

SAPPI LTD  
Form 6-K  
November 14, 2008

FORM 6-K

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Report of Foreign Private Issuer

Pursuant to Rule 13a-16 or 15d-16

under the Securities Exchange Act of 1934

For the month of November, 2008

Commission file number: 1-14872

SAPPI LIMITED

(Translation of registrant's name into English)

48 Ameshoff Street

Braamfontein  
Johannesburg 2001

REPUBLIC OF SOUTH AFRICA  
(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.

Form 20-F

X

Form 40-F

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Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b) (1):

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b) (7):

Indicate by check mark whether by furnishing the information contained in this Form, the registrant is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes

No

X

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If “Yes” is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-

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## INCORPORATION BY REFERENCE

Sappi Limited's information below is furnished by the Registrant under this Form 6-K is incorporated by reference into (i) the Registration Statements on Form S-8 of the Registrant filed December 23, 1999 and December 15, 2004 in connection with The Sappi Limited Share Incentive Scheme, (ii) the Section 10(a) Prospectus relating to the offer and sale of the Registrant's shares to Participants under The Sappi Limited Share Incentive Scheme, (iii) the Registration Statements on Form S-8 of the Registrant filed December 15, 2004 and December 21, 2005 in connection with The Sappi Limited 2004 Performance Share Incentive Plan and (iv) the Section 10(a) Prospectus relating to the offer and sale of the Registrant's shares to Participants under The Sappi Limited 2004 Performance Share Incentive Plan.

## FORWARD-LOOKING STATEMENTS

In order to utilize the "Safe Harbor" provisions of the United States Private Securities Litigation Reform Act of 1995 (the "Reform Act"), Sappi Limited (the "Company") is providing the following cautionary statement. Except for historical information contained herein, statements contained in this Report on Form 6-K may constitute "forward-looking statements" within the meaning of the Reform Act. The words "believe", "anticipate", "expect", "intend", "estimate", "plan", "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 Report on Form 6-K may include forward-looking statements relating to the Company's potential exposure to various types of market risks, such as interest rate risk, foreign exchange rate risk and commodity price risk. Reliance should not be placed on forward-looking statements because they involve known and unknown risks, uncertainties and other factors which are in some cases beyond the control of the Company, together with its subsidiaries (the "Group"), and may cause the actual results, performance or achievements of the Group 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 material, energy and employee costs, and pricing levels in North America, Europe, Asia and southern Africa; any major disruption in production at the Group's key facilities; changes in environmental, tax and other laws and regulations; adverse changes in the markets for the Group's products; any delays, unexpected costs or other problems experienced with any business acquired or to be acquired; consequences of the Group's 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 and other risks, uncertainties and factors are discussed in the Company's Annual Report on Form 20-F and other filings with and submissions to the Securities and Exchange Commission, including this Report on Form 6-K. Shareholders and prospective investors are cautioned not to place undue reliance on these forward-looking statements. These forward-looking statements are made as of the date of the submission of this Report on Form 6-K and are not intended to give any assurance as to future results. The Company undertakes 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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USE OF TERMS AND CONVENTIONS

Unless otherwise specified or the context requires otherwise herein:

references to “Sappi”, “Group”, “we”, “us” and “our” are to Sappi Limited together with its subsidiaries excluding, unless otherwise indicated, the Acquired Business (as defined below);

references to the “Acquired Business” are to the coated graphic paper business and certain related uncoated graphic paper business activities of M-real Corporation to be acquired by us pursuant to the Acquisition Agreement;

references to the “Acquisition Agreement” are to the Master Business and Share Sale and Purchase Agreement dated September 29, 2008, among M-real Corporation, Sappi, and their respective subsidiaries named therein;

references to the “Proposed Acquisition” are to the acquisition of the Acquired Business pursuant to the Acquisition Agreement;

references to “pro forma” or “pro forma basis” refer to financial or other data which is presented on a pro forma basis after giving effect to the Proposed Acquisition and any related financing;

references to our “annual financial statements” or our “audited financial statements” are to our annual financial statements contained in our annual report on Form 20-F for fiscal 2007;

references to our “interim financial statements” are to our interim financial statements for the nine months and the quarter ended June 2008 contained in our current report on Form 6-K dated August 1, 2008;

references to “IFRS” are to the International Financial Reporting Standards, as issued by the International Accounting Standards Board (“IASB”);

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”, “R”, “SA cents” are to South African Rands and 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 of the European Union;

references to “UK pounds sterling”, “GBP” and “£” are to United Kingdom pounds sterling, the currency of the United Kingdom;

references to “m<sup>2</sup>” are to square meters and references to “hectares” or “ha” are to a land area of 10,000 square meters or approximately 2.47 acres;

references to “tonnes” are to metric tonnes (approximately 2,204.6 pounds or 1.1 short tons);

references to “market share” are, unless otherwise specified, based upon production capacity in a particular market, as compared to the capacity of competitors in that market;

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references to “NBSK” are to northern bleached softwood kraft pulp, frequently used as a pricing benchmark for pulp;

references to “groundwood” or to “mechanical” are to pulp manufactured using a mechanical process, or where applicable to paper, made using a high proportion of such pulp;

references to “woodfree paper” are to paper made from chemical pulp, which is pulp made from wood fiber that has been produced in a chemical process;

references to “PM” are to individual paper machines; and

references to “SARB” are to the South African Reserve Bank.

Except as otherwise indicated, in this document the amounts of “capacity” or “production capacity” of facilities or machines are based upon our best estimates of production capacity at the date hereof. 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 organizations and associations and other contacts in our industries.

Unless otherwise provided herein, trademarks identified by ® are registered trademarks of Sappi Limited or its subsidiaries.

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NOTE REGARDING FORWARD-LOOKING STATEMENTS

Except for historical information contained herein, statements contained herein may constitute “forward-looking statements” within the meaning of the United States Private Securities Litigation Reform Act of 1995.

The words “believe”, “anticipate”, “expect”, “intend”, “estimate”, “plan”, “assume”, “positioned”, “will”, “may”, “should” and 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 risk that the Acquired Business will not be integrated successfully or such integration may be more difficult, time-consuming or costly than expected; that expected revenue synergies and cost savings from the acquisition may not be fully realized or realized within the expected time frame; that revenues following the acquisition may be lower than expected; or that any anticipated benefits from the consolidation of the European paper business may not be achieved;

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, including as a result of adverse changes in credit markets that affect our ability to raise capital when needed;

adverse changes in the political situation and economy in the countries in which we operate 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.

For further discussion on these factors, see “Risk Factors” and note 31 to our Group annual financial statements for the year ended September 2007. You are cautioned not to place undue reliance on these forward-looking statements. These forward-looking statements are made as of the date hereof and are not intended to give any assurance as to future results. We undertake no obligation to 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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ACCOUNTING PERIODS AND PRINCIPLES; PRESENTATION OF INFORMATION

On September 29, 2008, we entered into an agreement with M-real (which is subject to the satisfaction or, where permitted, waiver of certain conditions precedent as further described herein) to acquire the Acquired Business.

With regard to Sappi, unless otherwise specified, all references herein to a “fiscal year” and “year ended” of Sappi Limited refer to a twelve-month financial period. All references herein to fiscal 2007, fiscal 2006 and fiscal 2005, or the years ended September 2007, 2006 or 2005, refer to Sappi Limited’s twelve-month financial periods ended on September 30, 2007, October 1, 2006 and October 2, 2005, respectively. References to the nine months ended June 2008 and 2007 refer to the periods from October 1, 2007 to June 29, 2008 and October 2, 2006 ended July 1, 2007, respectively. References herein to fiscal 2008 refer to the period beginning October 1, 2007 and ending September 28, 2008 and references to fiscal 2009 refer to the period beginning September 29, 2008 and ending September 27, 2009. References to June 2008, September 2008, June 2007, September 2006 and September 2005 represent amounts as at, respectively, June 29, 2008, September 30, 2007, July 1, 2007, October 1, 2006 and October 2, 2005.

Our consolidated annual financial statements have been prepared in conformity with IFRS, which differs in certain respects from United States Generally Accepted Accounting Principles (“US GAAP”). Note 35 to our consolidated annual financial statements includes a reconciliation to US GAAP. As permitted by SEC Release No. 33-8879—Acceptance From Foreign Private Issuers of Financial Statements Prepared in Accordance with International Financial Reporting Standards Without Reconciliation to US GAAP, our financial information for the nine months ended June 2008 and 2007 was prepared in conformity with IFRS and omitted a reconciliation to US GAAP. Likewise, when filed with the SEC, our fiscal 2008 financial statements will be prepared in accordance with IFRS, without reconciliation to US GAAP (comparative financial information for fiscal 2007 and fiscal 2006 presented in our fiscal 2008 financial statements will also omit the reconciliations to US GAAP that were included in our fiscal 2007 and fiscal 2006 financial statements when such statements were originally prepared and filed).

The financial data presented herein with respect to the Acquired Business has been prepared on a “carve-out” basis from the consolidated financial statements of M-real using the historical results of operations, assets and liabilities attributable to the Acquired Business, and include allocations of expenses and assets from M-real. The financial statements for the Acquired Business have been prepared on an annual basis for the years ended December 31, 2007, 2006 and 2005 and on an interim basis for the six months ended June 30, 2008 and 2007 and the three months ended December 31, 2007 and 2006. With regard to the Acquired Business, all references herein to the years ended December 2007, 2006 and 2005 refer to the 12 month periods ended December 31, 2007, 2006 and 2005, respectively. All references herein to the six months ended June 2008 and 2007 refer to the periods ended June 30, 2008 and 2007, respectively. All references herein to the three months ended December 2007 and 2006 refer to the periods ended December 31, 2007 and 2006, respectively. The financial data for the Acquired Business as of and for the nine months ended June 2008 was combined from financial data for the Acquired Business for the three months ended December 2007 and the six months ended June 2008. The financial statements for the Acquired Business have been prepared in conformity with IFRS.

The unaudited condensed combined pro forma financial information presented herein has been derived from our consolidated historical financial statements and the combined financial statements of the Acquired Business.

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CURRENCY OF PRESENTATION AND EXCHANGE RATES

We publish our Group annual financial statements and all financial data presented herein in US dollars on a nominal (non-inflation adjusted) basis. For information regarding the conversion to US dollars in fiscal 2007, 2006 and 2005, see note 2 to our annual financial statements for fiscal 2007.

The pro forma combined financial information herein is presented in US dollars on a nominal (non-inflation adjusted) basis.

For purposes of the preparation of the pro forma combined financial information

the income statement data and cash flow data for the Acquired Business has been converted from euros to US dollars using the average exchange rate (i) for the year ended December 2007 of EUR1 = US\$1.3755, (ii) for the six months ended June 2008 of EUR1 = US\$1.5315, and (iii) for the three months ended December 2007 of EUR1 = US\$1.4556; and

the balance sheet data for the Acquired Business has been converted from euros to US dollars using (i) our June 2008 closing rate of EUR1 = US\$1.5795 for data as of June 2008 and (ii) our December 2007 closing rate of EUR1 = US\$1.4717 for data as of December 2007.

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RISK FACTORS

Risks Related to Our Industry

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

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. In addition, recent turmoil in the capital and credit markets has led to decreased availability of credit, which may have an adverse effect on the world economy and consequently adversely affect the markets for our products. 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.

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. Other input cost increases including energy and chemicals may affect our operations if we are unable to raise paper prices sufficiently.

The majority of our fine paper sales consist of sales to merchants. However, the pricing of products for merchant sales can generally be changed 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 approximately 5% of our sales during the nine months ended June 2008.

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

As a result of the short-term duration of paper and chemical cellulose pricing arrangements, we are subject to cyclical decreases in market prices for these products. A downturn in paper or chemical cellulose prices could have a material adverse effect on our sales or results of operations.

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.

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 a decrease in import duties 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.

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. Although we strive to ensure that our facilities comply with all applicable environmental laws, we have in the past been and may in the future be subject to governmental enforcement action for failure to comply with environmental requirements. 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. Impacts from historical operations, including the land disposal of waste materials, may require further investigation and cleanup. In addition, we could become subject to environmental liabilities resulting from personal injury, property damage or natural resources damage. Expenditures to comply with future environmental requirements and the cost related to any potential environmental liabilities and claims could have a material adverse effect on our business and financial condition.

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For further information, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Environmental Matters”.

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.

Although the insurance market has been stable for the last three to four years, it remains cyclical and catastrophic events can change the state of the insurance market, leading to sudden and unexpected increases in premiums and deductibles and unavailability of coverage due to reasons totally unconnected with our business. In addition, recent turmoil and volatility in the global financial markets may adversely affect the insurance market.

Although we have successfully negotiated the renewal of our 2008 insurance cover, and expect to renew our 2009 cover, at rates similar to those of 2007 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 favorable terms. For property damage and business interruption, there generally does not seem to be cost effective cover available to full value; however, we believe that the loss limit cover of \$1 billion should be adequate for what we have determined as the reasonably foreseeable loss for any single claim.

While we believe our insurance programs provide adequate coverage for reasonably foreseeable losses, we continue working on improved 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 insurance coverage or that such excess will not be material.

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

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 utilize 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 negatively impact consumption of our products.

## **Risks Related to Our Business**

Our indebtedness may impair our financial and operating flexibility.

Our level of indebtedness and the terms of our indebtedness could negatively impact our business and liquidity. On a pro forma basis as of June 2008, our interest bearing debt (long-term and short-term interest bearing debt plus overdraft, less cash on hand) was US\$3,086 million. While reduction of our indebtedness is one of our priorities, opportunities to grow within our businesses will continue to be evaluated, and the financing of any future acquisition or capital investment may include the incurrence of additional indebtedness.

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The level of our debt has important consequences, including:

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;

our ability to withstand competitive pressure may be more limited; and

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

During fiscal 2009, we have approximately US\$827 million of renewable facilities that mature. We expect to be able to continue to refinance these rolling facilities under our existing longer-term funding arrangements and bilateral banking facilities. Other than rolling facilities, the first significant scheduled debt repayment is a €400 million facility maturing in December 2010. We will seek to refinance such indebtedness when it becomes due through the issuance of new debt in the global capital markets.

Our ability to refinance our debt, incur additional debt, the terms of our existing and additional debt and our liquidity could be affected by a number of adverse developments. In the third quarter of fiscal 2007, the global debt markets were subject to significant pressure triggered by the collapse of the sub-prime mortgage market in the U.S. This liquidity crunch has continued through and worsened in calendar 2008, leading to unprecedented volatility in the financial markets, an acute contraction in the availability of credit, including in interbank lending, and the failure of a number of leading financial institutions. Changes in investment markets, including changes in interest rates, exchange rates and returns from equity, property and other investments, could result in worsening general economic conditions. As a result, certain government bodies and central banks worldwide have undertaken unprecedented intervention programs, the effects of which remain uncertain. In addition, since 2006 the Group's credit ratings have been downgraded to sub-investment grade by Standard & Poor's (S&P) and Moody's. These adverse developments in the credit markets and in our credit rating, as well as other future adverse developments, such as further deterioration in the financial markets and a worsening of general economic conditions, may negatively impact our ability to issue additional debt as well as the amount and terms of the debt we are able to issue. Our liquidity will be adversely affected if we must repay all or a portion of our maturing debt from available cash or through use of our existing liquidity facilities. In addition, our results of operations will be adversely impacted to the extent the terms of the debt we are able to issue are less favorable than the terms of the debt being refinanced. It is also possible that we will need to agree to covenants that place additional restrictions on our business.

We are subject to South African exchange controls, which may restrict the transfer of funds directly or indirectly between our subsidiaries or between the parent company and our subsidiaries and can restrict activities of our subsidiaries. We may also incur tax costs in connection with these transfers of funds. 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. As a consequence, our ability or the ability of 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

we or any of our subsidiaries are unable to achieve operating results or otherwise obtain access to funds sufficient to enable us to meet our debt service obligations, we could face substantial liquidity problems. As a result, we might need to delay investments or dispose of material assets or operations. The timing of and the proceeds to be realized from any such disposition would depend upon circumstances at the time.



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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 rate 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, reaching a low of approximately \$0.83 per euro in October 2000 before trading at approximately \$1.42, \$1.27 and \$1.20 per euro at the end of fiscal 2007, 2006 and 2005, respectively, and rising to a high of \$1.60 per euro in April 2008. On November 6, 2008, it was trading at approximately \$1.28 per euro. In recent months, the US dollar has been appreciating against the euro. A significant weakening of the US dollar in comparison to the euro could redirect a significant amount of imports from Europe.

In recent years, the value of the Rand against the US dollar has fluctuated considerably. It has moved against the US dollar from a low of approximately R13.90 per US dollar in December 2001 to approximately R6.89, R7.77 and R6.37 per US dollar at the end of fiscal 2007, 2006 and 2005, respectively. More recently, the Rand has been declining against US dollar and was trading at approximately R9.80 per US dollar on November 6, 2008.

For further information, see notes 2, 21 and 31 to our audited financial statements and “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Currency Fluctuations”.

There are risks relating to the countries in which we operate that could impact our earnings or affect your investment in our Company.

We own manufacturing operations in five countries in Europe, four states in the United States, South Africa and Swaziland, and have an investment in a joint venture in China. These risks arise from being subject to various economic, fiscal, monetary, regulatory, operational and political factors that affect companies generally and which may change as economic, social or political circumstances change. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations—South African Economic and Political Environment”.

Our southern African operations have in recent years accounted for a disproportionate percentage of our operating profits. In fiscal 2007, 45% of our sales originated from Europe, 28% from North America and 27% from southern Africa and 40% of our operating assets were located in Europe, 22% in North America and 38% in southern Africa. However, in fiscal 2007, 23% of our operating profits were from Europe, 6% from North America and 71% from southern Africa. In the nine months ended June 2008, 47% of our sales originated from Europe, 28% from North America and 25% from southern Africa and 42% of our operating assets were located in Europe, 21% in North America and 37% in southern Africa but 16% of our operating profits were from Europe, 22% from North America and 62% from southern Africa. Adverse developments in the economic, fiscal, monetary, regulatory or political circumstances in southern Africa could negatively affect our operations.

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. The HIV/AIDS infection rate of our southern African workforce is expected to increase over the next decade. The costs and lost workers’ time associated with HIV/AIDS may adversely affect our southern African

operations.

For further information, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—South African Economic and Political Environment”.

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The inability to recover increasing input costs through increased prices of our products has had, and may continue to have, an adverse impact on our profitability.

The selling prices of the majority of the products manufactured and the purchase prices of many of the raw materials we use generally fluctuate in correlation with global commodity cycles. In addition, we have been experiencing increasing costs of a number of raw materials due to global trends beyond our control. The global warming and carbon footprint imperatives are causing the increased use of sustainable, non-fossil fuel, sources for electricity generation. Electricity generation companies are competing for the same raw material, namely wood and wood chips, in the same markets as us, driving prices upwards, especially during winter in the Northern hemisphere. In addition, the price of crude oil recently reached historically high levels. Although oil prices have since decreased, they are likely to remain at high levels for the foreseeable future because of, among other things, political instability in the oil producing regions of the world. This impacts the oil-based commodities required by our business in the areas of energy (including electricity), transport and chemicals.

As occurred during the 2006 and 2007 fiscal years, and during the nine months ended June 2008, a major potential consequence of the increase in the price of input commodities is our inability to counter this effect through increased selling prices. This results in reduced operating profit, and has a negative impact on business planning.

While we are in the process of implementing steps to reduce our cost of commodity inputs, other than maintaining a high level of pulp integration, the hedging techniques we apply on our raw materials and products are on a small scale and short term in nature. Moreover, in the event of significant increases in the prices of pulp, our non-integrated and partially integrated operations could be adversely affected if they are unable to raise paper prices by amounts sufficient to maintain margins.

A limited number of customers account for a significant amount of our revenues.

We sell a significant portion of our products to several major customers, including PaperlinX, Igepa, xpedx and Antalis. For Sappi Fine Paper products, PaperlinX and Igepa represented individually more than 10% of our total sales during fiscal 2007 and for the nine months ended June 2008. 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.

Because of the nature of our business and workforce, we are facing challenges in the retention of management and the employment of skilled people 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. We may be unable to attract and retain sufficient qualified replacements when and where necessary to avoid an adverse impact on our business.

Catastrophic events affecting our plantations, such as fires, may adversely impact our ability to supply our southern African mills with timber from the region.

The southern African landscape is prone to, and ecologically adapted to, frequent fires. The risk of uncontrolled fires entering and burning significant areas of plantation is high, but under normal weather conditions this risk is managed through comprehensive fire prevention and protection plans. In 2007 and 2008, southern Africa experienced a number of abnormal weather events (hot, dry conditions fanned by extremely strong winds), which resulted in disastrous

plantation fires across vast areas of eastern South Africa and Swaziland affecting 14,000 hectares and 26,000 hectares, respectively, of our plantations. There is some cause for concern that these abnormal weather conditions may be occurring more frequently as a result of the potential impact of climate change. In addition, because the transformation of land ownership and management in southern Africa has been moving ownership and management of plantations to independent growers, we have less ability to directly manage fire risk, as well as risks of other catastrophic events, such as pathogen and pest infestations. As a consequence, the risk of plantation fires or other catastrophic events remains high and may be increasing. Continued or increased losses of our wood source could jeopardize our ability to supply our mills with timber from the region.

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### Risks Related to the Proposed Acquisition and the Acquired Business

The risks associated with the Proposed Acquisition and the integration of the Acquired Business could have a material adverse effect on our business, financial condition and results of operations. We may not be able to successfully integrate the Acquired Business into our business.

We may experience unforeseen operating difficulties as we integrate the Acquired Business into our existing operations. These difficulties may disrupt our operations and require significant management attention and financial resources that would otherwise be available for day-to-day operations or the ongoing development or expansion of existing operations. The Proposed Acquisition involves risks, including:

unexpected losses of customers or suppliers of the Acquired Business;

challenges in integrating IT systems and administrative services;

difficulties in retaining management and key personnel and in working cooperatively with the employees of the Acquired Business;

difficulties in integrating the financial, technological and management standards, processes, procedures and controls of the Acquired Business with those of our existing operations;

the performance by M-real and its parent company of their obligations under various agreements they will enter with us, including supply agreements;

any inability of our management to cause our best practices to be applied to the Acquired Business;

challenges in managing the increased scope, geographic diversity and complexity of our operations; and

difficulties in mitigating contingent and assumed liabilities.

If we are unable to successfully meet the challenges associated with the Proposed Acquisition, this could have a material adverse effect on our business, financial condition and results of operations.

We may not be able to realize some or all of the anticipated benefits of the proposed Acquisition or there may be delays and unexpected difficulties in realizing such benefits or higher costs.

Our estimates regarding the earnings, operating cash flow, capital expenditures and liabilities of the Acquired Business are based on information currently available to us and may prove to be incorrect. Since we are not involved in the management of the Acquired Business, our assessment of the risks and opportunities may not be accurate. In addition, we may not realize any anticipated benefits of the Proposed Acquisition and may not be successful in integrating the Acquired Business into our existing business.

Achieving the anticipated benefits of the Proposed Acquisition will depend in part upon whether we integrate the Acquired Business in an efficient and effective manner. We may not be able to accomplish this integration process smoothly or successfully.

Although parts of the information herein assume the consummation of the Proposed Acquisition, the consummation is subject to the satisfaction of certain conditions precedent. In addition, we may terminate the Acquisition Agreement if a significant adverse change occurs or is likely to occur prior to completion. Our failure to consummate the Proposed

Acquisition would result in our asset base being smaller than anticipated. Accordingly, we would not realize the anticipated benefits that are based on our completion of the Proposed Acquisition, including the synergies that we expect to realize from the Proposed Acquisition.

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An inability to realize the full extent of the anticipated benefits of the Proposed Acquisition, as well as any delays encountered in the integration process, could have an adverse effect upon our revenues, level of expenses and operating results.

### 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 our ordinary shares is on the exchange operated by the JSE Limited (“JSE”) (formerly known as the Johannesburg Stock Exchange). Historically, trading volumes and liquidity of shares listed on the JSE have been low in comparison with other major international markets. In fiscal 2008, 241 million of our ordinary shares were traded on the JSE and 51 million ADSs were traded on the New York Stock Exchange. The relatively low liquidity of shares traded on JSE Limited could affect your ability to sell ordinary shares. See “—Significant shareholders may be able to influence the affairs of our Company”.

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

Although our investigation of beneficial ownership of our shares identified only two beneficial owners of more than 5% of our ordinary shares, holding approximately 18.1%, as shown in our shareholders’ register at September 26, 2008, the five largest shareholders of record, four of which are nominees that hold shares for a multitude of beneficial owners, owned approximately 96% of our ordinary shares as of that date.

The proposal by the South African Government to replace Secondary Tax on Companies with withholding tax on dividends and other distributions may impact the amount of dividends or other distributions received by our shareholders.

On October 21, 2008, the South African Government tabled a bill containing proposed legislation to replace Secondary Tax on Companies with a 10% withholding tax on dividends and other distributions payable to shareholders for implementation in late 2009, following amendments to some of the existing double tax treaties. This is the second phase in a process that started in October 2007. Although this may reduce the tax payable by our South African operations, thereby increasing distributable earnings, the withholding tax will generally reduce the amount of dividends or other distributions received by our shareholders.

Sales of large quantities of our ordinary shares and ADSs, or the perception that these sales may occur, could adversely affect the prevailing market price of such securities, as could future offerings of our ordinary shares, ADSs or securities exchangeable or exercisable for ordinary shares.

The market price of our ordinary shares or ADSs could fall if large quantities of ordinary shares or ADSs are sold in the public market, or there is the perception in the marketplace that such sales could occur. Subject to applicable securities laws, holders of our ordinary shares or ADSs may decide to sell them at any time. The market price of our ordinary shares or ADSs could also fall as a result of any future offerings we make of ordinary shares, ADSs, or securities exchangeable or exercisable for our ordinary shares, or the perception in the marketplace that these sales might occur. We may make such offerings, including offerings of additional, share rights or similar securities, at any time or from time to time in the future.

As part of the consideration for the Proposed Acquisition we expect to issue 11,159,702 ordinary shares to M-real. We have entered into a lock-up agreement with M-real restricting M-real’s ability to dispose of shares issued to M-real as part of the consideration for the Acquired Business for a period of nine months following the completion of the

Proposed Acquisition. The lock-up agreement contains certain exceptions, including exceptions allowing M-real to dispose, subject to our consent, of any of the shares issued as consideration for the Proposed Acquisition, if the sale proceeds are needed by M-real to avoid triggering a default of a financial covenant to which it is subject, or dispose of any such shares if the sale proceeds are needed by M-real to satisfy a breach of warranty claim or other liability to us in respect of the Proposed Acquisition. In addition, M-real may seek to divest its interest in us after the expiration of the lock-up and any such divestment would result in the sale or distribution of substantial amounts of our ordinary shares. Sales by M-real of our ordinary shares, if substantial, or the perception that such sales may occur and be substantial, could exert downward pressure on the prevailing market prices for our ordinary shares or our ADSs causing their market prices to decline.



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## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis together with our Group annual financial statements, including the notes, and the other financial information included herein. Certain information contained in the discussion and analysis set forth below and elsewhere in this document includes forward-looking statements that involve risk and uncertainties. See "Note Regarding Forward-Looking Statements", "Risk Factors" and notes 2, 12, 15, 17, 21, 22, 23, 25, 26, 28, 29, 31, 35 and 36 to our annual financial statements and notes 8 and 9 to our interim financial statements for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained herein.

Our consolidated financial statements, including the applicable notes thereto, and our consolidated financial information have been prepared in accordance with International Financial Reporting Standards, as issued by the International Accounting Standards Board. We implemented IFRS for the first time in fiscal 2006 and comparative amounts for fiscal 2005 were restated.

Fiscal 2007 and 2006 included 52 accounting weeks, compared to 53 accounting weeks in fiscal 2005. Our fiscal years operate on a 52 accounting week cycle, except every sixth fiscal year which includes an additional accounting week ("additional accounting week").

## Company and Business Overview

We are a global company which through acquisitions in the 1990s has been transformed into one of the global market leaders in coated fine paper. Two acquisitions were pivotal in establishing us as a global company, namely the acquisition in 1994 of S.D. Warren Company, now known as Sappi Fine Paper North America, and the acquisition in 1997 of KNP Leykam, now integrated into Sappi Fine Paper Europe. The fine paper acquisitions have been integrated into a single fine paper business, which operates under the name Sappi Fine Paper. In September 2008, we entered into an agreement to acquire certain assets of M-real's graphic paper business. Further opportunities to grow within core businesses will continue to be evaluated.

Our group is organized into two operating segments: Sappi Fine Paper and Sappi Forest Products. We also operate a trading network, called Sappi Trading, for the international marketing and distribution of chemical cellulose and market pulp throughout the world and of our other products in areas outside the core operating regions of North America, Europe and southern Africa.

Sales by source and destination for the nine months ended June 2008 and fiscal 2007, fiscal 2006 and fiscal 2005 were as follows:

	Sales by Source				Sales by destination			
	Nine Months ended June 2008	2007	2006	2005	Nine Months ended June 2008	2007	2006	2005
North America	28%	28%	29%	29%	29%	29%	30%	30%
Europe	47%	45%	44%	45%	40%	39%	40%	40%
Southern Africa	25%	27%	27%	26%	15%	15%	15%	15%
Far East and others	—	—	—	—	16%	17%	15%	15%
Total	100%	100%	100%	100%	100%	100%	100%	100%

Sappi Fine Paper has a total paper production capacity of 4.4 million tonnes per annum. Our group is one of the global market leaders in the coated fine paper business with a capacity of 3.4 million tonnes of coated fine paper per annum.

On a historical basis our group is approximately 103% integrated on a net basis in terms of pulp usage, meaning that, while some facilities are market buyers of pulp and others are market sellers, in the aggregate we produce slightly more pulp than we use. By region, the southern African operations are net sellers of pulp, Sappi Fine Paper North America sells slightly more pulp than it uses and the European operations are approximately 46% integrated. Approximately 69% of the wood requirements of the South African businesses are from sources either owned or managed. Both the North American and European operations are dependent on outside suppliers of wood for their pulp production requirements. On a pro forma basis, our Group is approximately 92% integrated on a net basis, meaning that we produce slightly less pulp than we use.

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On November 5, 1998, our American Depositary Receipts commenced trading on the New York Stock Exchange. Based on available information, we believe beneficial shareholding by region is as follows:

	September 2008	2007	2006	2005
North America	17%	20%	30%	49%
Europe & elsewhere	14%	7%	10%	10%
Southern Africa	69%	73%	60%	41%
	100%	100%	100%	100%

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Source: Registered addresses and disclosure by nominee companies, excluding the shares owned by a subsidiary of Sappi.

### Principal Factors Impacting on Group Results

Our results of operations are affected by numerous factors. Given the high fixed cost base of pulp and paper manufacturers, industry profitability is highly sensitive to changes in sales prices. Prices are significantly affected by changes in industry capacity and output levels, customer inventory levels and cyclical changes in the world economy. Profitability in the industry is, however, also influenced by factors such as sales volume, the level of raw material, energy, chemicals and other input costs, exchange rates, and operational efficiency.

The principal factors that have impacted the business during the financial periods presented in the following discussion and analysis and that are likely to continue to impact the business are:

- (a) New acquisitions, expansions, restructuring, cost-reduction initiatives, our ability to maintain and continuously improve operational efficiencies and performance, and other significant factors impacting costs;
- (b) cyclical nature of the industry and its impact on sales volume;
- (c) movement in market prices for products and for raw materials and other input costs of manufacturing;
- (d) sensitivity to currency movements and inflation rates; and
- (e) the South African economic and political environment, and environmental matters.

Because many of these factors are beyond our control and certain of these factors have historically been volatile, past performance will not necessarily be indicative of future performance and it is difficult to predict future performance with any degree of certainty.

### Acquisitions, Expansions, Restructurings and Cost-reduction Initiatives

We continually evaluate the performance of our assets by maintaining a focus on profitability and we actively manage our asset base, including by directing or closing non-performing assets and by pursuing an investment policy that is focused on high-return projects. Some of these recent transactions include the following:

#### Completion of the Sappi Saiccor expansion project

In August 2006, we announced the expansion of the capacity at Sappi Saiccor in South Africa, where Chemical Cellulose products are produced. The capacity of the mill was approximately 600,000 tonnes per annum. The expansion has increased such capacity to approximately 800,000 tonnes per annum. Originally scheduled for completion in the first half of 2008, the project was subject to delays and cost increases. Production using the increased capacity commenced in September 2008. On October 27, 2008, a leak of sulfur dioxide gas from a new pipeline occurred at the Saiccor mill expansion. Following all necessary checks, the new plant is expected to be fully operational by mid November 2008. Production at the rest of the Saiccor mill was not affected by the incident.

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### Blackburn mill closure and cessation of production from PM 5 at Maastricht mill

In August 2008 we announced that we had undertaken a review of our European production activities in response to overcapacity and significant input cost pressure, and in accordance with our strategy of maintaining an efficient asset base. In that context, we reached an agreement with labor representatives at our Blackburn mill on September 22, 2008, pursuant to which the mill will be closed on November 12, 2008 unless a buyer can be found before that date. Production at the Blackburn mill stopped on October 17, 2008. We also intend to cease production from PM 5 at our Maastricht mill. Upon closure of our Blackburn mill and cessation of production from PM 5 at our Maastricht mill, our coated graphic fine paper capacity will be reduced by 190,000 tonnes. See “—Liquidity and Capital Resources—Mill Closures, Acquisitions, Dispositions, Impairment and Joint Venture”.

### Acquisition of M-real’s coated graphic paper business

On September 29, 2008, we entered into an agreement with M-real (which is subject to the fulfillment of certain conditions precedent as further described herein) to acquire specific assets of M-real’s graphic paper division.

### Markets

The markets for pulp and paper products are cyclical, with sales prices significantly affected by factors such as changes in industry capacity and output levels, customer inventory levels and changes in the world economy. The pulp and paper industry has often been characterized by periods of imbalances between supply and demand, causing prices to be volatile. Prices also vary significantly by geographic region and product. Coated fine paper, our core product used for many types of publications, is susceptible to the highly cyclical advertising market, a major driver in our business.

### Coated Fine Paper

Paper demand from fiscal 2005 to fiscal 2007, and during the nine months ended June 2008, increased as the upswing in world economic growth and resultant increase in advertising activities resulted in an increase in demand for coated fine papers. Global demand started to decline during the remainder of fiscal 2008 due to a slowdown in the global economy.

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Global Coated Fine Paper Market Balance

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Source: EMGE

The demand to capacity ratio for global coated fine paper increased to approximately 95% in fiscal 2007 and further increased to approximately 96% during the nine months ended June 2008 and to approximately 98% during fiscal 2008 overall. Increases in industry capacity in Europe and North America were limited during this period, with companies reluctant to undertake major new capital projects in these regions due to the poor returns being achieved. Despite global overcapacity, high Asian demand growth rates and availability of funding led to significant coated fine paper capacity additions between fiscal 2000 and fiscal 2006 and this trend has continued during the nine months ended June 2008 in Asia, particularly in China. Announced closures of coated fine paper production capacity of approximately 1.2 million tonnes in Europe and North America are expected to result in a reduction in supply/demand imbalance.

Despite increased demand, operating rates were low in fiscal 2002 through the first half of fiscal 2004 due to excess capacity, causing price erosion in both Europe and North America. Despite the weakening US dollar during this period, net imports into the United States continued to grow, putting further pressure on prices. Prices in North America, however, did start to improve in the latter half of fiscal 2004 due to a sharp increase in seasonal demand. These tight supply/demand conditions in North America continued into fiscal 2005, and more so in fiscal 2006 as inventory throughout the supply chain dropped, giving rise to further price increases. In total, North American apparent consumption, including imports, grew by 8.6% in fiscal 2006 but declined by 7.2% in fiscal 2007. Excluding exports, apparent consumption grew by 4.3% and declined by 3.4% in fiscal 2006 and 2007, respectively. Apparent consumption, including imports, further declined by 9.5% in the nine months ended June 2008, as compared to the corresponding period in 2007, and by 10.1% during fiscal 2008 as compared to fiscal 2007. The decreases in apparent consumption during fiscal 2007 and fiscal 2008 were due to a decrease in advertising activities and printer consumption, and to a significant reduction in imports. Imports of coated fine paper into the United States decreased by approximately 22% during fiscal 2007 as compared to fiscal 2006, and by approximately 30% in the nine months ended June 2008, as compared to the corresponding period in 2007. This decrease, which continued during the remainder of fiscal 2008, was mainly due to a decrease in coated fine paper imports from China. Following the imposition of import duties on certain Asian producers in calendar 2007, Chinese coated fine paper imports were reclassified as coated groundwood paper. As a result, such imports are accounted for statistically as coated groundwood paper rather than coated fine paper.

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Coated fine paper prices in North America increased during fiscal 2008 compared to fiscal 2007, with the largest increase of approximately 35% occurring with respect to No 3 60lb rolls, the grade representing the largest end use of coated fine paper.

In Europe, demand for coated fine paper declined by 1.8% in the nine months ended June 2008 as compared to the corresponding period in the prior year but was flat in fiscal 2008 as compared to fiscal 2007. Demand grew by 1.4% in fiscal 2007, 2.3% in fiscal 2006 and 4.7% in fiscal 2005. Capacity utilization, including exports, was high in fiscal 2007. Despite demand growth or flat demand in the year-on-year comparison and sharp increases in input costs, attempts to increase prices in the European market in fiscal 2007 and in the nine months ended June 2008 were unsuccessful due to intense competition and persisting over-capacity. However, a small increase in coated fine paper prices of approximately 1% occurred during September 2008. Although the relative weakness of the US dollar versus the euro made exports less attractive compared to regional sales, exports from Europe grew by 8% in the nine months ended June 2008 compared to the corresponding period in 2007 and by 3.7% in fiscal 2008 compared to fiscal 2007.

The graph below reflects apparent consumption for the United States and Europe. Apparent consumption is consumption as indicated by mill sales volumes, which ignores the impact of customer inventory and the reclassification of imports. The sales volume to customers is used as the indicator of demand, with the difference between apparent and real demand being the movement in inventories.

US and European Apparent Consumption of Coated Paper

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Source: AF&PA & Cepifine

US short tons converted to tonnes

Average selling prices realized for the Sappi Fine Paper businesses increased by US\$92 per tonne, from US\$972 in the nine months ended June 2007 to US\$1,064 per tonne in the nine months ended June 2008. In the year-on-year comparison, average selling prices increased by US\$94 per tonne, from US\$979 in fiscal 2007 to US\$1,073 per tonne in fiscal 2008. Average prices had increased by US\$38 per tonne, from US\$941 per tonne in fiscal 2006 to US\$979 per tonne in fiscal 2007, compared to US\$1,006 per tonne in fiscal 2005.

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The recent price history for benchmark coated woodfree grades in North America and Europe is shown in the following chart:

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Prices are list prices. Actual transaction prices could differ from prices depicted in graph  
Source: RISI (Resource Information System Inc).

### Coated Fine Paper—North America

Sappi Fine Paper North America's average price realized increased by US\$59 per tonne to US\$1,058 in the nine months ended June 2008 as compared to the nine months ended June 2007. In fiscal 2008, the average price realized increased by US\$68 per tonne, to US\$1,071, as compared to fiscal 2007. These increases were due to a weaker US dollar, reduced supply and a sales and marketing strategy that was more focused on price levels. Sappi Fine Paper North America's average price realized decreased by US\$6 per tonne to US\$1,003 per tonne in fiscal 2007 compared to fiscal 2006, mainly due to competitive import price pressure and changes in product mix. In fiscal 2006, prices in North America decreased to US\$1,009 per tonne from US\$1,017 per tonne in fiscal 2005.

### Coated Woodfree Paper—Europe

Prices in Europe, in the local currency, decreased in the nine months ended June 2008 (€706 per tonne) compared to the nine months ended June 2007 (€721 per tonne), and in fiscal 2008 (€709 per tonne) compared to fiscal 2007 (€722 per tonne), mainly due to increased competition in the market. Despite sharp input cost increases and capacity closures during fiscal 2007, prices in Europe, in the local currency, were relatively flat in fiscal 2007 (€722 per tonne) compared to fiscal 2006 (€724 per tonne), but significantly lower than fiscal 2005 (€732 per tonne). Sales prices in Europe are impacted by the movement in the US\$/euro exchange rate as explained in more detail in the analysis of sales development by region. See “—Financial Condition and Results of Operations—Comparison of the Nine Months ended June 2008 to the Nine Months ended June 2007 and a Comparison of Fiscal 2007, 2006 and 2005—Sales”.

### Coated Magazine Paper—Europe

In fiscal 2006, deliveries by European producers increased by approximately 0.8%, compared to fiscal 2005, primarily due to increased exports to markets outside Europe. Average market prices in Europe increased by approximately 0.7%. The strengthening of the euro against the US dollar depressed the euro-equivalent selling prices for exports. In fiscal 2007, deliveries by producers of coated magazine paper increased approximately 2.3%. The price development in Europe was unfavorable for coated magazine paper, decreasing by 3.2% compared to fiscal 2006. European deliveries of coated magazine paper increased by 1.5% in fiscal 2008 compared to fiscal 2007, while average market prices in Europe increased by 4.4%.



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Pulp

Pulp prices tend to display higher volatility than paper prices. During the period from 1993 to 1995 the price of the benchmark pulp grade, NBSK, ranged from a low of US\$395 (November 1993) to a high of US\$925 per tonne (September 1995). The average NBSK prices for fiscal 2008, the 9 months ended June 2008, fiscal 2007, fiscal 2006 and fiscal 2005 were US\$876, US\$873, US\$764, US\$643 and US\$611 per tonne, respectively. Throughout fiscal 2005, global demand for pulp was low in comparison to fiscal 2006 and fiscal 2007 and price fluctuations were driven primarily by currency movements, inventory movement and non-integrated paper capacity expansion. High pulp demand during fiscal 2007 resulted in the continued increase of pulp prices. The pulp demand during the latter part of fiscal 2007 and for the nine months ended June 2008 remained high as none of the usual seasonal decreases occurred. Pulp demand and prices started decreasing in the remainder of fiscal 2008.

The traditional softwood pulp price premium to hardwood was disrupted in fiscal 2005 as a result of pulp mills shifting from hardwood to softwood production, and hardwood pulp mills closing temporarily. This led to hardwood pulp prices exceeding that of softwood in the final quarter of fiscal 2005. However, during October 2005 softwood price premiums were restored as some softwood mills closed in eastern Canada, while hardwood supply increased during the latter part of fiscal 2005 as an additional 1.9 million tonnes came on stream with large expansions at Hainan Island in China and Veracel in Brazil. As a result, the softwood pulp price premium to hardwood increased considerably during fiscal 2006 and continued to increase through fiscal 2007 and to a lesser extent during the nine months ended June 2008 and the remainder of fiscal 2008.

Since we sell roughly as much pulp as we purchase, fluctuations in market pulp prices have a negligible direct impact on our overall profitability. At a divisional level, pulp prices do, however, affect profitability since Sappi Fine Paper Europe is a net buyer of hardwood pulp and Sappi Forest Products is a net seller of hardwood pulp.

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The price of NBSK and Northern Bleached Hardwood Kraft (“NBHK”) pulp is depicted in the following chart:

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Source: PIX (Index from Forex Indexes Ltd)

Chemical cellulose accounts for the majority of our third-party pulp sales. The chemical cellulose produced at our Saiccor operation in southern Africa (“Saiccor”) is used principally as an input in the production of various synthetic textiles and acetate flake used in the manufacturing of acetate tow for cigarette filter tips.

The movement in price of certain chemical cellulose grades is linked to the price of NBSK. Higher technical specifications allow chemical cellulose to typically trade at a premium to NBSK. Bleached Hardwood Kraft pulp (“BHK”) generally sells at a lower price than NBSK.

We increased chemical cellulose product sales significantly in this sector in fiscal 2004 and maintained these higher volumes in each of the fiscal years through to 2007. While demand for Saiccor’s chemical cellulose remained strong during the nine months ended June 2008, sales during that period were at a lower level as compared to the corresponding period in the prior year, primarily as a result of a shortfall in production volumes. Prices in US dollars have steadily increased year on year from 2005 to 2008.

Significant competitive sources of chemical cellulose supply were recently removed from the industry when Weyerhaeuser closed its 140,000 tonnes per annum Cosmopolis plant in September 2006 and the RGM mill in Indonesia (P.T. Toba) converted production from chemical cellulose to paper grade pulp in May 2008. The capacity of the RGM mill is 180,000 tonnes per annum (tpa). In addition, the Baikalsk mill in Russia (90,000 tpa) switched to producing unbleached kraft pulp during 2008 and the Borregaard mill in Switzerland (120,000 tpa) announced that it would close in December 2008. These closures are balanced by the start-up of an additional 250,000 tonnes per annum at the Bahia pulp mill in Brazil, the conversion of the AV Nackawic mill in Canada (180,000 to 200,000 tpa) to chemical cellulose and the increase in capacity at our Saiccor mill to approximately 800,000 tonnes per annum.

In line with the movement in the NBSK prices, prices for chemical cellulose produced at our Saiccor mill increased in the early part of fiscal 2005, but this trend was reversed later in the year. In fiscal 2006, 2007 and the nine months ended June 2008 our chemical cellulose business, which is 100% export-based, continued to be fully utilized and subsequently achieved strong price growth in 2007 as well as the nine months ended June 2008. We maintained a strong market position in the key Viscose Staple Fiber and Lyocell segments but also posted good sales in the specialty acetate flake and MCC segments.

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## Currency Fluctuations

The principal currencies in which our subsidiaries conduct business are the US dollar (US\$), the euro and the South African Rand (ZAR). Although our reporting currency is the US dollar, a significant portion of our sales and purchases are made in currencies other than the US dollar. In Europe and North America, sales and expenses are generally denominated in euro and US dollars, respectively; however, pulp purchases in Europe are primarily denominated in US dollars. In southern Africa, costs incurred are generally denominated in Rands, as are local sales. Exports, which are denominated primarily in US dollars, from the combined Southern African businesses to other regions represent approximately 39% and 43%, respectively, of sales, in local currency, for the nine months ended June 2008 and 2007. Exports represented 43% of sales for fiscal 2007 (2006: 41%, 2005: 39%).

Our consolidated financial position, results of operations and cash flows may be materially affected by movements in the exchange rate between US dollars and the respective local currencies to which our subsidiaries are exposed. The principal currencies in which subsidiaries conduct business that are subject to these risks are the euro and the Rand. The following table depicts the average and year end exchange rates for the Rand and euro against the US dollar used in preparation of our financial statements in the nine months ended June 2008 and 2007, fiscal 2007, fiscal 2006 and fiscal 2005:

Exchange Rates	Nine Months ended June 2008	Nine Months ended June 2007	2007	2006	2005
Period end rate : US\$1=ZAR	7.9145	7.0393	6.8713	7.7738	6.3656
Average rate YTD : US\$1=ZAR	7.3236	7.2121	7.1741	6.6039	6.2418
Period end rate : EUR1=US\$	1.5795	1.3542	1.4272	1.2672	1.2030
Average rate YTD : EUR1=US\$	1.5071	1.3178	1.3336	1.2315	1.2659

Source: audited financial statements of Sappi Limited.

US\$1 = ZAR, Euro 1 = US\$.

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### Euro and Zar Exchange Rate Movement against USD Daily Rate January 1999 to June 2008

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Source: Saint Louis Federal Reserve.  
US\$1 = ZAR, Euro 1 = US\$.

The profitability of certain of our southern African operations is directly dependent on the Rand proceeds of the US dollar exports. Prices in the local South African market are also influenced by pricing of imports.

The translation, from local currency to US dollars, of our results for reporting purposes, tends to distort comparisons between financial periods when currencies are volatile. In the nine months ended June 2008, the US dollar decreased to an average of US\$1.50/Euro, from an average of US\$1.31/Euro in the nine months ended June 2007 and the Rand decreased to an average of ZAR7.32/US\$, from an average of ZAR7.21/US\$ in the nine months ended June 2007. The impact on sales for the nine months ended June 2008 was to increase sales by US\$239 million compared to the same period in fiscal 2007. The euro strengthened substantially against the US dollar in fiscal 2007 (from an average US\$1.23/Euro in fiscal 2006 to US\$1.33/Euro in fiscal 2007), while the Rand weakened on average against the US dollar in fiscal 2007 (from an average ZAR6.60/US\$ in fiscal 2006 to an average ZAR7.17/US\$ in fiscal 2007). The impact of exchange rates in fiscal 2006 was to reduce sales by US\$137 million. This is referred to as the currency translation effect in the following discussion of the financial condition and results of operations. For a more detailed discussion of these impacts see “—Financial Condition and Results of Operations”.

### Inflation and Interest Rates

South African prime overdraft interest rates declined in fiscal 2005 (10.5%) and remained at those levels until April 2006. The rate then increased during the remainder of fiscal 2006 (11.5%), fiscal 2007 (13.5%) and nine months ended June 2008 (15.5%). South African interest and inflation rates can be influenced by a variety of factors, including currency exchange rates. The Rand on average decreased against the US dollar during fiscal 2007 moving from an average of ZAR6.60/US\$ in fiscal 2006 to an average of ZAR7.17/US\$ in fiscal 2007 (fiscal 2005: ZAR6.24/US\$). The Rand on average further decreased to an average of ZAR7.32/US\$ in the nine months ended June 2008 from an average of ZAR7.21/US\$ in the nine months ended June 2007. The year end closing rate strengthened from ZAR7.77/US\$ in fiscal 2006 to ZAR6.87/US\$ in fiscal 2007. Partly due to the weaker Rand during fiscal 2007 and fiscal 2006, the South African inflation rate increased from 4.4% in fiscal 2005 to 5.4% in fiscal 2006 and at the end of fiscal 2007 it was 7.2%. This increase is also largely due to the effect of the impact of higher oil prices on the South African economy. The South African Reserve Bank (SARB) increased its repurchase rate in fiscal 2006 to 8%, further increases were implemented during fiscal 2007 closing at 10% at our fiscal year end. As at the end of June 2008, the South African inflation rate was 11.6% and the repurchase rate had increased to 12%. The repurchase rate is the rate at which the SARB lends assistance to the banking sector and therefore represents the cost of credit to the banking sector. When the repurchase rate is changed, the interest rates on overdrafts and other loans extended by the banks also change. In this way the SARB indirectly affects interest rates in the economy. Although South African interest rates impact the cost of our South African borrowings, the majority of our borrowings have been incurred by subsidiaries outside southern Africa, denominated in either US dollars or euros.

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Source: Standard Bank South Africa.

In the US and Europe, inflation rates have been relatively stable in recent years, and accordingly had a lesser impact on our North American and European businesses. Please see table below depicting the United States three-month Libor.

Annual Average US\$ Three-Month Libor

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The three-month Euribor interest rate in Europe is depicted below. The interest rates in the United States and Europe continue to represent a significant interest rate differential when compared to South Africa's 12.0% repurchase rate as determined by the SARB. As of June 2008, this differential between South Africa's repurchase rate and the interest rates in the US and Europe was 9% and 7%, respectively.

### Annual Average European Three-Month Euribor

We borrow in the currencies of the countries in which we invest. As a result, finance costs are related to the location of activities and not the domicile of our Group.

Our foreign exchange policy consists of the following principal elements:

External borrowings are taken up in the functional currency of the operating company concerned and, if not, then the exposure is hedged. Where appropriate we aim, in accordance with IFRS, to apply hedge accounting treatment to avoid volatility in our results due to mark-to-market effects of such hedging instruments.

Any debtors or creditors not in the operating currency of the mill are hedged. Sales are hedged from the time of invoicing, purchases from the time of the approval of the capital expenditures in the case of capital expenditures, and other purchases are hedged, in most instances, at the time the order is placed.

Exposures are hedged through our central treasury, where external hedging instruments are contracted after netting the various Group exposures.

Variations in this policy are considered from time to time, but any deviations from the central treasury policy are always subject to prior approval.

No speculative positions are permitted.

Our group has a current policy of not hedging translation risks. The South African and European operations use the Rand and the euro as their respective functional currencies. Any translation of the value of these operations into US dollars results in foreign exchange translation differences as the Rand and the euro exchange rates move against the US dollar. These changes are booked to the foreign currency translation reserve account. We prefer not to hedge this exposure with financial instruments, as these result in cash settlements which impact results on a permanent basis. Borrowings taken up in a currency other than the functional currency of the borrowing entity are specifically hedged with financial instruments, such as currency swaps and forward exchange contracts.

With regard to interest rate swaps, hedge accounting is permitted when the hedging relationship between the hedging instrument and the underlying debt meets the relevant requirements of IFRS. For example, we have entered into hedging relationships to swap the fixed rate on our outstanding public bonds to a variable rate.

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### South African Economic and Political Environment

Sappi Limited is a public company incorporated in South Africa. We have significant operations in South Africa, which accounted for 71% of our operating profit in fiscal 2007 and 62% of our operating profit in the nine months ended June 2008.

South Africa features a highly developed, sophisticated “first world” infrastructure at the core of its economy. Econometrix, a provider of economic analysis and forecasting for the South African economy, forecasts the South African GDP to grow by 3.7% and 3.0%, respectively, in calendar 2008 and calendar 2009. South Africa’s long-term foreign currency investment ratings have remained constant over the last year at Baa1 from Moody’s Investor Services Inc. and BBB+ from Standard & Poor’s Rating Service (“S&P”). Exchange controls regulations have not been amended during fiscal 2008 and are not expected to be amended in the short term. South African companies remain subject to restrictions on their ability to raise and deploy capital outside of the southern African Common Monetary Area. South Africa achieved 14 years of democracy in calendar 2008; however, the country continues to face challenges in overcoming substantial differences in levels of economic and social development among its people. Access to land, poverty, unemployment, crime and a growing prevalence of HIV/AIDS are some of the social and economic factors that affect businesses operating in this country.

The Restitution of Land Rights Act (Act 22 of 1994), as amended, provides for the restoration of rights in land or other equitable redress to persons or communities dispossessed of their land rights after June 19, 1913 as a result of old laws or practices discriminating on the basis of race. The legislation empowers the Minister of Land Affairs to expropriate land in order to restore it to a successful claimant provided that there is just and equitable compensation to the owner of the land. Claims under the Act were required to be filed on or before December 31, 1998 and are presently being processed by the Commission on Restitution of Land Rights and adjudicated upon by the Land Court. This process is expected to continue for many years. As one of the largest land owners in South Africa, we anticipate that a substantial number of claims may affect land we own. The process of determining the extent of claims filed in respect of our land and the potential impact of these claims on our South African operations continues. The total number of land claims against us is 64, of which 27 in Mpumalanga and 37 in Kwa Zulu-Natal. Four of these claims are in the process of being settled in Kwa Zulu-Natal. The remaining claims have not been finalized and are still under investigation by the Regional Land Claims Commissioner.

The southern African region has one of the highest infection rates of HIV/AIDS in the world. In 1992, we started a program to address the effects of HIV/AIDS and its impact on our employees and our business. Our aim is to ensure that our program prevents new infections and to treat the HIV/AIDS positive employees. Each operating unit has an elected HIV/AIDS committee and a workplace HIV/AIDS prevention program which are adapted to suit the needs of each particular business unit and to ensure that they are active owners and managers of their programs. Each Sappi operation in southern Africa has also identified the relevant role players in their geographical area and is working with them on the implementation of a comprehensive HIV/AIDS program, eliminating duplication and making optimum use of relevant resources through private-public partnerships. To ensure that our program remains current, we are members of the Global Business Coalition on HIV/AIDS (“GBC”) and of the South African Business Coalition against HIV/AIDS (“SABCOHA”). The GBC is a global partnership and SABCOHA is a national partnership focused on developing an integrated strategy for dealing with HIV/AIDS.

Following two previous anonymous, voluntary prevalence tests, a third comprehensive voluntary study was initiated in 2007 in all of our southern African operations. Based on a participation rate of greater than 80%, at the locations tested, we estimate that the overall infection rate in our southern African operations is approximately 14%, which is well below the national average. Similar studies conducted in 2008 confirmed an infection rate of approximately 14%.

Our HIV/AIDS response strategy places special emphasis on testing and counseling to ensure that staff is informed with regard to their HIV/AIDS status to enable them to make informed decisions as to their life choices. Since August 2002, our medical care for employees has included treatment to prevent mother to child transmission. Anti-retroviral treatment has been offered to HIV-infected permanent employees from the beginning of 2003. More recently, special focus has been given to the identification of the environmental risks that could lead to an increase in the prevalence of HIV in the company. We have also extended our voluntary counseling and testing (“VCT”) programs, and are offering an HIV test to every employee who visits the clinics for a medical examination. We estimate that approximately 50% of our employees that are HIV/AIDS positive participate in our HIV/AIDS management program, which is an improvement on the prior year’s participation rate.



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The government and organized business have taken a number of steps in recent years to increase the participation of Black people in the South African economy. To this end, the Employment Equity Act (No. 55 of 1998), the Skills Development Act (No. 97 of 1998) and the Preferential Procurement Policy Framework Act (No. 5 of 2000) were promulgated. The Broad-Based Black Economic Empowerment Act (No. 53 of 2003) has formalized the country's approach to distributing skills, employment and wealth more equitably between races and genders. Broad-Based Black Economic Empowerment ("BBBEE") focuses on increasing equity in ownership, management and control of businesses, and improving Black representation in all levels of employment. It also promotes the development of skills within a business, the nurturing of Black entrepreneurship through preferential procurement and enterprise development, and the uplifting of communities through social investment.

More recently, our South African businesses have actively participated in the drafting of a transformation charter for the South African forestry industry. This charter sets the objectives and principles for BBBEE, and includes the scorecard and targets to be applied within the industry, as well as certain undertakings by government to assist the forestry industry to achieve its BBBEE targets. This Forestry Charter has been signed in May 2008 but has not been gazetted. Until such time as it is formally gazetted as a Transformation Charter and Sector Code in terms of sections 12 and 10 of the Broad-Based Black Economic Empowerment Act (No. 53 of 2003), the South African business will continue to be evaluated against the generic BBBEE scorecard, based on guidelines set out in the Codes of Good Practice published by the Department of Trade and Industry.

In 2006, we achieved an overall BBBEE rating of BBB (BB rating in 2005) as verified by Empowerdex, a leading external BBBEE rating agent. In February 2007, the BBBEE scorecard as set out in the Codes of Good Practice published by the Department of Trade and Industry was streamlined and simplified without affecting their intended objectives. The South African businesses' BBBEE scorecard was evaluated in December 2007. Based on this revised generic BBBEE scorecard, we achieved an overall BBBEE status of a "level seven contributor" (B rating) with preferential procurement recognition level of 50%. As a result, 50% of the value of all purchases from our South African businesses qualify as preferential procurement spend in a customer's BBBEE scorecard. New BBBEE targets have been set for 2010 and 2013. In addition to the generic scorecard, the Forestry Charter will set out further qualifying criteria for companies associated to the forestry industry.

We will consider and are pursuing empowerment transactions where they add to the value of our business and meet our empowerment criteria.

The representation of Black people, particularly Black women, in management and all levels of employment within the company is a focus within the organization, driven by employment equity targets set in each occupational category. Skills development initiatives, particularly programs aimed at improving management and leadership skills, are geared to meet these targets. Where practical, we purchase goods and services from Black-owned businesses and seek opportunities to develop future Black vendors. We are committed to the support of our Project Grow, which is an initiative with local communities using their land for plantations while training them in the core principles of forestry management. This is achieved through financial and technical input, as well as by providing a secure market during the start-up phase of these small tree farming enterprises. This initiative has been extended to encourage aspirant tree farmers who wish to undertake forestry activities on a larger scale. We have a number of enterprise development initiatives and have established programs to train new entrepreneurs. These initiatives involve the transfer of business skills, technical assistance, financial support and preferential payment terms to assist new enterprises to enter the market. We have a history of investment in the communities in which we operate. Initiatives to promote education, health and welfare, arts and culture, and rural and community development, amongst others, are regularly undertaken.

The South African constitution guarantees ownership rights of assets, and it is the stated intent of the constitution that transfer of ownership will occur at market prices. It should be noted that BBBEE equity participation need not necessarily occur at the corporate level, and can be effected at divisional, business unit or lower levels. Because the

BBBEE Act sets forth a framework for plans rather than specific requirements or goals, it is not possible to predict whether or how our business or assets may be impacted.

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## Environmental Matters

We operate in an industry subject to extensive environmental regulations. Typically, we do not separately account for environmental operating expenses but do not anticipate any material expenditures related to such matters. We do separately account for environmental capital expenditures. See note 34 to our audited financial statements for a discussion of these matters.

## Financial Condition and Results of Operations

The operations of our Group are organized into two main business units:

- I. Sappi Fine Paper (“SFP”), which consists of Sappi Fine Paper North America (“SFPNA”), Sappi Fine Paper Europe (“SFPE”) and Sappi Fine Paper South Africa (“SFPSA”); and
- II. Sappi Forest Products (“FP”), which consists of Sappi Kraft (“Kraft”), Saiccor and Sappi Forests (“Forests”). Kraft and Saiccor are jointly referred to as the Pulp and Paper business of FP and Forests comprises the forests business for purposes of this discussion and analysis. The volume, revenue and cost relationship within the Forests business is substantially different to that of the pulp and paper business.

Corporate includes all other non-manufacturing and trading sectors of the business not included in our two main business units.

The analysis and discussion which follows should be read in conjunction with our consolidated financial statements.

Comparison of the Nine Months ended June 2008 to the Nine Months ended June 2007 and a Comparison of Fiscal 2007, 2006 and 2005

## Overview

This overview of our Group’s operating results is intended to provide context to the detailed discussion and analysis which follow. General trends are highlighted with detailed discussions and analysis in separate sections below. The key indicators of our Group’s operating performance are:

Key Figures	Nine Months ended June 2008	Nine Months ended June 2007	2007 (Tonnes '000)	2006	2005
Sales volume	5,093	5,083	6,863	7,199	7,479
			(US\$ million)		
Sales value	4,344	3,882	5,304	4,941	5,018
Operating profit/(loss)	289	296	383	125	(109)
Net income/(loss)	134	127	202	(4)	(184)
Basic EPS (US cents)	59	56	89	(2)	(81)

Operating profit in the nine months ended June 2008 was US\$289 million compared to US\$296 million in the nine months ended June 2007, US\$383 million in fiscal 2007, US\$125 million in fiscal 2006 and a loss of US\$109 million in fiscal 2005. From fiscal 2005 to fiscal 2007, operating profit has shown improvement in year-on-year comparisons due to volume improvement in North America and Europe, but mainly due to price realisation in North America and

South Africa and the positive impact of exchange rates on the translation of European results into US\$. Certain items, either by their nature or due to their magnitude relative to other periods, have significantly impacted the results in fiscal 2007 and fiscal 2006 or negatively impacted fiscal 2005. These items will be dealt with in the relevant section of this discussion and analysis.

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Segment contributions to operating profit are as follows:

	Nine Months ended June 2008 Variance			Nine Months ended June 2007		2007 Variance			2006 Variance			2005
Operating Profit/(Loss)	Value	Value	%	Value	Value	Value	%	Value	Value	%	Value	
(US\$ million, except percentages)												
Fine Paper												
North												
America	62	49	377	13	22	38	—	(16)	243	—	(259)	
Europe	47	(24)	(34)	71	88	115	—	(27)	(111)	(132)	84	
South Africa	5	(1)	(17)	6	9	15	—	(6)	5	—	(11)	
Total	114	24	27	90	119	168	—	(49)	137	—	(186)	
Forest												
Products	167	(45)	(21)	212	264	89	51	175	92	111	83	
Corporate	8	14	—	(6)	—	1	—	(1)	5	—	(6)	
Total	289	(7)	(2)	296	383	258	206	125	234	—	(109)	

Operating profit for the nine months ended June 2008 as compared to the nine months ended June 2007 decreased primarily due to a poorer performance in Europe and South Africa, partly offset by an improved performance in North America. The decrease in operating profit for the nine months ended June 2008 when compared to the nine months ended June 2007 was due primarily to significantly increased variable costs (US\$330 million) and fixed costs (US\$96 million) and a less positive fair valuation of plantation adjustment (US\$46 million), partly offset by higher sales (US\$462 million) in all regions. Increased sales were attributable to a volume increase at Sappi Fine Paper, and, to a greater extent, to price increases in North America and South Africa and the positive impact of exchange rates on the translation of European results into US\$. The US\$330 million increase in variable costs was due primarily to an increase in delivery (US\$43 million), wood (US\$60 million), energy (US\$91 million) and pulp (US\$130 million) costs. Fixed costs increases (US\$96 million) were mainly attributable to increased personnel (US\$76 million) and maintenance (US\$17 million) costs. Cost increases reflect the adverse impact of increases in global commodity prices, particularly oil. Operating profit in fiscal 2007 compared to fiscal 2006 was favorably impacted by the significantly improved performances in all segments of the business. The major contributor to the improved performance was the improvement in sales, partly offset by some cost escalations. Of the US\$363 million improvement in sales in fiscal 2007, US\$123 million was attributable to volume improvements, US\$179 million to price improvement and US\$61 million due to the impact of exchange rates on reporting in US\$. The major drivers of these changes are dealt with in more detail below.

The underlying reasons for the movement in our operating profit can be explained as follows:

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Movements in the sales and variable and fixed cost components of the movement in operating profit are explained below. The items not dealt with in separate sections are as follows:

**Plantation fair value:** This relates to the fair value adjustment of the timber assets of the Forestry operation of Forest Products. There is a fair value pricing and volume or growth component to the adjustment. The movement on this item is mainly impacted by timber selling prices, value of standing timber and costs of harvesting and delivery, the estimated growth rate or annual volume changes and discount rates applied. The parameters applied are all market related. Plantation values increased by US\$67 million in the nine months ended June 2008, compared to an increase of US\$113 million for the corresponding period in fiscal 2007. The increase was US\$130 million positive in fiscal 2007, US\$104 million positive in fiscal 2006 and US\$118 million positive in fiscal 2005.

**Impairment:** In fiscal 2005, impairment charges were US\$182 million in SFPNA, and US\$49 million in Forest Products for a total of US\$231 million. During fiscal 2006, Forest Products, due to the improved performance of the mill, reversed the impairment of the Usutu mill resulting in a credit to profit of US\$40 million. This resulted in an improvement of reported profitability from fiscal 2005 to fiscal 2006 of US\$271 million due to changes to impairment charges.

**Sale of Nash:** The SFPE Nash mill was closed in May 2006 and the operations were transferred to other operations in our Group. The mill property was sold during fiscal 2007 and realized a profit of US\$26 million.

**Fire damage:** During July and August 2007 the forestry operations of Forest Products experienced devastating fires across a wide area of afforested land. The cost of fighting these fires and of the forest destroyed, net of salvage, was US\$17 million.

## Sales

## Group

	Nine Months ended June 2008 Variance			Nine Months ended June 2007		2007 Variance		2006 Variance			2005
Sales	Volume	Volume	%	Volume	Volume	Volume	%	Volume	Volume	%	Volume
	(Tonnes '000, except percentages)										
Fine Paper											
North											
America	1,164	56	5	1,108	1,506	80	6	1,426	(7)	—	1,433
Europe	1,918	58	3	1,860	2,493	43	2	2,450	23	1	2,427
South Africa	246	(14)	(5)	260	350	22	7	328	11	3	317
Total	3,328	100	3	3,228	4,349	145	3	4,204	27	1	4,177
Forest Products											
Pulp & Paper	1,039	(28)	(3)	1,067	1,484	14	1	1,470	(95)	(6)	1,565
Forestry	726	(62)	(8)	788	1,030	(495)	(32)	1,525	(212)	(12)	1,737
Total	1,765	(90)	(5)	1,855	2,514	(481)	(16)	2,995	(307)	(9)	3,302
Total	5,093	10	—	5,083	6,863	(336)	(5)	7,199	(280)	(4)	7,479



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	Nine Months ended June 2008			Nine Months ended June 2007
	Variance			
Sales Value	Value	Value	%	Value
	(US\$ million, except percentages)			
Fine Paper				
North America	1,231	124	11	1,107
Europe	2,040	272	15	1,768
South Africa	271	8	3	263
Total	3,542	404	13	3,138
Forest Products				
Pulp & Paper	747	53	8	694
Forestry	55	5	10	50
Total	802	58	8	744
Total	4,344	462	12	3,882

Sales Value	Value	2007		Value (US\$ million)	2006		2005
		Variance			Variance		
		Value	%		Value	%	
Fine Paper							
North America	1,511	72	5	1,439	(19)	(1)	1,458
Europe	2,387	193	9	2,194	(45)	(2)	2,239
South Africa	358	33	10	325	2	1	323
Total	4,256	298	8	3,958	(62)	(2)	4,020
Forest Products							
Pulp & Paper	979	83	9	896	(12)	(1)	908
Forestry	69	(18)	(21)	87	(3)	(3)	90
Total	1,048	65	7	983	(15)	(2)	998
Total	5,304	363	7	4,941	(77)	(2)	5,018

Sales Variance Analysis vs. Comparable Period in Previous Year	Nine Months ended June 2008			
	Volume	Exchange		Total
		Price	Rate	
		(US\$ million)		
Fine Paper				
North America	56	68		124
Europe	55	(39)	256	272
South Africa	(14)	26	(4)	8
Total	97	55	252	404
Forest Products				
Pulp & Paper	(18)	83	(12)	53
Forestry	(4)	10	(1)	5
Total	(22)	93	(13)	58
Total	75	148	239	462





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The three factors impacting sales are volume, price and exchange rate. The South African and European businesses transact in Rand and euro respectively, but the results of their operations are translated into US dollars for reporting purposes. The movement in the exchange rate from local currency to US dollars during periods of high volatility significantly impacts reported results from one period to the next. Sales improvement was a major contributor to sustained profitability as it partly offset the impact of cost escalations in the nine months ended June 2008. Volume contributed US\$75 million, price realisation US\$148 million and exchange rate US\$239 million to the US\$462 million improvement in sales value for the nine months ended June 2008, when compared to the nine months ended June 2007. The Fine Paper European US\$55 million and Fine Paper North American US\$56 million improvements in sales volumes were partly offset by negative volume contributions from Fine Paper South Africa (US\$14 million) and Forest Products (US\$22 million). Positive price contributions from Fine Paper North America (US\$68 million), Fine Paper South Africa (US\$26 million) and Forest Products (US\$93 million) were partly offset by negative pricing impacts in Fine Paper Europe (US\$39 million). Positive exchange rate impacts in Europe (US\$256 million) were partly offset by negative impacts at Fine Paper South Africa (US\$4 million) and Forest Products (US\$13 million).

Sales Variance Analysis vs. Previous Year	2007				2006			
	Volume	Price	Exchange Rate	Total	Volume	Price	Exchange Rate	Total
	(US\$ million)							
<b>Fine Paper</b>								
North America	81	(9)		72	(7)	(12)		(19)
Europe	39	(28)	182	194	21	(5)	(61)	(45)
South Africa	22	41	(30)	32	11	10	(19)	2
<b>Total</b>	<b>142</b>	<b>4</b>	<b>152</b>	<b>298</b>	<b>25</b>	<b>(7)</b>	<b>(80)</b>	<b>(62)</b>
<b>Forest Products</b>								
Pulp & Paper	9	159	(85)	83	(55)	95	(52)	(12)
Forestry	(28)	16	(6)	(18)	(11)	13	(5)	(3)
<b>Total</b>	<b>(19)</b>	<b>175</b>	<b>(91)</b>	<b>65</b>	<b>(66)</b>	<b>108</b>	<b>(57)</b>	<b>(15)</b>
<b>Total</b>	<b>123</b>	<b>179</b>	<b>61</b>	<b>363</b>	<b>(41)</b>	<b>101</b>	<b>(137)</b>	<b>(77)</b>

The increase in sales volume in Fine Paper Europe and North America was attributable to an increase in customer market share in both regions. The decrease in volume losses in South Africa was largely due to operational issues with our production activities. In fiscal 2007, volumes improved as market share was more effectively retained and in some instances increased from previous levels. Volume growth at Fine Paper was not at expected levels during fiscal 2005 and fiscal 2006 as all regions experienced market share declines. Forest Products saw declines in pulp and paper volumes due to some loss of local market share in 2006 resulting from import substitution on the back of a much stronger local currency. In 2007, import substitution was less evident as the local currency had weakened against the US dollar making import substitution less attractive. Sappi Fine Paper South Africa experienced similar local market dynamics to Forest Products in 2006 with import substitution being a major threat. Production output difficulties in the nine months ended June 2008, fiscal 2007 and fiscal 2006 at Kraft and the impact of the Saiccor expansion project in the nine months ended June 2008 impacted Forest Products sales volumes adversely. The decline in external timber sales volumes reflects efforts to reduce these sales in order to protect timber stocks in anticipation of the increased Group demand that will occur when the Saiccor upgrade is at full capacity. This situation has been exacerbated by the fires in 2007.

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Sales price development by region in US\$/tonne is as follows:

Sales Price Development	Nine Months to June 2008			Nine Months to June 2007		2007		2006			2005
	Variance					Variance		Variance			
	US\$/Tonne	US\$/Tonne	%	US\$/Tonne	US\$/Tonne	US\$/Tonne	%	US\$/Tonne	US\$/Tonne	%	US\$/Tonne
<b>Fine Paper</b>											
<b>North</b>											
America	1,058	59	6	999	1,003	(6)	(1)	1,009	(8)	(1)	1,017
Europe	1,064	113	12	951	957	61	7	896	(27)	(3)	923
South Africa	1,102	90	9	1,012	1,023	32	3	991	(28)	(3)	1,019
Total	1,064	92	9	972	979	38	4	941	(21)	(2)	962
<b>Forest Products</b>											
Pulp & Paper	719	69	11	650	660	50	8	610	30	5	580
Forestry	76	13	21	63	67	10	18	57	5	10	52
Total	454	53	13	401	417	89	27	328	26	9	302
Total	853	89	12	764	773	87	13	686	15	2	671

#### Sappi Fine Paper North America

The average price for the nine months ended June 2008 increased to US\$1,058 per tonne from US\$999 per tonne for the nine months ended June 2007 as a result of a weaker US dollar and a sales and marketing strategy that was more focused on price levels. The average price realized decreased to US\$1,003 per tonne in fiscal 2007 from US\$1,009 per tonne in fiscal 2006 and US\$1,017 per tonne in fiscal 2005 due to continued market pricing and competition pressure. The major contributor to improved sales is volume resulting from market share gain in the nine months ended June 2008 and fiscal 2007. Volumes in fiscal 2006 were adversely affected by declines in market share due to increased import substitution. There is no exchange rate impact as the translation currency is the same as the reporting currency, namely the US dollar.

#### Sappi Fine Paper Europe

The average price for the nine months ended June 2008 increased to US\$1,064 per tonne from US\$951 per tonne for the nine months ended June 2007 due mainly to the depreciation of the US\$ against the Euro. Average prices realized in US dollar terms were US\$957 per tonne in fiscal 2007, US\$61 per tonne up from US\$896 per tonne in fiscal 2006, which was US\$27 per tonne down from the US\$923 per tonne in fiscal 2005. Pricing in Europe has been under pressure since fiscal 2005 due to strong competition for local market position largely due to the weakening of the US dollar. The average exchange rate for the nine months ended June 2008 was US\$1.50/Euro, compared to an average of US\$1.31/Euro in the same period during fiscal 2007. Pricing in US dollars benefits from the depreciation of the US dollar against the euro when euro values are translated into the US dollar reporting currency. From fiscal 2005 to fiscal 2007 the US dollar declined 19% from US\$1.20/Euro to US\$1.42/Euro. Volumes have, since fiscal 2005, been impacted by changes in market share resulting from attempts to improve pricing and increasing competition in local markets.

#### Sappi Fine Paper South Africa

The average price for the nine months ended June 2008 compared to the nine months ended June 2007 increased to US\$1,102 per tonne from US\$1,012 per tonne for the nine months ended June 2007. The average price realized at SFPSA in US dollar terms increased to US\$1,023 per tonne in fiscal 2007 from US\$991 per tonne in fiscal 2006 after declining from US\$1,019 per tonne in fiscal 2005. During 2006, the region experienced pricing pressure due to import substitution as a result of the strength of the Rand against the US dollar. In 2007, the Rand weakened, lessening the threat and creating the climate for price increases. This trend has continued into fiscal 2008. The weakening of the currency also reduces import substitution volumes creating increased demand for locally produced product. The average exchange rate for the nine months ended June 2008 was ZAR7.32/US\$, compared to an average of ZAR7.21/US\$ in the same period during fiscal 2007, ZAR7.17/US\$ in fiscal 2007, ZAR6.60/US\$ in fiscal 2006 and ZAR6.24/US\$ in fiscal 2005. The commercial benefit achieved as a result of the relatively weaker Rand was partly offset by an adverse impact on the translation of results into the reporting currency (US dollars).

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## Forest Products

Timber volumes at Forest Products have shown a decline as the region reduced external sales in order to conserve and build timber supply inventories in anticipation of the full commissioning of the Saiccor upgrade. Recent fires have placed inventories under further pressure and strategic plans to secure long term fiber supplies are being implemented. A major determinant of pricing in both the Kraft and Saiccor businesses of Forest Products is the international NBSK price. Its price remained high during the nine months ended June 2008 at an average of US\$872/tonne, which was higher than the price as at the close of fiscal 2007 of US\$811 per tonne. These prices were at historical highs and contributed to increasing sales value for both the Kraft and Saiccor businesses. Hardwood Pulp sales, which form a major portion of Kraft sales, have also experienced favorable pricing conditions with an average market price at US\$791/tonne. Hardwood pulp was at US\$720 per tonne at end of fiscal 2007. Kraft's local packaging board sales have also benefited from the depreciation of the Rand against the US dollar which results in a decrease in import substitution and an increase in both local pricing and volumes. The commercial benefit achieved as a result of the relatively weaker Rand was partly offset by the adverse impact of the translation results into the reporting currency (US dollars).

## Operating expenses

An analysis of our operating expenses is as follows:

	Nine Months ended June 2008				Nine Months ended June 2007	
			Variance			
	Costs US\$ Million	US\$/Tonne	Value	%	Costs US\$ Million	US\$/Tonne
Operating Costs						
Variable Costs						
Delivery	371	73	43	13	328	65
Manufacturing	2,258	443	287	15	1,971	388
Total Variable	2,629	516	330	14	2,299	453
Fixed Costs	1,434	282	96	7	1,338	263
Fair value plantation	(67)	(13)	46	(41)	(113)	(22)
Impairment	—	—	—	—	—	—
Restructuring	—	—	—	—	—	—
Pension cost	—	—	—	—	—	—
Profit on sale of Nash	—	—	—	—	—	—
Fire damage	—	—	—	—	—	—
Other	59	12	(3)	(5)	62	12
Total	4,055	797	469	13	3,586	706

	2007				2006				2005	
			Variance				Variance			
	Costs US\$ Million	US\$/ Tonne	Value	%	Costs US\$ Million	US\$/ Tonne	Value	%	Costs US\$ Million	US\$/ Tonne
Operating Costs										
Variable Costs										
Delivery	453	66	12	3	441	61	(10)	(2)	451	60
Manufacturing	2,685	391	169	7	2,516	349	90	4	2,426	324

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Total Variable	3,138	457	181	6	2,957	410	80	3	2,877	384
Fixed Costs	1,808	263	9	1	1,799	250	(135)	(7)	1,934	259
Fair value plantation	(130)	(19)	(26)	25	(104)	(14)	14	(12)	(118)	(16)
Impairment	—	—	31	(100)	(31)	(4)	(262)	(113)	231	31
Restructuring	(7)	(1)	(57)	(114)	50	7	29	138	21	3
Pension cost	—	—	1	(100)	(1)	—	(42)	(102)	41	5
Profit on sale of Nash	(26)	(4)	(26)	—	—	—	—	—	—	—
Fire damage	17	2	17	—	—	—	—	—	—	—
Other	121	18	(25)	(17)	146	20	5	4	141	19
Total	4,921	716	105	2	4,816	669	(311)	(6)	5,127	685

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In the analysis which follows cost per tonne has been based on sales tonnes. The fair value pricing adjustment, impairment charge, profit on sale of Nash mill and fire damage items are discussed under “Overview”. The restructuring charge in 2006 relates to a provision created at SFPE for the restructuring as a result of the cost and operational improvement project run in the region. The US\$7 million reversal in 2007 relates to the balance of this restructuring provision not utilized. This project was implemented and benefits started to flow to the region in 2007. The pension cost reversal in 2006 relates to the impact of the changes to IFRS and restructuring of certain of our post employment benefit funds. Variable and fixed costs have been analyzed in more detail below.

## Variable manufacturing costs

## Group

Variable manufacturing costs relate to costs of inputs which vary directly with output. Other costs relate to inputs such as electricity, water, fillers and consumables. Our variable costs are impacted by sales volume, exchange rate impacts on translation of European and South African businesses into US dollars, and the underlying costs of inputs. In the analysis and discussion of variable costs, volume reflects the changes in cost attributable to sales volume changes, costs refer to changes in input costs and exchange rate relates to the impact of the movement in exchange rate on the translation from local currency to US dollars for reporting purposes at Fine Paper Europe and South Africa. The major contributors to variable cost escalations at a Group level were the impact of the exchange rate on translation of the European and South African operations into the US dollar reporting currency and actual input cost escalations. See “—Currency Fluctuations” for exchange rate movements. Increases due to volume are related to the movement in sales volumes year on year and changes in usage. Cost escalations are being driven by international commodity price movements. The two major cost drivers have been oil and pulp price movements.

An analysis of the impact of these components is as follows:

	Nine Months ended June 2008				Nine Months ended June 2007	
	US\$		Variance		US\$	
	Million	US\$/Tonne	Value	%	Million	US\$/Tonne
Variable Manufacturing Costs						
Wood	535	105	60	13	475	93
Energy	417	82	91	28	326	64
Pulp	598	117	130	28	468	92
Chemical & Other	708	139	6	1	702	138
Total	2,258	443	287	15	1,971	388

	2007				2006				2005	
	US\$		Variance		US\$		Variance		US\$	
	Million	US\$/Tonne	Value	%	Million	US\$/Tonne	Value	%	Million	US\$/Tonne
Variable Manufacturing Costs										
Wood	635	93	4	1	631	88	(16)	(2)	647	87
Energy	438	64	5	1	433	60	68	19	365	49
Pulp	623	91	60	11	563	78	49	10	514	69
Chemical & Other	989	143	100	11	889	124	(11)	(1)	900	120
Total	2,685	391	169	7	2,516	350	90	4	2,426	324

Variable Cost Movement Analysis vs. Comparable Period in Previous Year	Nine Months ended June 2008			
	Volume	Exchange		Total
		Rate	Price	
		(US\$ million)		
Wood	33	17	10	60
Energy	11	24	56	91
Pulp	48	50	32	130
Chemical & Other	(77)	55	28	6
Total	15	146	126	287



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Variable Cost Movement Analysis vs. Previous Year	2007				2006			
	Volume	Exchange Rate	Price	Total (US\$ million)	Volume	Exchange Rate	Price	Total
Wood	(43)	5	42	4	(39)	(9)	32	(16)
Energy	(7)	7	5	5	(3)	(11)	82	68
Pulp	(15)	25	50	60	25	(14)	38	49
Chemical & Other	71	26	3	100	17	(27)	(1)	(11)
Total	6	63	100	169	—	(61)	151	90

The regional variable costs in the table below are regional operating costs excluding consolidation adjustments and reallocation and represent the operating costs as reported internally at a regional level for management purposes.

Regional Variable Manufacturing Costs	Nine Months ended June 2008				Nine Months ended June 2007	
	US\$ Million	US\$/Tonne	Variance		US\$ Million	US\$/Tonne
			Value	%		
SFPNA	682	586	40	6	642	579
SFPE	1,206	629	189	19	1,017	547
SFPSA	160	650	2	1	158	608
Forest Products	386	219	57	17	329	177

Regional Variable Manufacturing Costs	2007				2006				2005	
	US\$ Million	US\$/ Tonne	Variance		US\$ Million	US\$/ Tonne	Variance		US\$ Million	US\$/ Tonne
			Value	%			Value	%		
SFPNA	869	577	44	5	825	579	42	5	783	546
SFPE	1,370	550	139	11	1,231	502	63	5	1,168	481
SFPSA	210	600	7	3	203	619	7	4	196	618
Forest Products	462	184	(22)	(5)	484	162	(6)	(1)	490	148

An analysis of variable cost developments by regions is as follows:

## Sappi Fine Paper North America

Wood costs and product re-design have been major focus areas in the region in recent years with improved management systems and processes being introduced in order to address escalating costs. However, market conditions and escalating energy costs have resulted in wood costs for the nine months ended June 2008 increasing to US\$124 per tonne compared to US\$117 per tonne for the corresponding period in the prior fiscal year. Wood costs decreased to US\$98 per tonne in fiscal 2007 from US\$110 per tonne in fiscal 2006 and US\$111 per tonne in fiscal 2005. Energy costs are largely driven by international crude oil prices. Given the escalating cost of energy, the region has embarked on a number of energy utilization improvement plans which have contributed to a reduction in energy costs relative to the potential impact of oil price movements. Pulp costs are driven by the cost of bought-in non-integrated pulp. Escalating international pulp pricing in US\$ have contributed to the cost increases. Cost management remains a major focus area with product design being constantly reviewed in order to ensure products are not over-designed for intended use, thereby minimizing costs.

Sappi Fine Paper Europe

SFPE has experienced a number of cost pressures during the nine months ended June 2008 and fiscal 2007. Wood costs are being driven by specific supply and demand issues as well as increased demand for alternative renewable fuels in Europe. International crude oil prices have driven energy and other oil-based input costs up significantly in recent years. Significant cost reduction initiatives have managed to curtail the increased pressure from escalating commodity input costs to some extent through process as well as product re-engineering initiatives. Escalating international pulp prices have increased the cost of non-integrated pulp. The region has been protected to some extent by the relative strength of the euro against the US dollar for US dollar-based inputs, such as pulp and certain chemicals. However, when reporting, costs in US dollars increase significantly due to the impact of the exchange rate on the translation of costs from euro into US dollars.

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## Sappi Fine Paper South Africa

The region has minimal external purchased wood input costs as wood is supplied by the forestry operations of Forest Products. The costs of producing and supplying timber for own consumption are included in fixed and variable costs, according to their nature. The costs of growing timber are accounted for as silvicultural costs. In Rand, the region's costs have shown increases in year-on-year comparison and in the nine months ended June 2008 as compared to the same period in the previous year. These increases are largely attributable to the impact of the weakening of the Rand against the US dollar on US dollar-based inputs. The major contributors have been purchased pulp, energy and chemical input costs, which are being driven by international oil, commodity price pressures and the impact of the exchange rate movements.

## Forest Products

The wood cost at Forest Products relates to the cost of timber consumed that is purchased externally by Forestry. Wood pricing is driven by export parity pricing pressures which reflect both the international trend in wood pricing and the impact of the ZAR/US\$ exchange rate dynamics. The cost of local timber has been escalating due to increased demand from both major local paper producers and exporters. The pool of non-integrated timber in South Africa is relatively small and currently very costly due to the increasing demand. The impact of pulp cost movements are limited as in the region we only purchase pulp in instances when we experience pulp production capacity issues that limit supply. Chemical and other costs are being driven by a combination of escalating international commodity prices and the impact of the depreciation of the Rand relative to US dollars on US dollar-based variable inputs.

## Fixed costs

## Group

A summary of our major fixed cost components is as follows:

	Nine Months ended June 2008				Nine Months ended June 2007	
			Variance			
	US\$ Million	US\$/Tonne	Value	%	US\$ Million	US\$/Tonne
Fixed Costs						
Personnel	763	150	76	11	687	135
Maintenance	188	37	17	10	171	34
Depreciation	281	55	—	—	281	55
Other	202	40	3	2	199	39
Total	1,434	282	96	7	1,338	263

	2007				2006				2005	
			Variance				Variance			
	US\$ Million	US\$/Tonne	Value	%	US\$ Million	US\$/Tonne	Value	%	US\$ Million	US\$/Tonne
Fixed Costs										
Personnel	926	135	48	5	878	122	(103)	(10)	981	131
Maintenance	236	34	7	3	229	32	(29)	(11)	258	34
Depreciation	372	54	(15)	(4)	387	54	(29)	(7)	416	56
Other	274	40	(31)	(10)	305	42	26	9	279	37
Total	1,808	263	9	1	1,799	250	(135)	(7)	1,934	259

The regional fixed costs in the table below are regional operating costs excluding consolidation adjustments and reallocations and represent the operating costs as reported internally at a regional level for management purposes.

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	Nine Months ended June 2008				Nine Months ended June 2007	
	Variance					
	US\$ Million	US\$/Tonne	Value	%	US\$ Million	US\$/Tonne
Regional Fixed Costs						
SFPNA	411	353	7	2	404	365
SFPE	651	339	65	11	586	315
SFPSA	84	341	5	6	79	304
Forest Products	302	171	31	11	271	146

	2007				2006				2005	
	Variance				Variance					
	US\$ Million	US\$/Tonne	Value	%	US\$ Million	US\$/Tonne	Value	%	US\$ Million	US\$/Tonne
Regional Fixed Costs										
SFPNA	542	360	(19)	(3)	561	393	(59)	(10)	620	433
SFPE	778	312	8	1	770	314	(52)	(6)	822	339
SFPSA	107	306	3	3	104	317	(8)	(7)	112	353
Forest Products	374	149	(3)	(1)	377	126	(36)	(9)	413	125

## Sappi Fine Paper North America

The region has been involved in restructuring and cost reduction processes in recent years and the benefits of these initiatives are contributing to the fixed cost reductions after fiscal 2005.

## Sappi Fine Paper Europe

During fiscal 2006, the region embarked on a major restructuring project aimed at reducing costs and improving efficiencies, which has been the major contributor to the cost reductions in fiscal 2006. Included in the program was a significant headcount reduction. 2006 personnel costs were also impacted by a post-employment benefit credit of US\$11 million. Fixed costs in US dollars in fiscal 2007 were US\$8 million higher than fiscal 2006 which was US\$52 million lower than fiscal 2005 due to the impact of the currency on translation. In the nine months ended June 2008, cost saving initiatives remained a key focus area.

## Sappi Fine Paper South Africa and Forest Products

In the nine months ended June 2008, personnel and maintenance cost increases in local currency remained the major drivers of fixed cost increases. These cost increases were, in US dollars, offset by the impact of the exchange rate on translation of the costs into the US dollar reporting currency. Personnel costs are under pressure from labor rate increases due to cost of living adjustments and the impact of the skills shortage on labor rates, particularly in the skilled technical functions.

## Net Finance Costs

Net finance costs consists of gross interest and other finance costs net of interest received, interest capitalized, foreign exchange gains and losses and change in fair value of financial instruments. Net finance costs for the nine months ended June 2008 were US\$100 million as compared to US\$107 million for the nine months ended June 2007. Net finance costs were US\$134 million in 2007, US\$130 million in 2006 and US\$80 million in 2005. Net interest cost for the nine months ended June 2008 decreased by US\$6 million to US\$106 million as compared to the corresponding period the previous year. Net interest cost increased in 2007 from 2006 by US\$16 million to US\$152 million.

Cash interest cover (cash generated by operations divided by net finance costs (before capitalized interest)) for the nine months ended June 2008 increased to 4.22 times from 3.7 times for the corresponding period in 2007. Cash interest cover also increased from 2.9 times in 2006 to 3.8 times for 2007. The increases in the nine months ended June 2008 and fiscal 2007 were mainly due to higher cash generated by operations.

Finance costs capitalized for the nine months ended June 2008 were US\$16 million compared to US\$8 million for the corresponding period in 2007. Finance costs capitalized were US\$14 million in 2007 and US\$2 million in 2006. Finance costs capitalized relate primarily to the capitalized interest on major projects under construction, in particular the Saiccor upgrade.

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## Taxation

The taxation charge for the nine months ended June 2008 was US\$55 million (effective tax rate 29%) compared to US\$62 million (effective tax rate 33%) for the corresponding period in 2007. The taxation charge for fiscal 2007 was US\$47 million (fiscal 2006: US\$1 million benefit; fiscal 2005: US\$5 million benefit) corresponding to an effective tax rate of 19% (fiscal 2006: 15%; fiscal 2005: 3%). The effective tax rate is impacted by the magnitude of the fair value price adjustment of plantations relative to operating profitability, which affects the deferred tax provision as well as the geographical source of operating profit in a particular period. Also the expected taxation (fiscal 2007: US\$68 million charge; fiscal 2006: US\$13 million benefit; fiscal 2005: US\$109 million benefit), which is derived by applying the average statutory tax rate applicable to our profit and loss making tax entities, respectively, was favorably impacted by announced tax rate reductions in Germany (fiscal 2007: US\$19 million; fiscal 2006: nil; fiscal 2005: nil), the Netherlands (fiscal 2007: US\$2 million; fiscal 2006: US\$1 million; fiscal 2005: US\$4 million) and South Africa (fiscal 2007: nil; fiscal 2006: nil; fiscal 2005: US\$9 million). Certain of our Group's profits are not taxed as a result of losses carried forward or favorable permanent differences. Tax relief was not taken on the taxation losses of certain loss-making entities due to management's judgment that these taxation losses may not be recoverable in the near future (net impact fiscal 2007: US\$1 million benefit; fiscal 2006: US\$3 million charge; fiscal 2005: US\$93 million charge). The Secondary Tax on Companies (nine months ended June 2008: US\$7 million; fiscal 2007: US\$8 million; fiscal 2006: US\$9 million; fiscal 2005: US\$8 million) relates to South African tax on the dividend.

## Net Profit

Net profit for the nine months ended June 2008 increased to US\$134 million compared to US\$127 million for the corresponding period in 2007. Net profit increased to US\$202 million in fiscal 2007 from a loss of US\$4 million in fiscal 2006 and a loss of US\$184 million in fiscal 2005. The increased profitability in the nine months ended June 2008 as compared to the corresponding period in 2007 was mainly attributable to lower finance (US\$7 million) and tax (US\$7 million) charges partly offset by lower operating profits (US\$7 million). The increased profitability in fiscal 2007 was mainly due to improved sales. The factors impacting operating profitability have been dealt with in the sales and cost discussions above. Net loss in fiscal 2005 was impacted by the Muskegon and Usutu impairment charges of US\$231 million pre-tax. Restructuring charges in Europe were partly offset, in fiscal 2006, by the reversal of impairment on Usutu mill at Sappi Forest Products.

Basic earnings per share for the nine months ended June 2008 were 59 US cents, compared with 56 US cents for the corresponding period in 2007. Basic earnings per share increased from a loss of 2 US cents per share in 2006 (2005: 81 US cents loss per share) to an income of 89 US cents per share in 2007.

## Liquidity and Capital Resources

## Cash Flow—Operations

An analysis of cash flow for our Group is as follows:

Cash Flow	Nine Months ended June		2007 (US\$ million)	2006	2005
	2008	2007			
Cash generated by operations	487	424	585	396	569
Movement in working capital	(134)	(80)	60	(17)	(30)
Finance costs	(150)	(109)	(162)	(138)	(127)
Taxation	(56)	(18)	(27)	(13)	(43)

Capital expenditure	(368)	(320)	(442)	(303)	(293)
Cash generated utilized	(277)	(117)	24	(127)	(78)

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Cash generated from operations for the nine months ended June 2008 was US\$487 million compared to US\$424 million for the corresponding period in 2007. Profit for the period (US\$134 million) increased by US\$7 million compared to the same period 2007 (US\$127 million). Cash generated was reduced by finance costs paid (net of interest income) of US\$150 million US\$41 million more than for the corresponding period in 2007, taxation paid of US\$56 million US\$38 million more than for the corresponding period in 2007. Finance costs paid during the nine months ended June 2007 were US\$109 million and taxation paid US\$18 million. Working capital decreased by US\$134 million during the nine months ended June 2008 and decreased by US\$80 million during the nine months ended June 2007.

Cash generated from operations during fiscal 2007 was US\$585 million compared to US\$396 million in fiscal 2006, an increase of US\$222 million in cash generated compared to fiscal 2006 (fiscal 2005 cash generated by operations was US\$569 million). Operating Profit (US\$383 million) improved by US\$258 million as against fiscal 2006 operating profit (US\$125 million). Fiscal 2005 operating loss was US\$109 million. Cash generated was reduced by finance costs paid (net of interest income) of US\$162 million (US\$24 million more than fiscal 2006), taxation paid of US\$27 million (US\$14 million more than 2006). Finance costs paid in 2006 were US\$138 million (fiscal 2005 US\$127 million) and taxation paid US\$13 million (fiscal 2005 US\$43 million). Working capital reduced by US\$60 million in fiscal 2007 and increased US\$17 million in fiscal 2006 and US\$30 million in fiscal 2005.

Total non-cash items included the following:

Non-cash Items	Nine Months ended June		2007 (US\$ million)	2006	2005
	2008	2007			
Depreciation	283	282	374	391	422
Fellings	61	52	70	74	66
Asset Impairments & closures	3	1	2	(14)	232
Plantation fair value-price	(12)	(56)	(54)	(34)	(60)
Plantation fair value-volume	(55)	(57)	(76)	(70)	(58)
Post-employment benefits	(65)	(80)	(101)	(68)	—
Other	(17)	(14)	(13)	(9)	76
	198	128	202	270	678

The fiscal 2005 impairment charges related mainly to the Sappi North American Muskegon and Forest Products Usutu mills. The Usutu impairment was reversed in fiscal 2006 (US\$40 million). Impairment charges for the nine months ended June 2008 and 2007 related mainly to the ongoing impairment of capital expenditure at impaired mills.

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Net working capital changes are shown in the graph below:

## Working Capital Movement—US\$ million

## Investing

Cash utilized in investing activities was US\$351 million in the nine months ended June 2008, US\$265 million in the same period 2007, US\$364 million in fiscal 2007, US\$287 million in fiscal 2006 and US\$379 million in fiscal 2005.

Investing Activities	Nine Months ended June		2007 (US\$ million)	2006	2005
	2008	2007			
Capital expenditure	368	320	442	303	293
Proceeds on disposals	(3)	(48)	(50)	(5)	(5)
Investments and loans	(14)	(7)	(28)	(11)	91
	351	265	364	287	379

Capital Expenditure by region is as follows:

Capital Expenditure by Region	Nine Months ended June		2007 (US\$ million)	2006	2005
	2008	2007			
SFPNA	98	28	42	48	76
SFPE	48	72	102	136	109
SFPSA	5	6	12	19	22
Forest Products	217	213			