

SAPPI LTD
Form 20-F
December 20, 2005
As filed with the Securities and Exchange Commission on December 20, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

☐ REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended October 2, 2005

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 1-14872

SAPPI LIMITED

(Exact name of Registrant as specified in its charter)

Not Applicable

(Translation of Registrant's name into English)

Republic of South Africa

(Jurisdiction of incorporation or organisation)

48 Ameshoff Street
Braamfontein
Johannesburg 2001
Republic of South Africa
(Telephone: +27-11-407-8111)

(Address and telephone number of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

American Depositary Shares, evidenced by
American Depositary Receipts, each representing
1 Ordinary Share

(Title of each class)

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New York Stock Exchange
Ordinary Shares, par value R1.00 per Share*

(Name of each exchange on which registered)

Securities registered or to be registered pursuant to Section 12(g) of the Act.

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

239,071,892 Ordinary Shares

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES ☒ **NO** ☐

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

YES ☐ **NO** ☒

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES ☒ **NO** ☐

Indicate by check mark which financial statements item the registrant has elected to follow.

ITEM 17 ☐ **ITEM 18** ☒

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES ☐ **NO** ☒

* Not for trading but only in connection with the registration of the American Depositary Shares, pursuant to the requirements of the Securities and Exchange Commission.

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OUR USE OF TERMS AND CONVENTIONS IN THIS ANNUAL REPORT

Unless otherwise specified or the context requires otherwise in this Annual Report on Form 20-F (Annual Report):

- references to Sappi , Sappi Group , Group , we , us and our are to Sappi Limited together with its subsidiaries;
- references to southern Africa are to the Republic of South Africa, the Kingdom of Swaziland, the Kingdom of Lesotho, the Republic of Namibia and the Republic of Botswana;
- references to North America are to the United States, Canada and the Caribbean;
- references to Latin America are to the countries located on the continent of South America and Mexico;
- references to Rand , ZAR and R are to South African Rand and references to SA cents are to South African cents, the currency of South Africa;
- references to US dollar(s) , dollar(s) , US\$, \$ and US cents are to United States dollars and cents, the currency of the United States;
- references to euro , EUR and are to the currency introduced at the start of the third stage of the European Economic and Monetary Union pursuant to the Treaty establishing the European Economic Community, as amended by the Treaty on the European Union;
- references to Guilders and NLG are to Dutch Guilders, the former currency of the Netherlands;
- references to Deutsche marks and DEM are to German Deutsche marks, the former currency of Germany;
- references to UK pounds sterling and GBP are to United Kingdom pounds sterling, the currency of the United Kingdom;
- references to m² are to square metres and references to hectares or ha are to a land area of 10,000 square metres or approximately 2.47 acres;
- references to tonnes are to metric tonnes (approximately 2,204.6 pounds or 1.1 short tonnes);
- references to market share are based upon sales volumes in a specified geographic region during the fiscal year ended September 26, 2004; and
- references to the Potlatch acquisition are to the acquisition on May 13, 2002 of Potlatch Corporation's coated fine paper business in an asset purchase. The acquisition included Potlatch's Cloquet, Minnesota pulp and paper mill as well as the brands, order book and working capital of the Cloquet mill and the brands, order book and inventories of Potlatch's Brainerd, Minnesota paper mill for an aggregate purchase price of \$483 million. We did not acquire Potlatch's Brainerd mill, which Potlatch has closed.

Except as otherwise indicated, in this Annual Report the amounts of capacity or production capacity of our facilities or machines are based upon our best estimates of production capacity at the date of filing of this Annual Report. Actual production by machines may differ from production capacity as a result of products produced, variations in product mix and other factors.

Certain market share information and other statements presented herein regarding our position relative to our competitors with respect to the manufacture or distribution of particular products are not

based on published statistical data or information obtained from independent third parties, but reflect our best estimates. We have based these estimates upon information obtained from our customers, trade and business organisations and associations and other contacts in our industries.

Unless otherwise provided in this Annual Report, trademarks identified by ® are registered trademarks of Sappi Limited or our subsidiaries.

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ACCOUNTING PERIODS AND PRINCIPLES

Unless otherwise specified, all references in this Annual Report to a fiscal year and year ended of Sappi Limited refer to a twelve-month financial period. All references in this Annual Report to fiscal 2005, fiscal 2004, fiscal 2003, fiscal 2002 or fiscal 2001 or the year ended September 2005, 2004, 2003, 2002 or 2001 refer to Sappi Limited's twelve-month financial periods ended on October 2, 2005, September 26, 2004, September 28, 2003, September 29, 2002 and September 30, 2001, respectively; references in this Annual Report to fiscal 2006 refer to the period beginning October 3, 2005 and ending October 1, 2006. Our Group annual financial statements included elsewhere in this Annual Report have been prepared in conformity with South African generally accepted accounting principles (South African GAAP or SA GAAP), which differ in certain significant respects from United States generally accepted accounting principles (United States GAAP or US GAAP); see note 42 to our Group annual financial statements included elsewhere in this Annual Report. On May 13, 2002, we acquired the coated fine paper business of Potlatch Corporation. Our Group annual financial statements for the year ended September 2002 include the results for the acquired coated fine paper business since its acquisition.

CURRENCY OF PRESENTATION AND EXCHANGE RATES

We publish our Group annual financial statements and all financial data presented in this Annual Report in US dollars on a nominal (non-inflation adjusted) basis. For information regarding the conversion to US dollars in fiscal 2005, 2004 and 2003, see note 2 to our Group annual financial statements included elsewhere in this Annual Report.

FORWARD-LOOKING STATEMENTS

In order to utilise the Safe Harbor provisions of the United States Private Securities Litigation Reform Act of 1995 (the Reform Act), we are providing the following cautionary statement. Except for historical information contained herein, statements contained in this Annual Report may constitute forward-looking statements within the meaning of the Reform Act. The words believe, anticipate, expect, intend, estimate, assume, positioned, will, may, should, risk and other similar expressions, which are predictions of or indicate future events and future trends which do not relate to historical matters identify forward-looking statements. In addition, this document includes forward-looking statements relating to our potential exposure to various types of market risks, such as interest rate risk, foreign exchange rate risk and commodity price risk. You should not rely on forward-looking statements because they involve known and unknown risks, uncertainties and other factors which are in some cases beyond our control and may cause our actual results, performance or achievements to differ materially from anticipated future results, performance or achievements expressed or implied by such forward-looking statements (and from past results, performance or achievements). Certain factors that may cause such differences include but are not limited to: the highly cyclical nature of the pulp and paper industry; pulp and paper production, production capacity, input costs (including raw materials, energy and employee costs) and pricing levels in North America, Europe, Asia and southern Africa; any major disruption in production at our key facilities; changes in environmental, tax and other laws and regulations; adverse changes in the markets for our products; any delays, unexpected costs or other problems experienced with any business acquired or to be acquired and achieving expected savings and synergies; consequences of our leverage; adverse changes in the South African political situation and economy or the effect of governmental efforts to address present or future economic or social problems; and the impact of future investments, acquisitions and dispositions (including the financing of investments and acquisitions) and any delays, unexpected costs or other problems experienced in connection with dispositions.

These factors are fully discussed in this Annual Report. For further discussion on these factors, see Item 3 Key Information-Selected Financial Data , Item 3 Key Information-Risk Factors , Item 4 Information on the Company , Item 5 Operating and Financial Review and Prospects Operating Results , Item 10 Additional Information Exchange Controls and note 37 to our Group annual financial statements included elsewhere in this Annual Report. You are cautioned not to place undue reliance on these forward-looking statements. These forward-looking statements are made as of the date of the filing of this Annual Report and are not intended to give any assurance as to future results. We undertake no obligation to publicly update or revise any of these forward-looking statements, whether to reflect new information or future events or circumstances or otherwise.

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PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

Selected Financial Data

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The selected financial data set forth below has been derived from our Group annual financial statements and are qualified by reference to, and should be read in conjunction with, our Group annual financial statements and the notes thereto, which are included elsewhere in this Annual Report, and Item 5 Operating and Financial Review and Prospects .

We prepare our Group annual financial statements according to South African generally accepted accounting principles. There are significant differences between these principles and those applied in the United States. You can read about the principal differences in note 42 to our Group annual financial statements included elsewhere in this Annual Report.

	Year Ended September				
	2005	2004	2003	2002	2001
	(US\$ million, except per share and number of shares data)				
Consolidated Income Statement Data:					
South African GAAP:					
Sales(1)	5,018	4,728	4,299	3,729	4,184
Operating (loss) profit(4)	(137)	188	272	402	239
Net (loss) profit(5)	(213)	95	143	217	132
Basic (loss) earnings per share (US cents)(5)	(94)	42	62	94	57
Diluted (loss) earnings per share (US cents)(5)	(94)	42	62	93	56
Dividends per share (US cents)(3)	30	30	29	28	26
United States GAAP:					
Sales(1)	5,018	4,728	4,299	3,729	4,184
Operating (loss) profit(2)(7)	(232)	120	272	402	273
Extraordinary items(2)				6	5
Net (loss) profit(7)	(332)	46	148	237	130
Basic (loss) earnings per share (US cents)(7)	(148)	20	65	103	56
Diluted (loss) earnings per share (US cents)(7)	(148)	20	64	102	56
Dividends per share (US cents)(3)	30	30	29	28	26
Consolidated Balance Sheet Data:					
South African GAAP:					
Total assets(5)	5,708	6,144	5,855	4,752	4,594
Operating assets(4)	5,269	5,576	5,192	4,468	4,046
Total long-term borrowings	1,600	1,693	1,742	1,455	1,012
Shareholders' equity(5)	1,881	2,157	1,983	1,622	1,537
United States GAAP:					
Total assets(7)	5,808	6,419	6,090	4,931	4,766
Operating assets(5)(7)	5,369	5,889	5,465	4,672	4,258
Total long-term borrowings(7)	1,643	1,904	1,869	1,559	1,111
Shareholders' equity(7)	1,579	1,979	1,908	1,581	1,561

Other Information:

South African GAAP:

EBITDA(6)	353	653	667	740	590
Weighted average number of ordinary shares in issue (in million)	225.8	226.3	229.1	230.2	232.8

United States GAAP:

EBITDA(6)(7)	239	570	656	745	618
Weighted average number of ordinary shares in issue (in million)	224.7	225.0	227.6	228.8	231.0

- (1) Sales are defined in note 2 to our Group annual financial statements included elsewhere in this Annual Report.
- (2) Certain items, which are included under Operating profit under SA GAAP, are included under Extraordinary items for US GAAP. For more information refer to note 42 to our Group annual financial statements included elsewhere in this Annual Report.
- (3) The dividends per share were, in each case, declared after the end of the year indicated. For further information on our dividend policy, see Item 8 Financial Information Dividend Policy .
- (4) Operating assets are defined in note 38 to our Group annual financial statements included elsewhere in this Annual Report.
- (5) Net (loss) profit, basic (loss) earnings per share, diluted (loss) earnings per share, total assets and shareholders' equity has been restated under SA GAAP to take into account the requirements of AC 501 Accounting for Secondary Tax on Companies (STC) which became effective from the beginning of the current financial year. The effect on net (loss) profit is a decrease of US\$3 million, US\$4 million and US\$6 million for 2004, 2002 and 2001 respectively. The effect on basic (loss) earnings per share is a decrease of 1 US cents, 2 US cents and 2 US cents for 2004, 2002 and 2001 respectively. The effect on diluted (loss) earnings per share is a decrease of 1 US cents, 2 US cents and 3 US cents for 2004, 2002 and 2001 respectively. The effect on total assets and shareholders' equity is an increase of US\$38 million, US\$38 million, US\$25 million and US\$40 million for 2004, 2003, 2002 and 2001 respectively.
- (6) In connection with the U.S. Securities Exchange Commission (SEC) rules relating to Conditions for Use of Non-GAAP Financial Measures , we have reconciled EBITDA to net profit rather than operating profit and recalculated EBITDA. As a result our definition has been amended to retain non-trading profit/loss and minority interest as part of EBITDA. EBITDA represents earnings before interest (net finance costs), tax, depreciation and amortisation (including fellingings). We use EBITDA as an internal measure of performance and believe it is a useful and commonly used measure of financial performance in addition to operating profit and other profitability measures under SA GAAP or US GAAP. EBITDA is not a measure of performance under SA GAAP or US GAAP. EBITDA should not be construed as an alternative to operating profit as an indicator of the company's operations in accordance with SA GAAP or US GAAP. EBITDA is also presented to assist our shareholders and the investment community in interpreting our financial results. This financial measure is regularly used as a means of comparison of companies in our industry by removing certain differences between companies such as depreciation methods, financing structures and taxation regimes. However, EBITDA is presented on a Group basis, and there are regulatory and contractual limitations on our businesses' ability to transfer funds among each other. We may also incur tax costs with these transfers. As a result, EBITDA generated by one business may not be

available to make payments on borrowings by another business. Different companies and analysts may calculate EBITDA differently, so making comparisons among companies on this basis should be done very carefully. See the Group income statement to our Group annual financial statements included elsewhere in this Annual Report for an explanation of the computation of net finance costs.

(7) Operating (loss) profit, net (loss) profit, basic (loss) earnings per share, diluted (loss) earnings per share, total assets, operating assets, total long-term borrowings, shareholders' equity and EBITDA under US GAAP have been restated for certain changes identified under US GAAP. For more information on this restatement refer to Item 15 of this Annual Report and note 42 to our Group annual financial statements included elsewhere in this Annual Report.

The following table reconciles net (loss) profit to EBITDA.

	Year Ended September				
	2005	2004	2003	2002	2001
	(US\$ million)				
South African GAAP:					
Net (loss) profit	(213)	95	143	217	132
Add back:					
Depreciation and amortisation (fellings)	490	465	395	338	351
Net finance costs	87	110	111	102	92
Taxation	(11)	(17)	18	83	15
EBITDA	353	653	667	740	590
United States GAAP:					
Net (loss) profit	(332)	46	148	237	130
Add back:					
Depreciation and amortisation (fellings)	470	450	385	349	350
Net finance costs	55	93	90	74	92
Taxation	46	(19)	33	85	46
EBITDA	239	570	656	745	618

Risk Factors

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In addition to other information contained in this Annual Report, you should carefully consider the following factors before deciding to invest in our ordinary shares and American Depositary Shares (ADSs). There may be additional risks that we do not currently know of or that we currently deem immaterial based on the information available to us. Our business, financial condition or results of operations could be materially adversely affected by any of these risks, resulting in a decline in the trading price of our ordinary shares and ADSs.

Risks Related to Our Industry.

We operate in a highly cyclical industry, which has in the past resulted in substantial fluctuations in our results.

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The markets for our pulp and paper products are significantly affected by changes in industry capacity and output levels and by cyclical changes in the world economy. As a result of periodic supply/demand imbalances in the pulp and paper industry, these markets historically have been highly cyclical, with volatile pulp and paper prices. The timing and magnitude of price increases or decreases in the pulp and paper market have generally varied by region and by type of pulp and paper.

The selling prices of the majority of the products manufactured and purchase prices of many of our raw materials used generally fluctuate in line with commodity cycles; however, as occurred in fiscal 2005, we may not be able to increase selling prices sufficiently or in time to offset the effects of increased costs,

which has an adverse impact on our profitability. Other than maintaining a high level of pulp integration, no hedging techniques related to our raw materials and products are applied. Movements in prices of pulp and paper products are difficult to predict. Also, there may be periods during which demand for our products is insufficient to enable us to operate our production facilities in an economical manner. A sustained period of weak demand or excess supply would be likely to adversely affect pulp and paper prices which could have a material adverse effect on our operating rates and financial results.

Despite a relatively high level of pulp integration on a Group-wide basis, a significant increase in the prices for pulp or pulpwood could adversely affect our non-integrated and partially integrated operations if they are unable to raise paper prices sufficiently to offset the effects of increased costs.

The majority of our fine paper sales consist of sales to merchants. The pricing of products for merchant sales can generally be changed upon between 30 to 90 days advance notice to the merchant. Sales to converters may be subject to longer notice periods for price changes. Such notice periods generally would not exceed 6 to 12 months. In southern Africa, we have entered into longer-term fixed-price agreements of between 6 to 12 months duration for primarily packaging paper and newsprint sales with domestic customers. Such agreements accounted for less than 5% of consolidated sales during fiscal 2005.

Most of our chemical cellulose (dissolving pulp) sales contracts are multi-year contracts. The pricing is generally based on a formula linked to the NBSK price and reset on a quarterly basis.

For further information, see Item 4 Information on the Company Business Overview The Pulp and Paper Industry .

The markets for pulp and paper products are highly competitive, and many of our competitors have advantages that may adversely affect our ability to compete with them, particularly in North America.

We compete against a large number of pulp and paper producers located around the world. A recent trend towards consolidation in the pulp and paper industry has created larger, more focused pulp and paper companies. Some of these companies benefit from greater financial resources or operate mills that are lower cost producers of pulp and paper products than our mills. We cannot assure you that each of our mills will be competitive. Furthermore, we cannot assure you that we will be able to take advantage of consolidation opportunities which may arise, or that any failure to exploit opportunities for growth would not make us less competitive. Increased competition, including import duties decrease in accordance with the terms of free trade agreements, could cause us to lose market share, increase expenditures or reduce pricing, any of which could have a material adverse effect on the results of our operations. In addition, competition may result in our being unable to increase selling prices of our products sufficiently or in time to offset the effects of increased costs without losing market share, as occurred in Europe in fiscal 2005, which has an adverse impact on profitability.

Our North American business has experienced significant losses in recent years due to competition, and it may face additional competitive challenges to returning to profitability. There was a significant amount of coated fine paper capacity added in China in 2005. Some of this capacity may be exported to the US, depressing domestic operating rates and potentially also depressing prices. While we believe our North American business is competitive compared to our US competitors, the assets of our North American business are small in comparison to new world-scale coated fine paper machines. The cost position of our machines in relation to imports from both Asia and Europe may be less competitive due to a variety of factors including currency, fuel costs, shipping charges, duties and market pulp prices. A significant strengthening of the US dollar in comparison to the euro could attract a significant amount of imports from Europe.

The cost of complying with environmental regulation may be significant to our business.

Our operations are subject to a wide range of environmental requirements in the various jurisdictions in which we operate. We expect to continue to incur significant expenditures and may face operational constraints to maintain compliance with applicable environmental laws, to upgrade equipment at our mills and to meet new regulatory requirements, including those in the United States, South Africa and Europe. Expenditures to comply with future environmental laws and regulations could have a material adverse effect on our business and financial condition.

For further information, see Item 4 Information on the Company Business Overview Environmental and Safety Matters Environmental Matters and Item 5 Operating and Financial Review and Prospects Operating Results .

The availability and cost of Insurance cover can vary considerably from year to year as a result of events beyond our control, and this can result in our paying higher premiums and periodically being unable to maintain the levels or types of insurance carried.

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The events of September 11, 2001, and more recently the Asian Tsunami and hurricanes in the United States have resulted in substantial property damage losses seriously affecting the insurance industry, which has led to significant increases in premiums and self-insured deductibles over the last few years in some of the components of our insurance structure and may lead to future increases.

Although we have successfully placed the renewal of our 2006 insurance cover at rates lower than 2005 and self-insured deductibles for any one property damage occurrence have remained at \$25 million, with an unchanged aggregate limit of \$40 million, we are unable to predict whether past or future events will result in less favourable terms. For property damage and business interruption, there generally does not seem to be cost effective cover available to full value, however, the directors believe that the loss limit cover of \$1 billion should be adequate for what they have determined as the reasonably foreseeable loss for any single claim.

While we believe our insurance provides adequate coverage for reasonably foreseeable losses, we continue working on improved enterprise risk management to lower the risk of incurring losses from uncontrolled incidents. We are unable to assure you that actual losses will not exceed our coverage or that such excess will not be material.

New technologies or changes in consumer preferences may affect our ability to compete successfully.

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We believe that new technologies or novel processes may emerge and that existing technologies may be further developed in the fields in which we operate. These technologies or processes could have an impact on production methods or on product quality in these fields. Unexpected rapid changes in employed technologies or the development of novel processes that affect our operations and product range could render the technologies we utilise or the products we produce obsolete or less competitive in the future. Difficulties in assessing new technologies may impede us from implementing them and competitive pressures may force us to implement these new technologies at a substantial cost. Any such development could materially and adversely impact our revenues or net profits or both.

Consumer preferences may change as a result of the availability of alternative products or of services such as electronic media or the internet, which could impact consumption of our products.

Risks Related to Our Business

Our indebtedness may impair our financial and operating flexibility.

Our ratio of total interest-bearing borrowings to shareholders' equity has improved significantly in recent years, from 142% at September 1999, to 99% at September 2005. At September 2005, our total interest-bearing borrowings were \$1,870 million. While reduction of borrowings is a priority, opportunities to grow within our businesses will continue to be evaluated, and the financing of any future acquisition may include the incurrence of additional indebtedness.

We are subject to South African exchange controls, which partially inhibit the free flow of funds from South Africa and can restrict activities of subsidiaries of the Sappi Group. These exchange controls have affected the geographic distribution of our debt. As a result, acquisitions in the United States and Europe were financed with indebtedness incurred by companies in those regions. The level of our debt has important consequences. For example, our ability to obtain additional financing may be limited, which could limit, among other things, our ability to exploit growth opportunities; a substantial portion of our cash flow from operations may be required to make debt service payments; we are exposed to increases in interest rates because a portion of our debt bears interest at variable rates; we may be more leveraged than certain of our competitors; we may be more vulnerable to economic downturns and adverse changes in our business; and our ability to withstand competitive pressure may be more limited.

In addition, certain of our financing arrangements contain covenants and conditions that restrict the activities of certain Group companies.

Exchange control restrictions may restrict the transfer of funds directly or indirectly between our subsidiaries or between the parent company and our subsidiaries. We may also incur significant tax costs in connection with these transfers of funds. As a consequence, the ability of Sappi Limited or any of our subsidiaries to make scheduled payments on its debt will depend on its financial and operating performance, which will depend on various factors beyond our control, such as prevailing economic and competitive conditions. If Sappi Limited or any of our subsidiaries is unable to achieve operating results or otherwise obtain access to funds sufficient to enable it to meet its debt service obligations, it could face substantial liquidity problems. As a result, it might need to delay investments or dispose of material assets or operations. The timing of and the proceeds to be realised from any such disposition would depend upon circumstances at the time.

Labour agreements are under negotiation at several of our mills.

The Westbrook, Somerset and Muskegon Mills United Steelworkers union contracts that expired in May 2002, June 2003 and August 2005 respectively are under negotiation, and the Cloquet USW contract expires in April 2006. Collective labour agreements have been renegotiated for all sites in Europe during the fiscal 2004, with minor disruption to operations at only one site. At our southern African mills wage negotiations occur annually and in 2005 negotiations were conducted without any industrial action, despite several industry wide wage related strikes. While we hope to reach agreements on new contracts at all affected sites, in the event that agreements cannot be reached and a prolonged work stoppage that results in a curtailment of output ensues at any or all such sites, our business could be adversely affected.

Fluctuations in the value of currencies, particularly the Rand and the euro, in relation to the US dollar have in the past had and could in the future have a significant impact on our earnings in these currencies.

Exchange rates fluctuations have in the past, and may in the future, affect the competitiveness of our products in relation to the products of pulp and paper companies based in other countries.

Fluctuations in the exchange rate between currencies, particularly the Rand and euro, in relation to the US dollar have in the past significantly affected and could in the future significantly affect our earnings.

Since the adoption of the euro by the European Union on January 1, 1999 (when the euro was trading at approximately \$1.18 per euro), it has fluctuated against the US dollar to approximately \$1.20, \$1.23 and \$1.15 per euro at the end of fiscal 2005, 2004 and 2003, respectively. It reached a low of approximately \$0.83 per euro on October 25, 2000 and, on December 7, 2005, was trading at approximately \$1.17 per euro.

In recent years, the value of the Rand against the US dollar has fluctuated considerably. It has moved against the US dollar to approximately R6.37, R6.43 and R7.13 per US dollar at the end of fiscal 2005, 2004 and 2003, respectively. The Rand reached a low of approximately R13.90 per US dollar on December 21, 2001. Since then, it has appreciated and on December 7, 2005 was trading at approximately R6.30 per US dollar.

For further information, see notes 21 and 37 to our Group annual financial statements included elsewhere in this Annual Report and Item 5 Operating and Financial Review and Prospects Operating Results Foreign Exchange, Inflation and Interest Rates .

There are risks relating to South Africa that could affect your investment in our Company.

We are incorporated in South Africa and own operations in southern Africa. As a result, there are risks relating to South Africa, that could affect an investment in our Company. These risks arise from the fact that we are subject to various economic, fiscal, monetary, regulatory, operational and political policies and factors that affect South African companies and their subsidiaries generally. See Item 5 Operating and Financial Review and Prospects South African Economic and Political Environment and Item 5 Operating and Financial Review and Prospects South African Exchange Controls . While certain of these risks, for example regulatory and operational risks, are limited by the fact that in fiscal 2005, 26% of our sales emanated from southern Africa, 45% from Europe and 29% from North America, and 36% of our operating assets were located in southern Africa, 37% in Europe and 27% in North America, in fiscal year 2005 our operations outside southern Africa had an operating loss of \$194 million and our operations in southern Africa had an operating profit of \$57 million.

We face certain risks in dealing with HIV/AIDS which may have an adverse effect on our southern African operations.

There is a serious problem with HIV/AIDS infection among our southern African workforce, as there is in southern Africa generally. Although the HIV/AIDS infection rate of our southern African workforce is significantly lower than the national average, it is expected to increase over the next decade. While we have several programmes designed to mitigate the impact of the disease on our business, the costs and lost workers time associated with HIV/AIDS may adversely affect our southern African operations.

Several customers account for a significant amount of our revenues.

We sell a significant portion of our products to several major customers, including PaperlinX Ltd which acquired Buhrmann Paper Merchant Division in November 2003, Unisource Worldwide Inc. and International Paper Company. Any adverse development affecting our principal customers or our relationships with our principal customers could have an adverse effect on our business and results of

operations. See Item 4 Business Review Marketing and Distribution Sappi Fine Paper Customers and Item 4 Business Review Marketing and Distribution Sappi Forest Products Customers .

Because of the nature of our business and workforce, we are facing challenges in the retention and succession planning of management that could adversely affect our business.

We are facing an aging demographic work profile among our management due to the mature nature of our industry and the rural and often remote location of our mills, together with generally long tenure of employees at the mills. As a result we are likely to experience groups of employees leaving the company within a relatively short space of time of one another and may have difficulty attracting qualified replacements. The potential risks we face are a loss of institutional memory, skills, experience and management capabilities. Although we have put in place a number of initiatives to mitigate this risk, including implementing programs to promote phased retirement and transfer of knowledge, creating flexibility in career and job design and focussing greater effort on succession planning and talent review and effective skills training and leadership development we may be unable to attract and retain sufficient qualified replacements when and where necessary to avoid an adverse impact on our business.

Risks Related to Our Shares

Your ability to sell a substantial number of ordinary shares may be restricted by the limited liquidity of shares traded on the JSE Limited.

The principal trading market for the ordinary shares of Sappi Limited is the JSE Limited (JSE) (formerly the JSE Securities Exchange South Africa). Historically, trading volumes and liquidity of shares listed on the JSE have been low in comparison with other major international markets. In fiscal 2005, 264 million ordinary shares of Sappi Limited were traded on the JSE and 83 million ADSs were traded on the New York Stock Exchange. See Significant shareholders may be able to influence the affairs of our Company , Item 7 Major Shareholders and Related Party Transactions Major Shareholders , Item 9 The Offer and Listing Offer and Listing Details and Item 9 The Offer and Listing Markets .

Significant shareholders may be able to influence the affairs of our Company.

Although our investigation of beneficial ownership of our shares identified only four beneficial owners of more than 5% of our ordinary shares, holding approximately 25.1%, as shown in our shareholders register at September 30, 2005, the five largest shareholders of record, four of which are nominees that hold shares for a multitude of beneficial owners, owned approximately 94.7% of our ordinary shares. See Item 7 Major Shareholders and Related Party Transactions Major Shareholders .

ITEM 4. INFORMATION ON THE COMPANY

HISTORY AND DEVELOPMENT OF THE COMPANY

Sappi Limited is a public company incorporated in the Republic of South Africa. Its principal executive offices are located at 48 Ameshoff Street, Braamfontein, Johannesburg 2001, Republic of South Africa and its telephone number is +27-11-407-8111.

Sappi Limited was founded and incorporated in 1936 in South Africa and is a corporation organised under the Companies Act 61 of 1973 of the Republic of South Africa.

Until 1990, we primarily expanded our operations within southern Africa. Since 1990, we have grown through acquisitions outside of southern Africa. In December 1994, Sappi and a group of financial investors acquired S.D. Warren Company, the market leader in the United States in coated fine paper and a major producer of other speciality paper products. It now conducts business as Sappi Fine Paper North America. In December 1997, we acquired a 91.5% ownership interest in KNP Leykam, the leading European producer of coated fine paper. KNP Leykam now conducts business as Sappi Fine Paper Europe. On May 13, 2002, we acquired Potlatch Corporation's coated fine paper business and have integrated it in Sappi Fine Paper North America.

In December 2004 we acquired 34% of Jiangxi Chenming Paper Company, a joint venture which commissioned in mid-2005 a coated mechanical paper machine, mechanical pulp mill and deinked pulp mill in China.

For information on our principal investments and capital expenditures, see the description of our business in [Business Overview](#) and [Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources](#).

We currently have our primary listing on the JSE and have secondary listings on the New York and London Stock Exchanges.

BUSINESS OVERVIEW

Business Strategy

Our objective for the coming years is to build on our position as the global leader in the coated fine paper market, which was from the beginning of the 1990's one of the fastest growing market sectors in the paper industry, and to explore opportunities across the broad spectrum of coated paper to utilise our experience in paper coating as well as the chemical cellulose (dissolving pulp) market and to support this with a high level of economic pulp integration. These represent our core products and sectors in the paper and forest products industry. We will continue to invest in our southern African businesses which have important market shares. The key elements of our business strategy are and have been as follows:

Strengthen our leadership position in our core businesses through organic growth and selective acquisitions.

We believe that opportunities for further consolidation remain in our sector. We intend to be at the forefront of this consolidation, aiming to strengthen our position in Europe, North America, and eventually Asia. We intend to focus on investment and acquisition opportunities that fit our strategies, that offer a potential return that exceeds our expected cost of capital and that in the medium term are more advantageous than buying back our shares.

Maintain a global presence.

One of Sappi's key strengths is our geographically diverse business base. We have a significant presence in each of Europe, North America and Africa, and a modest presence in Asia. The presence in Europe and North America has been built up over the past ten years, largely through strategic acquisitions. We will continue to pursue a strategy of geographic diversification supported by leading market positions.

Maintain a high level of economic pulp integration.

We intend to maintain a high level of economic pulp integration, which helps reduce the impact of pulp price volatility on our earnings.

Maintain cost efficient asset base and invest to increase efficiency/productivity.

We believe our asset base has some of the lowest cost and most efficient assets in the coated fine paper sector in the world. We maintain a rigorous focus on costs, and actively manage our asset base, including divesting or closing non-performing assets. We have closed 13 paper machines since 1995, including the recent closure of the Number 4 paper machine at Muskegon Mill.

We maintain an investment policy that is focused on high return projects. A significant portion of our investments are designed to increase production capacity, reduce costs and improve product quality.

Drive growth through market focus and innovation.

The Sappi Group operations represent the originators of many of the major innovations in the industry in the last century. We continue to maintain a focus on innovation through our research and development centres in Europe, North America and South Africa and have established multi-regional, multi-discipline teams to ensure that we transfer knowledge throughout the Group and implement best practice and that our research and development efforts are market oriented. We intend to allocate additional resources to marketing, innovation and technology. This includes the recent creation of multi-regional marketing teams and their links with the relevant technology teams.

Through our partnership with a leading global software provider, we are focused on developing unique information technology solutions that satisfy our customers' requirements and production capabilities, resulting in improved service delivery and operational efficiency.

The Pulp and Paper Industry

The paper industry is generally divided into the printing and writing paper segment, consisting of newsprint, groundwood paper and fine paper, and the packaging segment, consisting of containerboard, boxboard and sackkraft.

Long-term, paper and board consumption has grown in line with overall economic growth, but consumption patterns are also influenced by short-term economic developments. Pricing largely is influenced by the supply/demand balance for individual products, which is partially dependent on capacity and inventory levels in the industry. The ability to adapt capacity changes in response to shorter-term fluctuations in demand is limited, as large amounts of capital are required for the construction or upgrade of production facilities and as lead times are long between the planning and completion of new facilities. Industry-wide over-investment in new production capacity has in the past led to situations of significant oversupply, which has caused product prices to decrease. This has been exacerbated by inventory speculation, as purchasers have sought to benefit from the price trend. As a result, financial performance has deteriorated during periods of significant oversupply to again improve when demand has increased to levels that support the implementation of price increases.

In recent years the industry has experienced significant strategic changes. The high costs associated with building new paper mills and establishing and growing market share has led to companies focusing on acquisition, rather than construction, of new capacity. This development has led to a reduction in events of significant dislocations in the supply/demand balance typically associated with the entry of new production capacity into established markets. Another result of this trend has been a greater concentration of production capacity among fewer producers. Many leading industry producers now focus on fewer core grades and have divested non-core assets that are not part of the industry or which have been considered not consistent with long-term strategies. The regional and global market shares of leading producers have increased significantly over the past decade.

The following table shows a breakdown and description of the major product categories Sappi participates in the products in these categories and the typical uses for such products. We have produced and sold each of these products in each of our last three fiscal years.

Major Product Categories	Description and Typical Uses
<i>Fine Paper:</i>	
Coated paper	Higher level of smoothness than uncoated paper achieved by applying a coating (typically clay based) on the surface of the paper. As a result, higher reprographic quality and printability is achieved. Uses include brochures, catalogues, corporate communications materials, direct mail promotions, educational textbooks, luxury advertising, magazine covers and upscale magazines.
Uncoated paper	Uses include business forms, business stationery, general printing paper, tissue and photocopy paper.
Speciality paper	Can be either coated or uncoated. Uses include bags, labels, packaging and release paper for casting textured finishes (e.g., artificial leather).
<i>Packaging products:</i>	
Packaging paper	Heavy and lightweight grades of paper and board primarily used for primary and secondary packaging of fast moving consumer goods, agricultural and industrial products. Products include containerboard (corrugated shipping containers), sack kraft (multi-walled shipping sacks) and machine glazed kraft (grocers bags). Can be coated to enhance barrier and aesthetics properties.
<i>Groundwood products:</i>	
Newsprint	Manufactured from groundwood and bleached chemical pulp. Uses include advertising inserts and newspapers. Demand is highly dependent on newspaper circulation and retail advertising.
Coated groundwood paper	A coated groundwood fibre based paper, primarily used for magazines, catalogues and advertising material. Manufactured from mechanical pulp.
<i>Pulp:</i>	
Paper pulp	Main raw material used in production of printing, writing and packaging paper. Pulp is the generic term that describes the cellulose fibre derived from wood. These cellulose fibres may be separated by mechanical, thermo-mechanical or chemical processes. The chemical processes involve removing the glues (lignins) which bind the wood fibres to leave cellulose fibres. Paper made from chemical pulp is generally termed woodfree. Uses include paper, paperboard and tissue.

Chemical cellulose (dissolving pulp) Manufactured by similar processes to paper pulp, but purified further to leave virtually pure cellulose fibres. Chemical cellulose is used in the manufacture of a variety of cellulose textile and non-woven fibre products, including viscose staple fibre (rayon), solvent spun fibre (lyocell) and filament. It is also used in various other cellulose-based applications in the food, cigarette, chemical and pharmaceutical industries. These include the manufacture of acetate tow microcrystalline cellulose, cellophane, ethers and moulding powders. The various grades of chemical cellulose are manufactured in accordance with the specific requirements of customers in different market segments. The purity of the chemical cellulose is one of the key determinants of its suitability for particular applications with the purer grades of chemical cellulose generally supplied into the speciality segments.

Timber products: Sawn timber for construction and furniture manufacturing purposes.

The following table sets forth selected pulp and paper prices in certain markets for the periods presented.

	Year Ended September		Year Ended September		Year Ended September	
	2005	2004	2005	2004	2003	2002
	Low	High	Low	High	Low	High
Coated Fine Paper						
100 gsm delivered Germany (euro per metric tonne) ⁽¹⁾	845	845	820	855	845	906
60 lb. delivered US (US\$ per short tonne) ⁽²⁾	870	920	735	840	740	755
Uncoated Fine Paper						
50 lb. delivered US (US\$ per short tonne) ⁽³⁾	700	770	575	750	590	730
Paper Pulp						
NBSK (US\$ per metric tonne) ⁽⁴⁾	585	655	540	660	420	560
Chemical cellulose						
92 alpha (US\$ per metric tonne) ⁽⁵⁾	600	780	600	780	500	630

- (1) 100 gsm sheets, Pulp & Paper International (PPI).
- (2) 60 lb. Coated Web, PPI.
- (3) 50 lb. Offset, PPI.
- (4) Northern Bleached Softwood Kraft Pulp CIF Northern Europe, PPI.
- (5) Selected indicative prices, Sappi.

Fine Papers

Our fine paper activities are divided into coated and uncoated fine paper and speciality paper grades. Our coated fine paper market share in the United States, Europe and southern Africa is approximately 24%, 20% and 60%, respectively, making us the largest producer of coated fine paper in the world.

Coated Fine Paper. Coated fine paper has been one of the fastest growing market sectors in the paper industry through the 1980s and 1990s. Major end uses include high-end magazines, catalogues, brochures, annual reports and commercial printing. Coated fine paper is made from chemical pulp and is coated on one or both sides for use where high reprographic quality is required. The majority of coated fine paper production is coated on two sides, permitting quality printing on both sides of the paper. Paper

that is coated on one side is used in special applications such as consumer product and mailing label applications.

Our 2005 North American coated fine paper sales volume was 31% in sheet form and 69% in reel form. The sheet volume is largely influenced by brochure and general commercial printing activities and printers using mainly sheetfed offset lithographic printing processes, which are not particularly seasonal, and corporate annual reports, which result in heaviest demand during the first calendar quarter. Reels volume is heavily influenced by catalogue and text book activity, which results in heaviest demand during the third calendar quarter, and publication printer activity, which is not particularly seasonal. These printers principally use heatset web offset printing processes.

Our 2005 European business sales volumes of coated fine paper were 74% in sheet form and 26% in reels form. Due to the diversity in languages in the European market, the print editions of brochure and general commercial printing activities are considerably smaller than in the US market. This translates into a significantly higher volume in sheets. The seasonal patterns of both sheets and reels are mostly influenced by the catalogue business. This segment has its highest seasonal activity in the spring, when the fashion catalogues come out, and the autumn, when the Christmas catalogues and holiday brochures are printed. Commercial print and publishing business provide a more steady demand in this market.

See Item 5 Operating and Financial Review and Prospects Markets .

Uncoated Paper. Uncoated fine paper represents the largest industry fine paper grade in terms of both global capacity and consumption. Uncoated fine paper is used for bond/writing and offset printing papers, photocopy papers, writing tablets (e.g., legal pads), speciality lightweight printing paper (e.g., bibles) and thin paper.

The market for uncoated paper products generally follows cyclical trends, which do not necessarily coincide with cycles for coated paper but are impacted by capacity changes in uncoated fine paper output levels.

Speciality Paper. The high value-added speciality paper markets in which Sappi Fine Paper operates generally follow trends in the respective end use sectors in addition to changes in production capacity, output levels and cyclical changes in the world economy. Largely due to the highly specialised nature of speciality paper, price fluctuations have historically tended to lag and be less precipitous than price changes in the uncoated fine paper market.

Packaging Products

Our range of forest products comprises a variety of packaging papers produced in southern Africa at the Tugela, Cape Kraft and Ngodwana mills. We are one of the two major suppliers of packaging papers in South Africa.

Packaging Paper. As with fine paper, the market for packaging papers is affected by cyclical changes in the world economy, local economic growth, retail sales and by changes in production capacity and output levels. The southern African containerboard market has been positively affected by gross domestic product growth and corresponding growth in retail sales. Demand for sack kraft is largely driven by the demand for cement, potatoes, sugar and milling products. Sappi's market share was negatively affected by lower priced imported products and production constraints in 2005.

Over the past decade, kraft linerboard prices have ranged from \$325 to \$685 per metric tonne (CIF) in Northern Europe. As of October 2005, kraft linerboard prices were approximately \$448 per metric tonne in Northern Europe. In the southern Africa domestic market, we have entered into medium-term contractual commitments with converters of boxes, sacks and bags. These commitments include certain volume targets and, in some cases, as is customary in the market, fixed prices for periods of 12 months.

Groundwood Products

Newsprint. The Ngodwana mill produces newsprint. The worldwide market for newsprint is a low growth sector in the paper industry and was adversely affected during the early 1990s by substantial increased capacity and stagnating demand from, and cost-cutting measures imposed by, major newsprint end-users. Over the past decade, the price of newsprint has ranged from a low of \$420 per metric tonne in the second quarter of 1992 to a high of \$750 per metric tonne in the fourth quarter of 1995 and the first quarter of 1996. In recent years, a significant increase in industry consolidation has stabilised the newsprint market and reduced segment over-capacity. As a result of the slowing economy, newsprint prices started to decline in the middle of 2001 from a peak of \$625 in April 2001, to a low of \$445 in July 2002. As of October 2005, the price of newsprint (delivered East Coast USA) had increased to approximately \$630 per metric tonne.

Coated Groundwood. Coated groundwood paper, primarily used for magazines, catalogues and advertising materials, has been one of the fastest growing paper grades in the paper industry in recent years. The segment is also one of the most consolidated segments of the paper industry. Demand for coated magazine paper is influenced by magazine circulation and demand for advertising, and by the price difference relative to coated fine paper and to uncoated groundwood paper as substitution between these grades is possible, depending on quality requirements and price levels. Western European producers are the leading producers of coated groundwood globally. Rapid capacity expansion by leading producers in the early 1990s led to volatile pricing and the development of a significant export business from Europe, primarily to North America and Asia. Pricing development has been more stable in the past three years, but prices have declined recently due to weaker demand and the start-up of new capacity in the industry.

Pulp

We produce chemical cellulose, as well as a wide range of paper pulp grades, including groundwood pulp used in newsprint, unbleached kraft pulp, bleached kraft pulp and bleached sulphite pulp.

Paper Pulp. The market pulp industry is highly competitive and is sensitive to changes in industry capacity, producer inventories, demand for paper and cyclical changes in the world economy. The market price per metric tonne of northern bleached softwood kraft (NBSK) pulp, a pulp principally used for the manufacture of fine paper, is a benchmark widely used in the industry for comparative purposes. Over the past decade, the price of NBSK has ranged from \$395 per metric tonne in November 1993 to \$925 per metric tonne in September 1995, only to decline to \$450 per metric tonne by March 1996.

NBSK market pulp prices, which increased steadily through the second half of fiscal 1997, were adversely affected during fiscal 1998 by declining pulp demand resulting from the Asian economic crisis. Pulp prices at the end of 1998 were 22% lower than at the beginning of the year. During the first quarter of 1999, pulp prices remained relatively stable at \$460 per metric tonne, the lowest level since 1993. Since the end of March 1999, pulp prices increased significantly based on improved demand and limited net capacity growth. At the start of the third quarter of 2000, the NBSK market pulp price in Europe reached \$710 per metric tonne. In line with the global economy, pulp demand has been low throughout 2002 and 2003 and price fluctuations have been driven primarily by supply management and the consequent impact on inventories. Accordingly, pulp prices fluctuated considerably with a difference of \$125 per metric tonne between the high and low of the NBSK price during fiscal 2003. The NBSK price fluctuated between \$540 and \$660 in fiscal 2004 compared to \$435 and \$560 in fiscal 2003. Indications are that the pulp market is improving as a result of production discipline and declining market pulp inventories with the NBSK price edging up to \$601 per metric tonne in November 2005.

Market unbleached kraft pulp (UKP) is used in the production of packaging papers, including kraft linerboard and sack kraft and for certain niche products such as oil and air filters. The market price of UKP generally follows the price trends of other paper pulp grades.

Chemical cellulose (dissolving pulp). The viscose staple fibre (VSF) industry which manufactures textile and non-woven fibres is the largest market segment for chemical cellulose. Prices of VSF grade chemical cellulose generally follow those of the European NBSK. Over the past decade, the price of VSF grade chemical cellulose has ranged from a high of over \$1,000 per metric tonne in the fourth quarter of 1995, to a low of \$470 per metric tonne in the second quarter of 2002. During the past year, prices of VSF grade chemical cellulose continued to trend upwards from this 2002 low, reaching a high of \$788 per metric tonne in the quarter ended June 2005 but they have subsequently begun to retreat from that level. Prices of the higher purity chemical cellulose used in applications other than for VSF products tend to be more stable and are largely unrelated to the price of NBSK. The manufacture of cellulose acetate flake (used in the manufacture of acetate tow for cigarette filter tips) is the second largest application for chemical cellulose after viscose staple fibre. The market price for chemical cellulose used for cellulose acetate flake production has increased to levels above \$900 per metric tonne and is set by competitive forces within this specific market.

Timber Products

Our timber products operations are concentrated in South Africa and consist of sawn timber for the building industry and components for the furniture and packaging industry.

Business Review

We are the world's largest producer of coated fine paper, with a market share of approximately 24% in the United States, 20% in Europe and greater than 60% in southern Africa. In addition, we are the world's largest producer of chemical cellulose, with a market share of approximately 15%.

We are a geographically diverse global paper company with significant manufacturing operations on three continents and sales in over 100 countries. During fiscal 2005, we had sales of \$5,018 million, operating loss of \$137 million and net loss of \$213 million. We currently have a paper production capacity of approximately 5.1 million metric tonnes per annum, chemical cellulose production capacity of 600,000 metric tonnes per annum and paper pulp production capacity of 3.4 million metric tonnes per annum.

Our operations are currently structured around two business units (segments):

- Sappi Fine Paper, which has fine paper and related paper pulp businesses in North America, Europe and South Africa. Pursuant to the reorganisation of our North American and European fine paper shareholding, our fine paper interests are now held by Sappi Papier Holding GmbH in Austria; and
- Sappi Forest Products, which produces commodity paper products (newsprint and packaging papers), pulp (including chemical cellulose and hardwood and softwood pulp) and forest and timber products (including pulpwood, sawlogs and sawn timber) for southern Africa and export markets. Sappi Forest Products is based in Johannesburg, South Africa.

We also operate a trading network for the international marketing and distribution of our products outside our core operating regions of North America, Europe and southern Africa. Our trading operation, which we refer to as Sappi Trading, co-ordinates our shipping and other logistical functions for exports from southern Africa, Europe and North America through subsidiaries in South Africa, Europe and in the United States, respectively. All sales and costs associated with Sappi Trading are allocated to the two business units.

The markets for our pulp and paper products are significantly affected by changes in industry capacity and output levels and by cyclical changes in the world economy. For further information, see [Information on the Company Business Overview The Pulp and Paper Industry](#) and [Item 5 Operating and Financial Review and Prospects Operating Results](#).

The chart set forth below represents the operational rather than the legal or ownership structure of Sappi as of November 2005. Units shown are not necessarily legal entities.

The following table sets forth certain information with respect to our operations for, or as at the end of, the year ended September 2005.

	Sappi Fine Paper North America	Europe	South Africa	Sappi Forest Products	Corporate And Other	Total
	(US\$ million, metric tonnes in thousands)					
Sales volume (metric tonnes)	1,433	2,427	317	3,302		7,479
Sales	1,458	2,239	323	998		5,018
Operating profit	(270)	76	(12)	73	(4)	(137)
Operating assets ⁽¹⁾	1,426	1,963	215	1,558	107	5,269

(1) Operating assets as defined in note 38 to our Group annual financial statements included elsewhere in this Annual Report.

SAPPI FINE PAPER

Overview

Sappi Fine Paper is the largest business sector of Sappi and contributed over 80% of our sales in fiscal 2005. It has the capacity to produce 4.2 million metric tonnes of paper per annum at its 15 paper and related paper pulp mills located on three continents. Sappi Fine Paper manages its business in three principal regions: Sappi Fine Paper North America, Sappi Fine Paper Europe and Sappi Fine Paper South Africa. Sappi Fine Paper also manages the Nash mill in the United Kingdom, which operates as a separate business.

The following chart sets forth certain information with respect to the mills and principal products of Sappi Fine Paper as of November 2005.

The following table sets forth approximate annual production capacity with respect to Sappi Fine Paper's products.

	Annual Production Capacity			
	North		South	
	America(1)	Europe(2)	Africa	Total
Production capacity (000s metric tonnes):				
Fine paper				
Coated(3)	1,190	2,585	80	3,960
Uncoated(4)		70	270	340
Total	1,190	2,655	350	4,195
Paper pulp	900	670	160	1,730
Percentage paper pulp integration(5)	102 %	44 %	62 %(6)	65 %

(1) Excludes the Number 4 paper machine and the mothballed pulp mill at Muskegon.

(2) Includes the Nash mill under uncoated.

(3) Includes coated fine paper, coated groundwood paper and speciality papers.

(4) Includes 30,000 metric tonnes of tissue manufactured at the Stanger mill in South Africa and 14,000 metric tonnes of kraft manufactured at the Enstra and Adamas mills in South Africa.

(5) Includes pulp used internally and pulp sold.

(6) Sappi Forest Products provides most of the additional pulp requirements of our South African fine paper operations.

Facilities and Operations

Sappi Fine Paper North America

Sappi Fine Paper North America is a leading producer and supplier of coated fine paper in the United States with a market share of approximately 24%. Sappi Fine Paper North America also produces a variety of other fine paper, including coated speciality paper.

Sappi Fine Paper North America is headquartered in Boston, Massachusetts, and operates four paper mills in the United States in Somerset, Maine; Muskegon, Michigan; Westbrook, Maine; and Cloquet, Minnesota. These four mills have a total annual production capacity of approximately 1.2 million metric tonnes of paper and a capacity of approximately 0.9 million metric tonnes of paper pulp, which represents approximately 102% of Sappi Fine Paper North American pulp requirements. This significantly reduces Sappi Fine Paper North America's exposure to fluctuations in the price of market pulp that are not driven by fluctuations in wood or other major raw material prices. In July 2005, we announced the closure of the Number 4 paper machine and the mothballing of the pulp mill at Muskegon, which had an annual production capacity of 105,000 metric tonnes of paper and 110,000 metric tonnes of pulp, respectively.

Coated paper accounted for approximately 79% of Sappi Fine Paper North America's sales in fiscal 2005. Speciality paper and pulp accounted for the remaining 21%.

The following table sets forth sales by product for our North American operations, including contribution from the closed Muskegon assets.

	Year Ended September		
	2005	2004	2003
Sales (US\$ million):(1)			
Coated fine paper	1,148	1,068	1,061
Speciality paper and other(2)	310	305	323
Total	1,458	1,373	1,384

(1) Includes sales for the Number 4 paper machine at Muskegon mill.

(2) Other consists primarily of market pulp.

For the year ended September 2005, Sappi Fine Paper North America sold approximately 1,433,000 metric tonnes of paper and pulp products. The following table sets forth, as of September 2005, the production capacity, number of paper machines, products, pulp integration and capital expenditures at each of our continuing mills in North America.

Production capacity (000s metric tonnes)	Mill Locations			
	Somerset	Muskegon	Westbrook	Cloquet
Paper	760	170	30	260
Market pulp	70			280
Number of paper machines	3	1	1	2
Products:				
Paper	Coated Fine Paper	Coated Fine Paper	Casting release paper	Coated fine paper
Market pulp	Bleached kraft pulp			Bleached kraft pulp
Percentage pulp integration(1)	87 %	None	None	231 %
Capital expenditures (October 2002-September 2005) (US\$ million)	67	29	16	67

(1) Includes pulp sold to third parties.

Cloquet. The Cloquet mill has two paper machines and an offline coater, producing premium coated paper. The newest machine and coater were installed in 1988 and 1989, respectively. The pulp mill started up by the previous owner in 2000 at a total cost of \$525 million and is the newest pulp mill in the United States. The Cloquet paper machines have an annual production capacity of 260,000 metric tonnes of coated paper, and the state-of-the-art pulp mill has an annual production capacity of 410,000 metric tonnes.

Somerset. The Somerset mill is a low-cost producer and has an annual production capacity of approximately 760,000 metric tonnes of paper and approximately 490,000 metric tonnes of pulp. The pulp mill was built in 1976, and Somerset became an integrated facility with the completion of Paper Machine 1 (PM1) in 1982. Each of the three paper machines at the Somerset facility employs Sappi Fine Paper North America's patented on-line coating and finishing technology. This technology combines the three steps (paper making, coating and finishing) in the manufacture of coated paper into one continuous process. It is well suited for the lightweight coated papers produced at Somerset, because it allows the production of high gloss, consistent quality products at high speeds.

Muskegon. The Muskegon mill consists of one continuing paper machine with an annual winder capacity of approximately 170,000 metric tonnes of text and cover weight coated paper using S