation charge (note 5)	**1 008**	1 202	**1 008**	1 172
	– Net finance (income)/ costs (note 4)	**113**	(85)	**113**	(85)
	– Equity accounted investee profits (note 9)	**(46)**	(45)	**(46)**	(45)
	– Dividends received	**–**	–	**(156)**	(211)
	– Profit/(loss) on disposal of property, plant and equipment (note 3.3)	**(12)**	(53)	**(12)**	58
	– Plantation fire, drought and other damages (note 7)	**58**	6	**58**	6
	– Fair value adjustment gains and growth on plantations (note 7)	**(1 324)**	(1 247)	**(1 324)**	(1 247)
	– Other non-cash items – forex	**75**	(1)	**73**	(3)
		4 343	3 688	**4 342**	3 672

Sappi Southern Africa Limited

Notes to the group and company financial statements

for the year ended September 2019 (continued)

		Group		Company	
		2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
19.	**Notes to the statements of cash flows** *(continued)*				
19.2	**Increase in working capital**				
	Decrease/(increase) in inventories	**10**	(395)	**10**	(401)
	Decrease/(increase) in receivables	**179**	(409)	**179**	(410)
	(Increase) in amounts owed by related parties	**(185)**	(364)	**(185)**	(364)
	(Decrease)/increase in payables	**(31)**	843	**(31)**	847
	(Decrease)/increase in amounts owed to related parties	**(52)**	32	**(52)**	32
		(79)	(293)	**(79)**	(296)
19.3	**Finance costs paid**				
	Interest and other finance costs on liabilities carried at amortised cost (note 4)	**(150)**	(128)	**(150)**	(128)
	Net foreign exchange (losses) gains (note 4)	**(31)**	33	**(31)**	33
	Non-cash movements included in items above	**88**	16	**88**	16
		(93)	(79)	**(93)**	(79)
19.4	**Taxation paid**				
	Net amounts payable at beginning of year	**(109)**	41	**(109)**	42
	Taxation (charge) to profit or loss (note 5)	**(758)**	(893)	**(758)**	(863)
	Taxation (charge) benefit per OCI (note 14)	**11**	(7)	**11**	(7)
	Less: Net amounts payable at end of year	**362**	109	**362**	109
		(494)	(750)	**(494)**	(719)

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
19. Notes to the statements of cash flows *(continued)*				
19.5 Proceeds on disposal of property, plant and equipment				
Book value of property, plant and equipment disposed of	**13**	91	**13**	71
Profit/(loss) on disposal of property, plant and equipment (note 3.3)	**12**	53	**12**	(58)
	25	144	**25**	13

19.6 Reconciliation of liabilities arising from financing activities

	2018 ZAR'millions	**Cash flows ZAR'millions**	**Transfers between long-term and short-term ZAR'millions**	**2019 ZAR'millions**
Long-term borrowings (note 17)	1 145	**1 497**	**(1 144)**	**1 498**
Short-term borrowings (note 17)	–	**–**	**1 144**	**1 144**
Total	1 145	**1 497**	**–**	**2 642**

20. Encumbered assets

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

21. Commitments

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Capital commitments				
Contracted but not provided	**2 294**	2 227	**2 294**	2 227
Approved but not contracted	**1 661**	3 425	**1 661**	3 425
	3 955	5 652	**3 955**	5 652
Future forecasted cash flows of capital commitments at September:				
2019	**–**	3 230	**–**	3 230
2020	**3 917**	2 263	**3 917**	2 263
2021 (2018 thereafter)	**38**	159	**38**	159
Thereafter	**–**	–	**–**	–
	3 955	5 652	**3 955**	5 652

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

Operating lease commitments

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

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
2019	**–**	101	**–**	101
2020	**106**	46	**106**	46
2021	**97**	32	**96**	32
2022	**93**	25	**92**	25
2023	**94**	22	**94**	22
2024 (2018: Thereafter)	**81**	99	**82**	99
Thereafter	**113**	–	**114**	–
	584	325	**584**	325

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

22. Contingent liabilities

Contingent liabilities mainly relate to environmental and taxation queries in respect of the group and company.

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

The group and company has been audited by the South African Revenue Service (SARS) in respect of transfer pricing relating to the 2011-2014 years of assessment. The group and company received an assessment from SARS on 26 February 2018 with an adjustment to taxable income of ZAR883 million which resulted in an additional tax liability of ZAR247 million, excluding any potential interest and penalties. SARS also issued a Dividend assessment of ZAR68,7 million. The group and company did not agree with the SARS analysis and consequently objected to and appealed against the basis for the adjustments, including representation on why interest and penalties should not be raised. The group and company made a payment without prejudice of ZAR268 million as well as quarterly instalments of ZAR6.8 million for the dividend assessment. SARS advised the group and company on 3 October 2019 that this matter is suitable for alternative dispute resolution (ADR). Two ADR meetings were held in December 2019 (10 & 17 December), with a settlement proposal submitted to SARS on 6 January 2020. The relevant SARS committee is meeting within the next two weeks to discuss this proposal.

23. Post-employment benefits – pensions

	Group		**Company**	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Reconciliation of balance sheet				
Defined benefit pension plan assets on balance sheet prior year	**256**	236	**256**	236
Post-employment plan cost recognised in profit or loss	**(38)**	(49)	**(38)**	(49)
Employer contributions paid during the financial year	**58**	61	**58**	61
Actuarial (losses)/gains on post-employment benefit funds	**(148)**	8	**(148)**	8
Defined benefit pension plan assets (note 10)	**128**	256	**128**	256

23. Post-employment benefits – pensions *(continued)*

Defined contribution plans

The group and company operates a defined contribution plan for all qualifying employees throughout the group and company. The assets of the plans are held separately from those of the group and company, in funds under the control of plan fiduciaries (trustees). The group and company also participates in local industry multi-employer plans, open to eligible employees as a voluntary alternative to the group and company's own sponsored plan. There are no obligations on the group and company other than to pay contributions according to the rules of each plan. At year end, the group and company was in the process of transferring the group and company sponsored plan to an umbrella fund.

The total defined contribution plan expense charged to the income statement of ZAR156 million (2018: ZAR140 million) represents contributions payable to these plans by the group and company based on rates specified in the rules of these plans.

Defined benefit pension plans

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

The assets of the funded plans are held in separate trustee-administered funds and are subject to statutory requirements. The trusts are required by law to act in the interests of the fund and its stakeholders, i.e. members and sponsoring companies The plans comprise of management and member-appointed trustees including an independent trustee, who collectively are responsible for the management of the trusts.

Benefits are formula-driven, based on final average salary.

Exposure to risks

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

- Discount rate: given the defined benefit nature of the liabilities, there is a risk that bond yields (and therefore the discount rate) reduce in future leading to higher liabilities. This risk has largely been mitigated by the implementation of a liability matching investment strategy;
- Inflation: The risk that future inflation is higher than expected, which will affect the size of the benefits,
- Future changes in legislation: The risk that changes to legislation with respect to the post-employment liability may increase the liability for the group and company,
- Future changes in the tax environment: The risk that changes in the tax legislation governing employee benefits may increase the liability for the group and company,
- Longevity: The risk that pensioners live longer than expected and thus the value of their pension benefit is larger than expected,
- Administration: Administration of this liability poses a burden to the group and company, or that data is incomplete or incorrect,
- Investment: the risk that the return earned by plan assets is lower than expected, although this risk has been partially mitigated by the implementation of a liability matching investment strategy; and
- Default: The risk of default on the instruments underpinning the plan assets.

23. Post-employment benefits – pensions *(continued)*

Exposure to risks *(continued)*

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 and company is exposed to equity, property, high yield bond market risk and for non-domestic holdings, currency risk. Debt instruments typically comprise investment grade corporate and government debt in markets around the globe, primarily held to match counter-movements in plan liabilities of the same value. The group and company is also exposed to losses from the effects of credit grade re-ratings on debt instruments in bond markets across the globe.

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

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

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

Investment management and strategic asset allocation

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

Funding policy

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

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

23. Post-employment benefits – pensions *(continued)*

Funding policy *(continued)*

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Components of defined benefit cost recognised in profit or loss				
Current service cost	**53**	61	**53**	61
Past service cost	**1**	2	**1**	2
Net interest on employee defined benefit liability	**(21)**	(19)	**(21)**	(19)
Fund administration costs	**5**	5	**5**	5
Net amount recognised in profit or loss	**38**	49	**38**	49
Components of defined benefit cost recognised in other comprehensive income				
Actuarial losses arising from membership experience	**(2)**	(33)	**(2)**	(33)
Actuarial gains arising from changes in demographic assumptions	**–**	2	**–**	2
Actuarial gains arising from changes in financial assumptions	**42**	181	**42**	181
Actuarial losses arising on assets	**(188)**	(142)	**(188)**	(142)
Net amount recognised in other comprehensive income	**(148)**	8	**(148)**	8

23. Post-employment benefits – pensions *(continued)*

Funding policy *(continued)*

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Movement in the present value of the defined benefit obligation in the current year				
Defined benefit obligation at beginning of year	**1 626**	1 729	**1 626**	1 729
Current service cost	**53**	61	**53**	61
Past service cost	**1**	2	**1**	2
Interest cost	**155**	157	**155**	157
Plan participants' contributions	**21**	21	**21**	21
Actuarial remeasurements gain/(loss)	**(40)**	(150)	**(40)**	(150)
– Membership experience	**2**	33	**2**	33
– Demographic assumption	**–**	(2)	**–**	(2)
– Financial assumption losses	**(42)**	(181)	**(42)**	(181)
Non-routine plan amendment, curtailment loss and settlement gain	**–**	–	**–**	–
Benefits paid	**(197)**	(194)	**(197)**	(194)
Defined benefit obligation at end of year	**1 619**	1 626	**1 619**	1 626
Movement in the fair value of the plan assets in the current year				
Fair value of plan assets at beginning of year	**1 882**	1 965	**1 882**	1 965
Interest income	**176**	176	**176**	176
Employer contributions	**58**	61	**58**	61
Plan participants' contributions	**21**	21	**21**	21
Actuarial remeasurement gain/(loss) – arising on assets	**(188)**	(142)	**(188)**	(142)
Non-routine plan amendment, curtailment loss and settlement gain	**–**	–	**–**	–
Benefits paid	**(197)**	(194)	**(197)**	(194)
Fund administration costs	**(5)**	(5)	**(5)**	(5)
Fair value of plan assets at end of year	**1 747**	1 882	**1 747**	1 882
Defined benefit pension plan assets (refer to note 10)	**(128)**	(256)	**(128)**	(256)

23. Post-employment benefits – pensions *(continued)*

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

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Investments quoted in active markets				
– Equity, property and high yield investments				
– Domestic				
– Foreign				
– Real estate				
– Investment grade debt instruments				
– Nominal				
– Index linked				
Unquoted investments				
– Other				
Cash and cash equivalents	**(128)**	(256)	**(128)**	(256)

Plan assets do not include any investments in the group and company's own quoted shares. However, Sappi shares will be held by appointed investment managers as part of the routine mandates investing in domestic equities.

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

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

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Discount rate (%)	**9.09**	9.69	**9.09**	9.69
Future salary increases (%)	**6.19**	7.09	**6.19**	7.09
Cost of living adjustment for pensions in payment (%)	**4.15**	4.87	**4.15**	4.87
Average life expectancy in years				
– For current beneficiaries (male of 60 years)	**19.20**	19.20	**19.20**	19.20
– Future retiree (male of 60 years in 20 years' time)	**20.20**	20.20	**20.20**	20.20

23. Post-employment benefits – pensions *(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 and mortality. The sensitivity analysis below has been determined based on reasonably possible changes of the respective assumptions occurring at the end of the reporting period, whilst holding all other assumptions constant.

- If the discount rate is 100 basis points higher (lower), the defined benefit obligation would decrease by ZAR209 million (increase by ZAR243 million).
- If the expected salary increase rate is 100 basis points higher (lower), the defined benefit obligation would increase by ZAR226 million (decrease by ZAR191 million).
- If the expected cost of living adjustment (pension increase) rate is 100 basis points higher (lower), the defined benefit obligation would increase by ZAR116 million (decrease by ZAR109 million).
- If the life expectancy increases (decreases) by one year for both men and women, the defined benefit obligation would increase by ZAR27 million (decrease ZAR28 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 financial year-end, which is the same as that applied in calculating that applied in calculating the defined benefit obligation recognised in the balance sheet. There was no change in the methods and assumptions used in preparing the sensitivity analysis from prior years.

The average duration of the defined benefit plan obligations at financial year-end is 8 years.

24. Post-employment benefits - post-retirement healthcare subsidy

	Group		**Company**	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Reconciliation of balance sheet				
Healthcare subsidy liability recognised on balance sheet prior year	**(271)**	(250)	**(271)**	(250)
Post-employment cost recognised in profit or loss	**(34)**	(32)	**(34)**	(32)
Employer contributions paid during the financial year	**9**	–	**9**	–
Actuarial (losses)/gains on post-employment benefit funds	**5**	11	**5**	11
Healthcare subsidy liability recognised on balance sheet (note 8)	**(291)**	(271)	**(291)**	(271)

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

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

	Group		**Company**	
	2019	2018	**2019**	2018
	ZAR'millions	ZAR'millions	**ZAR'millions**	ZAR'millions
Components of defined benefit cost recognised in profit or loss				
Current service cost	**8**	8	**8**	8
Net interest on employee liabilities defined benefit	**26**	24	**26**	24
Net amount recognised in profit or loss	**34**	32	**34**	32
Components of defined benefit cost recognised in other comprehensive income				
Actuarial losses arising from membership experience	**(27)**	(1)	**(27)**	(1)
Actuarial losses arising from changes in demographic assumptions	**–**	(25)	**–**	(25)
Actuarial gains arising from changes in financial assumptions	**32**	38	**32**	38
Actuarial losses arising on assets	**–**	(1)	**–**	(1)
Net amount recognised in other comprehensive income	**5**	11	**5**	11

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

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Movement in the present value of the defined benefit obligation in the current year				
Defined benefit obligation at beginning of year	**376**	359	**376**	359
Current service cost	**8**	8	**8**	8
Interest expense	**36**	34	**36**	34
Actuarial remeasurements (gain) loss	**(5)**	(12)	**(5)**	(12)
– Membership experience	**27**	1	**27**	1
– Demographic assumption changes	**–**	25	**–**	25
– Financial assumption gain	**(32)**	(38)	**(32)**	(38)
Non-routine plant amendment, curtailment loss and settlement gain	**(6)**	–	**(6)**	–
Benefits paid	**(15)**	(13)	**(15)**	(13)
Defined benefit obligation at end of year	**394**	376	**394**	376
Movement in the fair value of the plan assets in the current year				
Fair value of plan assets at beginning of year	**105**	109	**105**	109
Interest income	**10**	10	**10**	10
Employer contributions	**9**	–	**9**	–
Actuarial remeasurements gain/(loss)				
– Actuarial loss arising on assets	**–**	(1)	**–**	(1)
Non-routine plan amendment, curtailment loss and settlement gain	**(6)**	–	**(6)**	–
Benefits paid	**(15)**	(13)	**(15)**	(13)
Fair value of plan assets at end of year	**103**	105	**103**	105
Net balance sheet defined benefit liability (note 18)	**291**	271	**291**	271

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

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

	Group		Company	
	2019	2018	**2019**	2018
	ZAR'millions	ZAR'millions	**ZAR'millions**	ZAR'millions
Movement in the present value of the defined benefit obligation in the current year				
Investments quoted in active markets				
– Investment grade debt instruments				
– Nominal				
– Index linked				
Unquoted investments				
– Other	**92**	94	**92**	94
Cash and cash equivalents	**11**	12	**11**	12
	103	106	**103**	106

Assets consist of an annuity policy of insurance and money market funds. The fair value of the annuity policy is assessed by the insurer using established methods based on observable bond yields.

The principal assumptions used in determining post-retirement healthcare subsidy for the group and company's plans are shown below:

	Group		Company	
	2019	2018	**2019**	2018
Discount rate (%)	**10.44**	10.00	**10.44**	10.00
Healthcare cost trend rate (%)	**7.58**	7.75	**7.58**	7.75
Average expectancy in years				
– For current beneficiaries (male of 60 years)	**19.50**	19.50	**19.50**	19.50

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

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

- If the discount rate is 100 basis points higher (lower), the defined benefit obligation would decrease by ZAR45 million (increase by ZAR56 million).
- If the expected health care cost trend rate is 100 basis points higher (lower), the defined benefit obligation would increase by ZAR57 million (decrease by ZAR47 million).
- If the life expectancy increases (decreases) by one year for both men and women, the defined benefit obligation would increase by ZAR12 million (decrease ZAR12 million).

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

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 financial year-end, which is the same as that applied in calculating the defined benefit plan obligation liability recognised in the balance sheet.

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

The average duration of the defined benefit plan obligations at financial year-end is 14 years.

25. Share-based payments

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

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

The Sappi Limited Share Incentive Trust (the Scheme)

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

Under the rules of the Scheme:

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

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

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

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

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

25. Share-based payments *(continued)*

The Sappi Limited Performance Share Incentive Trust (the Plan)

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

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

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

The Plan rules also provide that if:

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

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

Movements in share options and performance shares for the financial years ended September 2019 and September 2018 are as follows:

	Performance shares [1]	Share options	Weighted average share option exercise price (ZAR)	Total shares
Outstanding at September 2017	3 313 180	514 610	29.08	3 287 790
– Offered	706 550	–	–	706 550
– Paid for/vested	(956 978)	(294 540)	31.28	(1 251 518)
– Returned, lapsed, forfeited and transfers	(66 662)	(23 900)	33.85	(90 562)
Outstanding at September 2018	2 996 090	196 170	26.15	3 192 260
– Offered	**685 000**	**–**	**–**	**685 000**
– Paid for/vested	**(719 637)**	**(76 250)**	**30.09**	**(795 887)**
– Returned, lapsed, forfeited and transfers	**(231 935)**	**(30 500)**	**27.51**	**(262 435)**
Outstanding at September 2019	**2 729 518**	**89 420**	**22.90**	**2 818 938**
Exercisable at September 2018	–	196 170	26.15	196 170
Exercisable at September 2019	**–**	**89 420**	**22.90**	**89 420**

[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.

25. Share-based payments *(continued)*

The Sappi Limited Performance Share Incentive Trust (the Plan) *(continued)*

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

	2019	Vesting conditions	Vesting rights	Expiry date	Exercise price (ZAR)
Share options					
2 December 2011	**89 420**	Time	Vested	2 December 2019	22.90
Performance shares					
7 December 2015	**803 492**	Performance	7 December 2019	n/a	–
9 December 2016	**622 189**	Performance	9 December 2020	n/a	–
4 December 2017	**625 193**	Performance	4 December 2021	n/a	–
19 November 2018	**678 644**	Performance	19 November 2022	n/a	–
	2 818 938				

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

	Issue 44	Issue 44
Date of grant	19 November 2018	19 November 2018
Type of award	Performance	Performance
Share price at grant date	ZAR 82.49	ZAR 82.49
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	68.5%	80.0%
Number of shares offered	1 544 075	1 544 075
Volatility	30%	n/a
Risk-free discount rate	7.8% (ZAR yield)	n/a
Expected dividend yield	2.5%	n/a
Model used to value	Monte-Carlo	Market price
Fair value of option	ZAR 61.79	ZAR 59.46

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

Refer to note 29 for more information on directors' and prescribed officers' participation in the Scheme and the Plan.

25. Share-based payments *(continued)*

Broad-based Black Economic Empowerment

Sappi's BBBEE transaction vested in August 2019 with the "A" ordinary shares vesting at Rnil value as the 30 volume-weighted average share price of ZAR46.91 was below the share price hurdle hurdle rate of ZAR72.18. As a result Sappi Limited repurchased and cancelled all the 19,961,476 "A" ordinary shares from the BBBEE trusts at par value. The 1,280,597 ordinary shares held within the ESOP trust for certain Sappi employees vested at ZAR42.70 per share.

The group and company incurred a total share-based payment expense of ZAR41 million (2018: ZAR50 million) during the 2019 financial year.

26. Derivative financial instruments

		Group		Company	
		2019	2018	**2019**	2018
		ZAR'millions	ZAR'millions	**ZAR'millions**	ZAR'millions
Hedging instrument	**Hedged item**				
Non-current assets					
Forward exchange contracts	Various	**–**	54	**–**	54
Current assets					
Forward exchange contracts	Various	**24**	123	**24**	123
Non-current liabilities					
Interest rate swap (IRS)	ZAR1500 million unsecured loan	**31**	**–**	**19**	17
Forward exchange contracts	Various	**1**	**–**	**14**	63
		32	**–**	**33**	80
Current liabilities					
Fx zero cost collars	Highly probable forecast sale	**19**	17	**19**	17
Forward exchange contracts	Various	**14**	63	**14**	63
		33	80	**33**	80

Refer to note 27 for more detail on financial instruments.

27. Financial instruments

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

Introduction

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

a) Market risk (the risk of loss arising from adverse changes in market rates and prices), arising from:
- Interest rate risk
- Currency risk and
- Commodity price risk

b) Liquidity risk and

c) Credit risk

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

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

The group and company'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 and company including the exposures and transactions relating to those financial instruments and risks referred to in this note.

a) Market risk

Interest rate risk

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

The group and company is exposed to interest rate risk as it borrows funds at both fixed and variable interest rates. The group and company 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 and company's exposure to interest rate risk is set out below.

27. Financial instruments *(continued)*

a) Market risk *(continued)*

Interest-bearing borrowings

The following table provides information about Sappi's principal amounts of current and non-current borrowings that are sensitive to changes in interest rates. The table presents cash flows of the carrying value by expected maturity dates and the estimated fair value of borrowings. The average fixed effective interest rates presented are based on weighted average contract rates applicable to the amount expected to mature in each respective year. Forward-looking average variable effective interest rates for the financial years ended September 2019 and thereafter are based on the yield curves for each respective currency as published by Bloomberg on 29 September 2019.

Group and company	**Expected maturity date**								
	2020	2021	2022	2023	2024	**2019**		2018	
ZAR'millions						**Carrying value**	**Fair value**	Carrying value	Fair value
Fixed rate debt	744	–	–	–	1 498	**2 242**	**2 399**	745	775
Average interest rate (%)	8.06	–	–	–	9.26	**8.86**	**–**	8.06	–
Variable rate debt	400	–	–	–	–	**400**	**424**	400	424
Average interest rate (%)	9.46	–	–	–	–	**9.74**	**–**	9.46	–
Fixed and variable	1 144	–	–	–	1 498	**2 642**	**2 823**	1 145	1 199
Current portion						**1 144**	**1 199**	–	–
Long-term portion						**1 498**	**1 624**	1 145	1 199
Total interest-bearing borrowings (refer to note 17)						**2 642**	**2 823**	1 145	1 199

27. Financial instruments *(continued)*

a) Market risk *(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.

A detailed analysis of the group and company's interest-bearing borrowings is presented in note 17.

Hedging of interest rate risk

Depending on the market conditions, Sappi uses interest rate derivatives 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.

Hedge effectiveness is assessed at inception of the hedge relationship and on a quarterly basis or upon a significant change in circumstances affecting the hedge effectiveness requirements. The hedge effectiveness requirements are principles-based, so there is no determined precise quantitative threshold of effectiveness. The hedge effectiveness assessment is only forward looking using the critical terms match.

Retrospective measurement is based on the hypothetical derivative approach which is a type of ratio analysis comparing changes in fair value or cash flows of the hedging instrument with the changes in fair value or cash flows of the perfect hypothetical derivative. The hypothetical derivative exactly mirrors the features of the underlying hedged item.

The valuation of the hedging instruments includes an adjustment for credit risk, i.e. 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 swaps (IRS) variable to fixed
In May 2019, Sappi contracted a variable rate term loan in the total amount of ZAR1.5 billion maturing in 2024 and swapped the variable rates into fixed rates. This liability and the corresponding interest rate swap are designated in a cash flow hedging relationship, allowing all mark-to-market valuations of the swaps to be booked to equity. As all critical terms of the hedged item and the hedging instrument match perfectly, the hedge is expected to continue being highly effective.

27. Financial instruments *(continued)*

a) Market risk *(continued)*

Cash flow hedges *(continued)*

Interest rate swaps (IRS) variable to fixed (continued)
At September 2019, the hedge was highly effective and the swap had a net negative fair value of ZAR31 million which was deferred to equity.

Summary of outstanding cash flow hedges

Group and company

					Recorded in	
September 2019	**Interest rate**	**Maturity date**	**Nominal value ZAR'millions**	**Total fair value[1] ZAR'millions**	**OCI ZAR'millions**	**Profit or loss ZAR'millions**
Cash flow hedges						
IRS	ZAR variable (3-M JIBAR + 180 BPS) to ZAR 9.248% fixed	May 2024	1 500	**31**	**31**	**–**
September 2018	–	–	–	–	–	–

[1] This refers to the carrying amount.

The total fair value of the IRS is 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 and company 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

Sensitivity analysis: interest rate risk - in case of a credit rating change of Sappi Southern Africa Limited
To the extent of any downgrade on the group and company's revolving credit facility, a change in the group and company's own credit rating will affect the funding rate. Assuming an annual drawdown of ZAR1 million, a one notch downgrade will negatively impact profit before tax by ZAR0.3 million (2018:ZAR0.3million) and a one notch upgrade will have a ZARnil (2018:ZARnil) positive impact. The revolving credit facility was undrawn at financial year-end.

Sensitivity analysis: interest rate risk of variable rate debt
The table below shows the sensitivity of the variable rate debt to a move by 50 bps to the interest rates.

	Fixed rate debt ZAR'millions	**Variable rate debt ZAR'millions**	**Impact on profit or loss of 50 bps interest ZAR'millions**	**Total ZAR'millions**
Total debt (note 17)	2 242	400	2	2 642
Ration fixed/variable total debt	85%	15%		

The variable rate debt represents 15% of total debt. If interest rates were to increase (decrease) by 50 bps, the finance cost on variable rate debt would increase (decrease) by ZAR2 million.

27. Financial instruments *(continued)*

a) Market risk *(continued)*

Currency risk

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

- Economic exposures which consist of planned net foreign currency trade in goods and services not yet manifested in the form of actual invoices and orders, and

- Transaction exposures arise from transactions entered into which result in a flow of cash in foreign currency such as payments under foreign currency long- and short-term loan liabilities, purchases and sales of goods and services, capital expenditure and dividends. Where possible, commercial transactions are only entered into in currencies that are readily convertible by means of formal external forward exchange contracts.

In managing currency risk, the group and company 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 2019 and 2018 financial years disclose financial instruments as determined by IFRS 9 *Financial Instruments: Recognition and Measurement*, classified by underlying currency, and does not indicate the group and company's foreign currency exchange exposure.

Sappi Southern Africa Limited

Notes to the group and company financial statements

for the year ended September 2019 (continued)

27. Financial instruments *(continued)*

a) Market risk *(continued)*

Currency risk *(continued)*

Currency risk analysis *(continued)*

Group and company 2019	Total ZAR'millions	Total in scope ZAR'millions	Currency USD ZAR'millions	EUR ZAR'millions	ZAR ZAR'millions	GBP ZAR'millions	Other ZAR'millions
Classes of financial instruments							
Non-current assets							
Other non-current assets	**329**	**145**	**–**	**–**	**145**	**–**	**–**
Amounts owing by related parties	**5 550**	**5 550**	**–**	**–**	**5 550**	**–**	**–**
Current assets							
Trade and other receivables	**645**	**419**	**–**	**–**	**419**	**–**	**–**
Derivative financial instruments	**24**	**24**	**16**	**7**	**–**	**–**	**1**
Amounts owing by related parties	**2 335**	**2 335**	**–**	**–**	**2 335**	**–**	**–**
Cash and cash equivalents	**1 843**	**1 843**	**–**	**–**	**1 843**	**–**	**–**
		10 316	**16**	**7**	**10 292**	**–**	**1**
Non-current liabilities							
Interest bearing borrowings	**1 498**	**1 498**	**–**	**–**	**1 498**	**–**	**–**
Derivative financial instruments	**32**	**32**	**–**	**1**	**31**	**–**	**–**
Other non-current liabilities	**291**	**–**					
Current liabilities							
Interest-bearing borrowings	**1 144**	**1 144**	**–**	**–**	**1 144**	**–**	**–**
Derivative financial instruments	**33**	**33**	**21**	**9**	**–**	**–**	**3**
Trade and other payables	**4 251**	**3 821**	**–**	**–**	**3 821**	**–**	**–**
Amounts owing to related parties	**153**	**153**	**–**	**–**	**153**	**–**	**–**
		6 681	**21**	**10**	**6 647**	**–**	**3**
Foreign exchange gap		**3 635**	**(5)**	**(3)**	**3 645**	**–**	**(2)**

27. Financial instruments *(continued)*

a) Market risk *(continued)*

Currency risk *(continued)*

Currency risk analysis *(continued)*

Group *(continued)*					**Currency**		
2018	**Total ZAR'millions**	**Total in scope ZAR'millions**	**USD ZAR'millions**	**EUR ZAR'millions**	**ZAR ZAR'millions**	**GBP ZAR'millions**	**Other ZAR'millions**
Classes of financial instruments							
Non-current assets							
Derivative financial instruments	54	54	–	54	–	–	–
Amounts owing by related parties	4 377	4 377	–	–	4 377	–	–
Current assets							
Trade and other receivables	610	304	–	–	304	–	–
Derivative financial instruments	123	123	69	48	–	–	6
Amounts owing by related parties	2 155	2 155	–	–	2 155	–	–
Cash and cash equivalents	1 014	1 014	–	–	1 014	–	–
		8 027	69	102	7 850	–	6
Non-current liabilities							
Interest bearing borrowings	1 145	1 145	–	–	1 145	–	–
Current liabilities							
Interest-bearing borrowings	–	–	–	–	–	–	–
Derivative financial instruments	80	80	–	–	80	–	–
Trade and other payables	3 675	3 256	–	–	3 256	–	–
Amounts owing to related parties	218	218	–	–	218	–	–
		4 699	–	–	4 699	–	–
Foreign exchange gap		3 328	69	102	3 151	–	6

27. Financial instruments *(continued)*

a) Market risk *(continued)*

Currency risk *(continued)*

Currency risk analysis *(continued)*

Company 2018	**Total** **ZAR'millions**	**Total in scope** **ZAR'millions**	**USD** **ZAR'millions**	**EUR** **ZAR'millions**	**Currency** **ZAR** **ZAR'millions**	**GBP** **ZAR'millions**	**Other** **ZAR'millions**
Classes of financial instruments							
Non-current assets							
Derivative financial instruments	54	54	–	54	–	–	–
Amounts owing by related parties	4 377	4 377	–	–	4 377	–	–
Current assets							
Trade and other receivables	610	304	–	–	304	–	–
Derivative financial instruments	123	123	69	48	–	–	6
Amounts owing by related parties	2 155	2 155	–	–	2 155	–	–
Cash and cash equivalents	1 014	1 014	–	–	1 014	–	–
		8 027	69	102	7 850	–	6
Non-current liabilities							
Interest bearing borrowings	1 145	1 145	–	–	1 145	–	–
Current liabilities							
Interest-bearing borrowings	–	–	–	–	–	–	–
Derivative financial instruments	80	80	–	–	80	–	–
Trade and other payables	3 675	3 256	–	–	3 256	–	–
Amounts owing to related parties	377	377	–	–	377	–	–
		4 858	–	–	4 858	–	–
Foreign exchange gap		3 169	69	102	2 992	–	6

27. Financial instruments *(continued)*

a) Market risk *(continued)*

Hedging of foreign currency risk

Based on the exposure at the end of September 2019, 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 ZAR4 million or a gain of ZAR4 million respectively.

During 2019, we contracted non-deliverable average rate foreign exchange transactions for a total notional value of US$203 million which were used as an overlay hedge of export sales from Southern Africa. The total impact on profit or loss amounted to a net gain of ZAR39 million. We also contracted zero cost foreign exchange collars for a total nominal value of US$250 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 2019 the net impact on profit or loss of the collar amounted to a loss of ZAR33 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 (FEC’s) 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 spot movements of the FEC's and the intrinsic value of the zero cost foreign exchange collar is designated as the hedging instrument. The forward points of the FEC's and the time value of the zero cost collars are not included in the hedge designation and will be reported as cost of hedging in other comprehensive income (OCI).

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 2019 financial year, the hedges were highly effective. A realised gain of ZAR39 million relating to the realised fair value movements of non-deliverable forward exchange contracts (including cost of hedging) was transferred from OCI to revenue in the income statement and at the financial year-end, a positive amount of ZAR2 million was deferred in equity. A realised loss of ZAR33 million relating to the settled zero cost foreign exchange collars (including cost of hedging) was transferred from OCI to revenue in the income statement and at the financial year-end, a negative value in the amount of ZAR14 million was deferred to equity.

27. Financial instruments *(continued)*

a) Market risk *(continued)*

Cash flow hedges *(continued)*

Mill expansion and maintenance capital expenditure projects
Sappi Southern Africa (SSA) has approved several capex projects requiring the acquisition of property plant and equipment for the maintenance and expansion of its South African mills Saiccor and Ngodwana. An important part of the equipment was ordered in foreign currency, predominantly in Euro's and in US Dollars which created a foreign exchange exposure as SSA is a South African Rand functional entity. To cover these foreign exchange exposures either as highly probable forecast transactions or as firm commitments, SSA entered into forward foreign exchange contracts (FEC's) which were designated as hedging instruments in a cash flow hedge. The full fair value of the FEC's, including forward points, have been designated as hedging instruments.

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.

b) Liquidity risk

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

The group and company'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 and company's long-term strategy.

Details of the group and company's borrowings, including the maturity profile thereof, as well as the group and company's committed and uncommitted facilities are set out in note 17.

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

Sappi Southern Africa Limited

Notes to the group and company financial statements

for the year ended September 2019 (continued)

27. Financial instruments *(continued)*

b) Liquidity risk *(continued)*

Liquidity risk management

The following tables for the 2019 and 2018 financial years disclose financial instruments, as determined by IFRS 9 *Financial Instruments: Recognition and Measurement*, are classified by liquidity and does not necessarily indicate the group and company's actual cash flows.

Group and company			Undiscounted cash flows					
2019	**Total financial assets and liabilities ZAR'millions**	**Fair value of financial instruments ZAR'millions**	**0 – 6 months ZAR'millions**	**6 – 12 months ZAR'millions**	**1 – 2 years ZAR'millions**	**2 – 5 years ZAR'millions**	**5 years ZAR'millions**	**Total ZAR'millions**
Non-current assets								
Other non-current assets	**145**	**145**	**–**	**–**	**–**	**–**	**145**	**145**
Amounts owing by related parties	**5 550**	**5 550**	**–**	**–**	**–**	**–**	**5 550**	**5 550**
Current assets								
Trade and other receivables	**419**	**419**	**419**	**–**	**–**	**–**	**–**	**419**
Derivative financial instruments	**24**	**24**	**24**	**–**	**–**	**–**	**–**	**24**
Amounts owing by related parties	**2 335**	**2 335**	**2 335**	**–**	**–**	**–**	**–**	**2 335**
Cash and cash equivalents	**1 843**	**1 843**	**1 843**	**–**	**–**	**–**	**–**	**1 843**
			4 621	**–**	**–**	**–**	**5 695**	**10 316**
Non-current liabilities								
Interest-bearing borrowings	**1 498**	**1 624**	**–**	**–**	**–**	**1 498**	**–**	**1 498**
Derivative financial instruments	**32**	**32**	**–**	**–**	**–**	**32**	**–**	**32**
Other non-current liabilities	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Current liabilities								
Interest-bearing borrowings	**1 144**	**1 199**	**1 144**	**–**	**–**	**–**	**–**	**1 144**
Trade and other payables	**3 821**	**3 821**	**3 821**	**–**	**–**	**–**	**–**	**3 821**
Derivative financial instruments	**33**	**33**	**33**		**–**	**–**	**–**	**33**
Amounts owing to related parties	**153**	**153**	**153**	**–**	**–**	**–**	**–**	**153**
			5 151	**–**	**–**	**1 530**	**–**	**6 681**
Liquidity surplus (gap)			**(530)**	**–**	**–**	**(1 530)**	**5 695**	**3 635**

27. Financial instruments *(continued)*

b) Liquidity risk *(continued)*

Liquidity risk management *(continued)*

Group and company *(continued)*			**Undiscounted cash flows**					
2018	**Total financial assets and liabilities ZAR'millions**	**Fair value of financial instruments ZAR'millions**	**0 – 6 months ZAR'millions**	**6 – 12 months ZAR'millions**	**1 – 2 years ZAR'millions**	**2 – 5 years ZAR'millions**	**5 years ZAR'millions**	**Total ZAR'millions**
Non-current assets								
Derivative financial instruments	54	54	–	–	54	–	–	54
Amounts owing by related parties	4 377	4 377	–	–	–	4 377	–	4 377
Current assets								
Trade and other receivables	304	304	304	–	–	–	–	304
Derivative financial instruments	123	123	68	55	–	–	–	123
Amounts owing by related parties	2 155	2 155	2 155	–	–	–	–	2 155
Cash and cash equivalents	1 014	1 014	1 014	–	–	–	–	1 014
			3 541	55	54	4 377	–	8 027
Non-current liabilities								
Interest-bearing borrowings	1 145	1 145	–	–	1 145	–	–	1 145
Current liabilities								
Trade and other payables	3 257	3 257	3 257	–	–	–	–	3 257
Derivative financial instruments	80	80	80		–	–	–	80
Amounts owing to related parties	218	218	218	–	–	–	–	218
			3 555	–	1 145	–	–	4 700
Liquidity surplus (gap)			(14)	55	(1 091)	4 377	–	3 327

27. 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 2019 and 2018 financial years that are included within the various categories on the balance sheet. The reported maturity analysis is calculated on an undiscounted basis.

Group and company		**Maturity analysis Undiscounted cash flows**					
2019	*Note*	**Total ZAR' millions**	**0 – 6 months ZAR' millions**	**6 – 12 months ZAR' millions**	**1 – 2 years ZAR' millions**	**2 – 5 years ZAR' millions**	**> 5 years ZAR' millions**
Classes of derivative financial instruments							
Assets							
Fair value of derivatives by risk factor							
Foreign exchange risk							
Short term - FEC's	*26*	**24**	**15**	**9**	**–**	**–**	**–**
– paying leg		**3**	**2**	**1**	**–**	**–**	**–**
– receiving leg		**21**	**13**	**8**	**–**	**–**	**–**
Liabilities							
Fair value of derivatives by risk factor							
Interest rate risk							
Interest rate swaps	*26*	**31**	**–**	**–**	**–**	**31**	**–**
Foreign exchange risk							
Short term - FEC's	*25*	**15**	**10**	**4**	**1**	**–**	**–**
– paying leg		**6**	**6**	**–**	**–**	**–**	**–**
– receiving leg		**9**	**4**	**4**	**1**	**–**	**–**
Fx zero cost collar	*26*	**19**	**19**	**–**	**–**	**–**	**–**
2018							
Classes of derivative financial instruments							
Assets							
Foreign exchange risk							
Short term - FEC's		177	67	56	54	–	–
– paying leg		(34)	(34)	–	–	–	–
– receiving leg		211	101	56	54	–	–
Liabilities							
Fair value of derivatives by risk factor							
Foreign exchange risk							
Short term - FEC's		80	80	–	–	–	–
– paying leg		80	80	–	–	–	–
– receiving leg		–	–	–	–	–	–

27. Financial instruments *(continued)*

c) Fair values

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

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

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

There are no financial assets and liabilities that have been remeasured to fair value on a non-recurring basis.

Group and company

2019			**Categories in accordance with IFRS 9**				
	Total balance ZAR' millions	**Total out of scope ZAR' millions**	**Total in scope ZAR' millions**	**Fair value through profit or loss ZAR' millions**	**Amortised cost ZAR' millions**	**Fair value through OCI ZAR' millions**	**Fair value ZAR' millions**
Classes of financial instruments							
Non-current assets							
Other non-current assets	**329**	**184**	**145**	**–**	**145**	**–**	**145**
Amounts owing by related parties	**5 550**	**–**	**5 550**	**–**	**5 550**	**–**	**5 550**
	5 879	**184**	**5 695**	**–**	**5 695**	**–**	**5 695**
Current assets							
Trade and other receivables	**645**	**226**	**419**	**–**	**419**	**–**	**419**
Derivative financial instruments	**24**	**–**	**24**	**24**	**–**	**–**	**24**
Amounts owing by related parties	**2 335**	**–**	**2 335**	**–**	**2 335**	**–**	**2 335**
Cash and cash equivalents	**1 843**	**–**	**1 843**	**–**	**1 843**	**–**	**1 843**
	4 847	**226**	**4 621**	**24**	**4 597**	**–**	**4 621**

27. Financial instruments *(continued)*

c) Fair values *(continued)*

Group and company *(continued)*

2019 *(continued)*	Categories in accordance with IFRS 9					
	Total balance ZAR' millions	**Total out of scope ZAR' millions**	**Total in scope ZAR' millions**	**Fair value through profit or loss ZAR' millions**	**Amortised cost ZAR' millions**	**Fair value ZAR' millions**
Classes of financial instruments						
Non-current liabilities						
Interest-bearing borrowings	**1 498**	**–**	**1 498**	**–**	**1498**	**1 624**
Derivative financial instruments	**32**	**–**	**32**	**32**	**–**	**32**
Other non-current liabilities	**291**	**291**	**–**	**–**	**–**	**–**
	1 821	**291**	**1 530**	**32**	**1 498**	**1 656**
Current liabilities						
Interest-bearing borrowings	**1 144**	**–**	**1 144**	**–**	**1 144**	**1 199**
Trade and other payables	**4 251**	**430**	**3 821**	**–**	**3 821**	**3 821**
Derivative financial instruments	**33**	**–**	**33**	**33**	**–**	**33**
Amounts owing to related parties	**153**	**–**	**153**	**–**	**153**	**153**
	5 581	**430**	**5 151**	**33**	**5 118**	**5 206**

Group and company 2018	Categories in accordance with IAS 39					
	Total balance ZAR' millions	**Total out of scope ZAR' millions**	**Total in scope ZAR' millions**	**Fair value through profit or loss ZAR' millions**	**Loans and receivables ZAR' millions**	**Fair value ZAR' millions**
Classes of financial instruments						
Non-current assets						
Derivative financial instruments	54	–	54	54	–	54
Amounts owing by related parties	4 377	–	4 377	–	4 377	4 377
	4 431	–	4 431	54	4 377	4 431
Current assets						
Trade and other receivables	610	306	304	–	304	304
Derivative financial instruments	123	–	123	123	–	123
Amounts owing by related parties	2 155	–	2 155	–	2 155	2 155
Cash and cash equivalents	1 014	–	1 014	–	1 014	1 014
	3 902	306	3 596	123	3 473	3 596
Classes of financial instruments						
Non-current liabilities						
Interest-bearing borrowings	1 145	–	1 145	–	1 145	1 145
Other non-current liabilities	271	271	–	–	–	–
	1 416	271	1 145	–	1 145	1 145
Current assets						
Derivative financial instruments	80	–	80	80	–	80
Trade and other payables	3 675	418	3 257	–	3 257	3 257
Amounts owing to related parties	218	–	218	–	218	218
	3 973	418	3 555	80	3 475	3 555

Refer to 2.4.1 for the changes in classification and measurement from IAS 39 to IFRS 9.

27. Financial instruments *(continued)*

c) Fair values *(continued)*

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in a financial loss to the group and company. The group and company 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 and company basis.

The group and company'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 and company.

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

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

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

Quantitative disclosures on credit risk are included in note 12.

28. Related party transactions

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

	Income and sales to related parties		Purchases and charges from related parties		Related party loans and amounts owed by related parties		Related party loans and amounts owed to related parties	
Group	**2019 ZAR' millions**	2018 ZAR' millions	**2019 ZAR' millions**	2018 ZAR' millions	**2019 ZAR' millions**	2018 ZAR' millions	**2019 ZAR' millions**	2018 ZAR' millions
Sappi Europe SA**	**8**	6	**171**	178	**–**	–	**48**	48
Sappi International SA**	**–**	–	**–**	–	**1**	–	**–**	–
Sappi Limited***	**9**	10	**85**	96	**5 550**	4 377	**–**	–
Sappi Papier Holding GmbH**	**11 564**	10 595	**57**	24	**2 210**	2 148	**–**	–
Sappi Trading Hong Kong Limited**	**–**	–	**–**	–	**43**	–	**–**	–
The Sappi Limited Share Incentive Trust	**–**	–	**–**	–	**–**	–	**18**	–
The Sappi Limited Performance Share Incentive Trust	**–**	–	**–**	–	**–**	–	**87**	67
The Sappi Share Facilitation (Pty) Ltd**	**–**	–	**–**	–	**–**	–	**–**	103
Sappi North America (SD Warren Company)**	**396**	–	**–**	–	**81**	–	**–**	–
Sappisure Försäkrings AB**	**13**	–	**64**	55	**–**	7	**–**	–
	11 990	10 611	**377**	353	**7 885**	6 532	**153**	218

** Fellow subsidiary of Sappi Southern Africa Limited

*** Holding company of Sappi Southern Africa Limited

Sappi Southern Africa Limited

Notes to the group and company financial statements

for the year ended September 2019 (continued)

28. Related party transactions *(continued)*

Company	Income and sales to related parties 2019 ZAR' millions	Income and sales to related parties 2018 ZAR' millions	Purchases and charges from related parties 2019 ZAR' millions	Purchases and charges from related parties 2018 ZAR' millions	Amounts owed by related parties 2019 ZAR' millions	Amounts owed by related parties 2018 ZAR' millions	Amounts owed to related parties 2019 ZAR' millions	Amounts owed to related parties 2018 ZAR' millions
Canonbrae Development Company Proprietary Limited*	**–**	–	**–**	**–**	**–**	**–**	**–**	1
Lereko Property Company Proprietary Limited*	**–**	**–**	**–**	**–**	**–**	**–**	**2**	1
Micawber 279 (RF) Proprietary Limited*	**–**	**–**	**–**	**–**	**–**	**–**	**–**	157
Sappi Europe SA**	**8**	6	**171**	178	**–**	**–**	**48**	49
Sappi International SA**	**–**	**–**	**–**	**–**	**1**	**–**	**–**	**–**
Sappi Limited*** ^	**9**	10	**85**	96	**5 550**	4 377	**–**	**–**
Sappi Papier Holding GmbH**	**11 564**	10 595	**57**	24	**2 210**	2 148	**–**	**–**
Sappi Trading Hong Kong Limited**	**–**	**–**	**–**	**–**	**43**	**–**	**–**	**–**
The Sappi Limited Share Incentive Trust	**–**	**–**	**–**	**–**	**–**	**–**	**18**	**–**
The Sappi Limited Performance Share Incentive Trust	**–**	**–**	**–**	**–**	**–**	**–**	**86**	67
The Sappi Share Facilitation (Pty) Ltd**	**–**	**–**	**–**	**–**	**–**		**–**	102
Sappisure Försakrings AB **	**13**	**–**	**64**	55	**–**	7	**–**	**–**
Sappi North America (SD Warren Company)**	**396**	**–**	**–**	**–**	**81**	**–**	**–**	**–**
	11 990	10 611	**377**	353	**7 885**	6 532	**154**	377

* Subsidiary of Sappi Southern Africa Limited
** Fellow subsidiary of Sappi Southern Africa Limited
*** Holding company of Sappi Southern Africa Limited
^ Management's intention remains, that it will not call on this receivable in the short term

Investment in Ngodwana energy of ZAR23 million (2018: ZAR23 million) and Shareholder loan of ZAR103 million (2018: ZAR45 million) provided by Sappi Southern Africa. Refer to note 10.

All loans are interest free and repayable on demand.

The amounts outstanding at balance sheet date are unsecured and will be settled in cash. The expected credit loss calculated for related party outstanding balances have been calculated and have been assessed as not material.

28. Related party transactions *(continued)*	**2019 ZAR'millions**	2018 ZAR'millions
Dividends received from equity accounted investee (refer to note 9)	**49**	77

Broad-based Black Economic Empowerment (BBBEE) transaction
Refer to notes 25 for details of the BBBEE transaction.

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

Key management personnel
The details of key management personnel, including emoluments, and participation in The Sappi Limited share schemes are disclosed below:

Group and company					
2019	**Salary ZAR'millions**	****Bonuses and performance related payments granted for the year ZAR'millions**	**Expense allowance ZAR'millions**	**Contributions paid under pension and medical aid scheme ZAR'millions**	**Total ZAR'millions**
Steve Binnie	**7 742**		**213**	**1 181**	**9 136**
Glen Pearce	**4 476**		**121**	**864**	**5 461**
Alex Thiel	**4 669**	**2 720**	**135**	**831**	**8 355**
Pramy Moodley	**2 312**	**939**		**442**	**3 693**
Key management remuneration	**19 199**	**3 659**	**469**	**3 318**	**26 645**
2018					
Steve Binnie	7 287	5 866	194	1 111	14 458
Glen Pearce	4 214	3 785	111	828	8 938
Alex Thiel	4 392	3 178	123	799	8 492
Pramy Moodley	2 011	805		436	3 252
Key management remuneration	17 904	13 634	428	3 174	35 140

** Note: For better consistency fiscal 2019 data shows bonuses granted for the reporting year, rather than prior year as was the practice reported in previous years.

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

Subsidiaries
Details of investments in subsidiaries are disclosed in note 31.

29. Compensation of key management personnel

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

	Allocated price R	Number of shares					
		SR Binnie	A Thiel	G Pearce	P Moodley	**Total 2019**	Total 2018
Outstanding at beginning of year							
Number of shares		664 000	371 000	313 000	71 100	**1 419 100**	1 779 300
A Ordinary shares	72.18	–	–	–	16 200	**16 200**	16 200
Performance shares 39	–	–	–	–	–	**–**	–
Performance shares 40	–	175 000	100 000	85 000	5 000	**365 000**	658 200
Performance shares 41	–	190 000	105 000	90 000	5 900	**390 900**	365 000
Performance shares 42	–	162 000	90 000	75 000	22 000	**349 000**	390 900
Performance shares 43	–	137 000	76 000	63 000	22 000	**298 000**	349 000
Offered and accepted during the year							
Performance shares 43		–	–	–	–	**–**	298 000
Performance shares 44		142 000	79 000	65 000	23 000	**309 000**	–
Vested during the year							
Number of shares		(175 000)	(100 000)	(85 000)	(21 200)	**(381 200)**	(658 200)
Outstanding at end of year							
Number of shares		631 000	350 000	293 000	72 900	**1 346 900**	1 419 100
A Ordinary shares	72.18	–	–	–	–	**–**	16 200
Performance shares 40	–	–	–	–	–	**–**	365 000
Performance shares 41	–	190 000	105 000	90 000	5 900	**390 900**	390 900
Performance shares 42	–	162 000	90 000	75 000	22 000	**349 000**	349 000
Performance shares 43	–	137 000	76 000	63 000	22 000	**298 000**	298 000
Performance shares 44	–	142 000	79 000	65 000	23 000	**309 000**	–

30. Events after balance sheet date

During the quarter ended December 2019, there were numerous fires at multiple plantations. The major fires were at the Venus and Winterton plantations. The combined impact of all the fires resulted in a write-off of 343k tons. Refer to note 22 – Contingent Liabilities for additional events after balance sheet date.

31. Investment in subsidiaries

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

			Effective holding percentage	
	Share capital (Rands)	**Principal activity**	**2019 %**	2018 %
Canonbrae Development Company Proprietary Limited	1 000	Property developments	**63.2**	63.2
Sappi Property Company Proprietary Limited	7 000	Land holdings	**100.0**	100.0

The subsidiaries are immaterial in relation to the company.

Sappi Southern Africa Limited

Notes to the group and company financial statements

for the year ended September 2019 (continued)

32. Segment information

The group and company's reportable segments comprise Dissolving Wood Pulp, Packaging and Specialities Graphics and Forestry and Lomati which is the basis of how the group and company allocates resources and evaluates performance.

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

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

Group	**Dissolving Wood Pulp**		**Packaging & Specialities**		**Graphics[1]**		**Forestry and Lomati**		**Unallocated & Eliminations**		**Group**	
R'millions	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018
External sales including external forestry sales	**11 411**	10 735	**4 960**	4 874	**2 427**	410	**1 154**	991	**61**	158	**20 012**	17 844
Operating profit excluding special items	**2 725**	2 291	**974**	735	**(65)**	8	**(203)**	(79)	**2**	7	**3 433**	2 962

Reconciliation of operating profit excluding special items to profit before taxation:

	Dissolving Wood Pulp		**Packaging & Specialities**		**Graphics[1]**		**Forestry and Lomati**		**Unallocated & Eliminations**		**Group**	
	2019	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018
Operating profit excluding special items	**2 725**	2 291	**974**	728	**(65)**	8	**(203)**	(79)	**2**	7	**3 433**	2 962
Special items* - gains	**–**	–	**–**	–	–	–	–	–	–	**–**	**222**	331
Net finance costs and dividends											**(113)**	85
Profit before taxation											**3 542**	3 378

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Notes to the group and company financial statements

for the year ended September 2019 (continued)

32. Segment information *(continued)*

Company	**Dissolving Wood Pulp**		**Packaging & Specialities**		**Graphics**[1]		**Forestry and Lomati**		**Unallocated & Eliminations**		**Company**	
R'millions	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018
External sales including external forestry sales	**11 411**	10 735	**4 960**	4 874	**2 427**	410	**1 154**	991	**61**	158	20 012	17 844
Operating profit excluding special items	**2 725**	2 291	**974**	735	**(65)**	8	**(203)**	(79)	**2**	(8)	3 433	2947

Reconciliation of operating profit excluding special items to profit before taxation:

	Dissolving Wood Pulp		**Packaging & Specialities**		**Graphics**[1]		**Forestry and Lomati**		**Unallocated & Eliminations**		**Company**	
	2019	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018
Operating profit excluding special items	**2 725**	2 291	**974**	728	(65)	8	(203)	(79)	2	(8)	3 433	2 947
Special items* - gains	**–**	–	**–**	–	–	–	–	–	–	**–**	223	220
Net finance costs and dividends											43	85
Profit before taxation											3 699	3 252

32. Segment information *(continued)*

Reconciliation of segment assets to total assets:

	Group		Company	
	2019 ZAR'millions	2018 ZAR'millions	**2019 ZAR'millions**	2018 ZAR'millions
Net operating assets	**24 724**	21 716	**24 723**	21 716
Deferred tax liabilities	**4 149**	3 979	**4 149**	3 979
Cash and cash equivalents	**1 843**	1 014	**1 843**	1 014
Trade and other payables	**4 251**	3 675	**4 251**	3 674
Derivative financial instruments (included in current liabilities)	**33**	80	**33**	80
Taxation payable	**362**	109	**362**	109
Total assets	**35 362**	30 573	**35 361**	30 572

(1) Graphics updated from printing and writing papers in the prior year

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

The operating results were reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance. During the current year review process the decision was made to adjust the operating segments to better reflect the nature of the business.

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

Sappi Southern Africa Limited

Annexure A – Definitions

for the year ended September 2019

FSC In terms of the Forest Stewardship Council® (FSC®) scheme, there are two types of certification. In order for forest land to achieve C certification, its forest management practices must meet the FSC 10 principles based on environmental, social and economic criteria. Roundwood (logs) with FSC-certification: Sappi Southern Africa Forests FSC C012316 and Sappi Southern Africa Group Scheme FSC – C017054. For manufacturers of forest products, including paper manufacturers like Sappi, Chain-of-Custody (CoC)-certification involves independent verification of the supply chain, which identifies and tracks the timber through all stages of the production process from the tree farm to the end product. Sappi's mills in South Africa are licenced – Ngodwana Mill – FSC C021636, Saiccor Mill - FSC C011012, Stanger Mill – FSC C019831 and Tugela Mill – FSC C012468

ISO Developed by the International Standardisation Organisation ("ISO"), ISO 9000 is a series of standards focused on quality management.

NBSK Northern Bleached Softwood Kraft pulp. One of the main varieties of market pulp, produced from coniferous trees (i.e. spruce, pine) in Scandinavia, Canada and Northern USA.

OHSAS Is an international health and safety standard aimed at minimising occupational health and safety risks firstly by conducting a variety of analyses and secondly by setting standards.

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