Sasol Limited

Energy

Company Update Report

Buy

Maintaining a buy after a more conservative valuation

Analyst recommendation

Counter	Share price	Intrinsic value	Upside/(downside)
SOL-ZA	R104.94	R192	83%

As at 04 November 2024

Executive summary

In this report we look at the 2024 full-year results and provide further insights to Sasol valuation.

On 20 August, Sasol released its FY24 results, which were characterised by the following:

1. Turnover decreased by 5%, driven mainly by a decrease in the chemicals average sales basket price due to a combination of weak demand and the impact of lower oil, feedstock and energy prices.
2. Core headline earnings per share decreased by 16% mainly due to lower chemical prices. However, earnings per share (EPS) decreased from a profit of R14 per share to a loss per share of R70 per share due to impairments with the largest relating to the US ethane value chain impairment of R59 billion.
3. Sales volumes were slightly higher with higher chemical sales volumes offset by lower energy sales volumes, with total volumes growth contributing R721 million to earnings before interest and tax growth.
4. The new dividend policy allows dividends to be paid on 30% of free cash flows provided that net debt (excluding leases) is below $4 billion. Net debt which increased by 7% to $4.1 billion and the interim dividend being based on the previous policy led to no final dividend being declared.

We decreased our intrinsic value by 31% from R279 to R192 while maintaining a buy with the main reasons being:

1. Even though we anticipated that the chemical margins might take longer to recover, we now expect margins to be structurally lower due to the increased competition from China (graph 5 and 6), similar to sectors such as the solar panel and vehicle industry. We expect margins to recover, but not to the previous highs it might have reached historically (graph 4).
2. We are concerned about the oil price outlook as it seems OPEC might not have the same influence it used to have as non-OPEC countries such as the US have gained market share (graph 7), and production is expected to increase while demand growth is soft.
3. To incorporate the above views, we updated our valuation. Refer to the valuation and assessment section for more details.

Analyst thesis

- **Attractive valuations with deep discounts outweighs the concerns.**
  This being reflected in in our probability weighted intrinsic value upside of 83% and its discounts relative to commodity price relationships (graph 8 and 9), peer multiples where it is trading at a 77% discount to peer LyondellBasel (graph 11) and its own historic price to earnings ratio (graph 12) trading at a discount of 59% to its 5-year average price to earnings ratio.
- **Various catalysts that should drive a recovery in its valuation.**
  1) Recovery in chemical industry margins will lead to significant increase in profits although it might take a couple of years as supply first needs to decline through significant closures to rebalance with demand which we expect will take longer than a year. 2) Reduction in debt to reduce financial risk uncertainty. 3) Clarification in regulations such as carbon tax should remove uncertainty around profitability and its path to reducing carbon emissions. 4) Increase in the rand oil price, although only to an extent as Sasol's share price relationship to the oil price has disconnected (graph 8). 5) Return of capital to shareholders through asset disposals at these low share price valuation multiples or Sasol being acquired at a share price premium.

Financial results

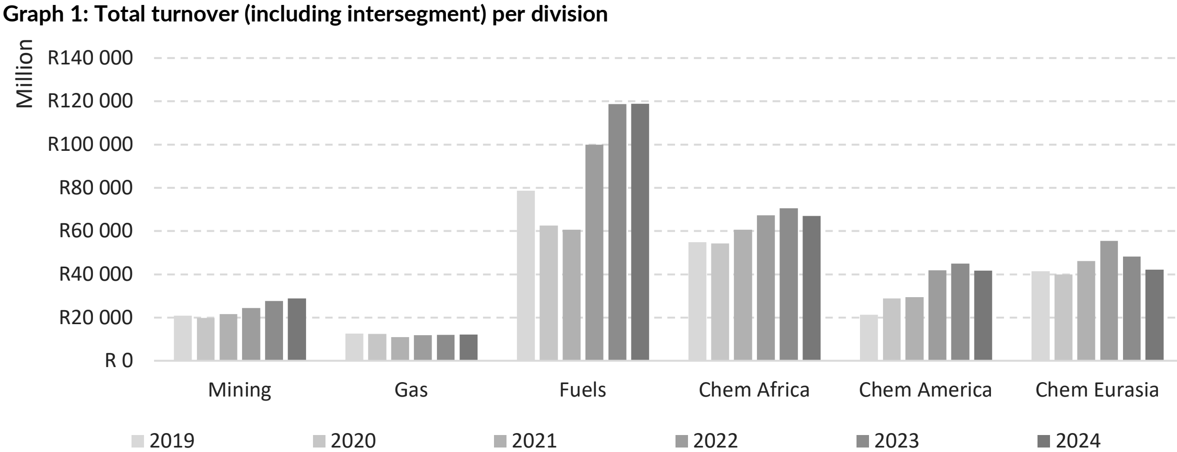
Table 1: Results summary

Metric (million)	1H23	1H24	Y/Y %
Turnover	289 696	275 111	-5.0
Adjusted EBITDA	66 305	60 012	-9.5
L/EBIT	21 520	-27 305	N.M.
Cash generated by operating activities	64 637	52 321	-19.1
Net debt/EBITDA (x)	1.3	1.5	15.4
Brent crude (US$/bbl) average	87	85	-3.0
Ethane (US$c/gallon) average	35	23	-34.9
R/US$ average	17.77	18.71	5.3
Core HEPS (ZAR)	47.71	40.28	-15.6
EPS (ZAR)	14.00	-69.94	N.M.
HEPS (ZAR)	53.75	18.19	-66.2

Source: Company financials

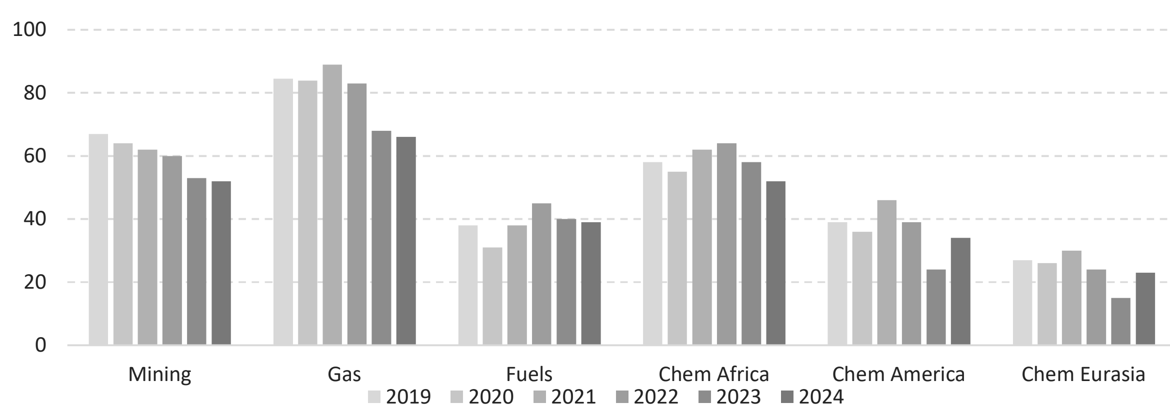
Note: | bbl – barrels | EBITDA – earnings before interest, tax, depreciation and amortisation | L/EBIT –loss/earnings before interest and tax |

Graph 1: Total turnover (including intersegment) per division



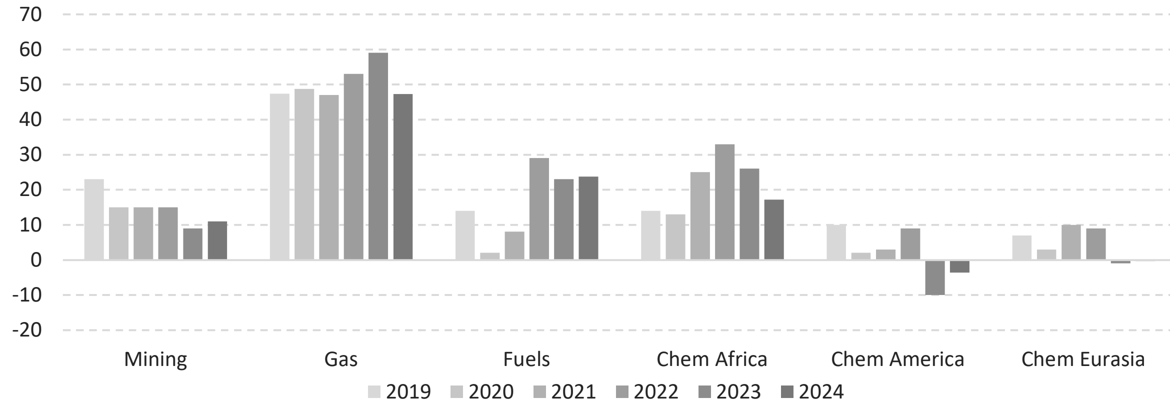
Source: Company financials

Graph 2: Gross margin percentage per division



Source: Company financials

Graph 3: Normalised EBIT margin percentage per division



Source: Company financials (normalised = excludes remeasurement items)

Table 2: 2025 management outlook

Metric	FY24 actual	FY25 outlook
Mining saleable production	30.2 million tons	30 - 32 million tons
Secunda operation volumes	7.0 million tons	7.0 million to 7.2 million tons
Liquid fuels sales	51.7 million barrels	0% to 4% higher
Natref run rate	519 cubic meters per hour	0% to 10% higher
Mozambique gas production	120.8 bscf	0% to 5% higher
ORYX GTL (Qatar) production	2.9 million barrels	40% to 60% higher
Chemicals Africa sales volumes	3 515 thousand tons	0% to 4% increase
Chemicals America and Eurasia sales volumes	2 790 thousand tons	In-line
Maintain and transform capital expenditure	R29.3 billion	R28 billion to R30 billion

Source: Sasol financials

As per the first quarter 2025 production update, management lowered its guidance on the Natref run rate from between 5% to 15% higher to 0% - 10% higher due to operational challenges and start-up delays.

Valuation and assessment

We changed our model for the bear case from a forecasted EBIT to a liquidation value method to incorporate a more conservative bear case outcome reflecting a more bearish view where the company had to close and sell off its operations.

In our base and bull case we forecasted Sasol's earnings per share with the most material assumptions relating to revenue per segment, normalised EBIT margins per segment and the group effective tax rate. The exit price to earnings multiple is also a material assumption in determining our intrinsic value. (refer to below table and graphs)

In our bear case we assumed that there is no net value in the South Africa business as the SA fuels and chemical business challenges such as greenhouse gas reduction road map, carbon tax, infrastructure challenges and deteriorating coals challenges lead to no value after repaying debt. Similarly, we take the same approach in Eurasia business with the view that Sasol needs to be part of the significant closures in the industry that is needed to improve margins, leading to no value after all debt is paid. After these closures we therefore assume all debt is covered. To further support this view, Sasol currently produce around R52 billion cash flow from operating activities yearly and has a R45 billion cash balance compared to total debt which is around R120 billion. We then value the Oryx GTL at R10.4 billion and Louisiana Integrated Polyethylene JV LLC (LIP JV) business at R26.7 billion based on their net asset values. As a bear case we view this approach as sufficiently conservative as peers such as LyondellBasell trade at price to book ratio of 2 times and this discount appropriately reflects a scenario where Sasol had to sell the assets in a distressed scenario. The 50% of the Louisiana Integrated Polyethylene JV LLC (LIP JV) business Sasol sold to LyondellBasell in 2020 was also estimated at $2 billion compared to our value above of R26.7 billion. Sasol also calculated in its most recent 2024 annual financial statements a recoverable amount of R47.6 billion for its chemicals America ethane value chain after a R59 billion impairment resulting from margin decreases, a longer-term depressed margin outlook and an increase in the weighted average cost of capital rate in its valuation assumptions. We acknowledge the bear case might play out in different ways such as which parts of the business are kept or sold off, but in our view, we believe it appropriately captures a worst-case scenario.

Our base case reflects a slow chemical margins recovery from closures or reduction in output by global chemical companies and we have no expectation of a recovery to 2022 levels as we view the increased global supply as a structural change. We also included a 10% reduction in the Eurasia volumes as we assume Sasol also needs to be one of the companies required to reduce supply through closures or downscaling. We lowered our earnings forecast in the fuels business as we forecast a $70 per barrel oil price from the $85 per barrel oil price average in 2024 financial year and we lowered our normalised EBIT margin to 10% from the average of 20% for the past four years. We deem a price to earnings ratio of 6 as fair for a slow growth company which is also below its ten-year average of 7.9.

Our bull case reflects a faster chemical margins recovery from closures or reduction in output by global chemical companies and with still no expectation of a recovery to 2022 levels as we view the increased global supply as a structural change. Again, we included a 10% reduction in the Eurasia volumes as we assume Sasol needs to be one of the companies required to reduce supply through closures or downscaling. We lowered our earnings forecast less in the fuels business as we forecast a $80 per barrel oil price from the $85 per barrel oil price average in 2024 financial year and we used a normalised EBIT margin to 20% in line with the average of 20% for the past four years. We used a slightly higher price to earnings ratio of 7 compared to our base case which is still below its ten-year average of 7.9 as we believe even in a bull case scenario Sasol will face more challenges in the next ten years than the past ten years due to global changes from environmental pressures.

We aligned our view and therefore the weights provided to the bear, base and bull case to reflect:

- An increased likelihood of a near term slowdown in global demand as the higher interest rate environment starts to take hold and as unemployment increases.
- A lower oil price as oil production increases while demand slows, and the market loses faith in OPECs ability to control the oil price.
- The structural change in the chemical supply industry to reflect the increased competition from China.

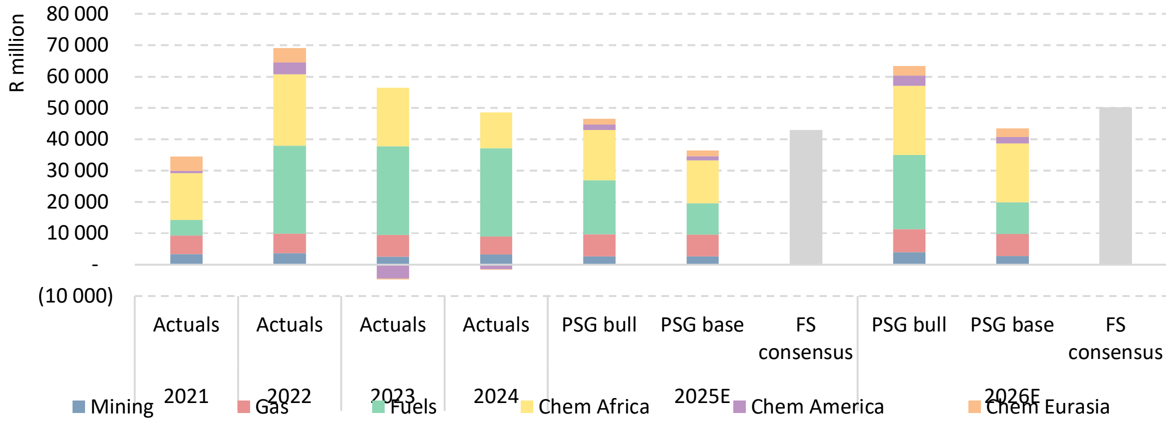
Table 3: Valuation

Case	Bear case	Base case	Bull case
FY2026 exit EBIT (R m)		42 418	62 429
PV of dividends (R per share)		6	17
Exit PE applied on 2026 EPS		6	7
FY26 earnings per share (R per share)		38	59
Consensus FY26 earnings per share (R per share) *	43	51	62
FY26 target price (R per share)		225	410
PV of target price (R per share)		195	355
Bear liquidation value (R b)	37		
Intrinsic value (R per share)	55	202	372
Upside/downside per case	-48%	92%	255%
Weight	30%	50%	20%
Cost of equity	15%		
Weighted intrinsic value	192		

Source: FactSet

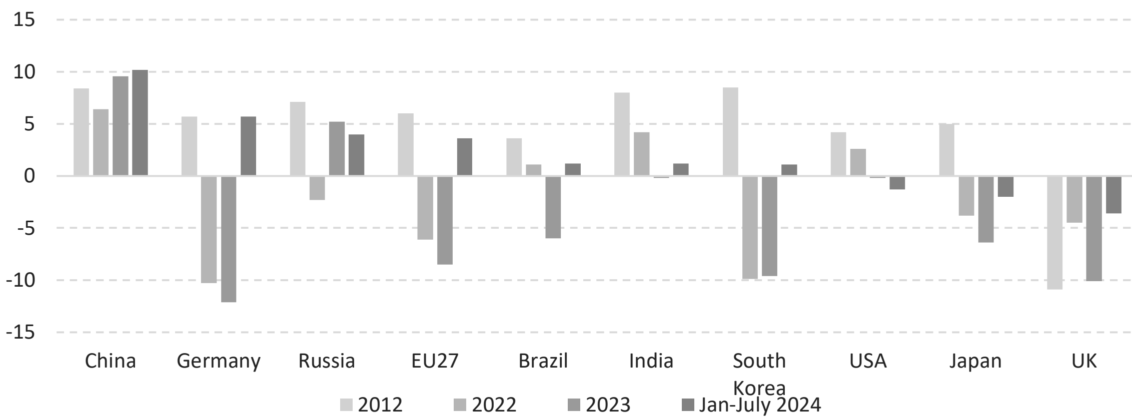
* FactSet sell side analysts minimum, median and maximum forecasts

Graph 4: Normalised EBIT forecast



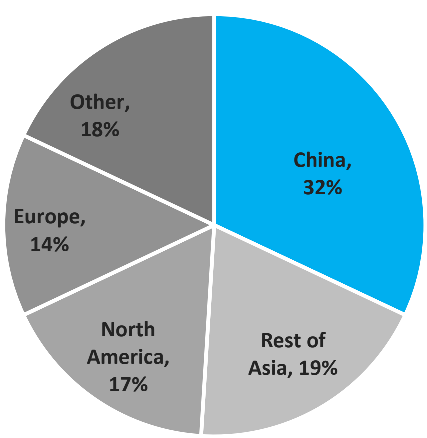
Source: FactSet

Graph 5: Chemicals production growth percentage for main countries



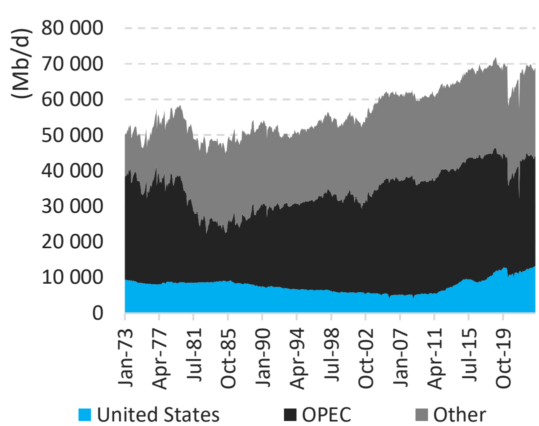
Source: Eurostat and Cefic analysis (2024)

Graph 6: Global plastic materials production share in 2022



Source: Statista

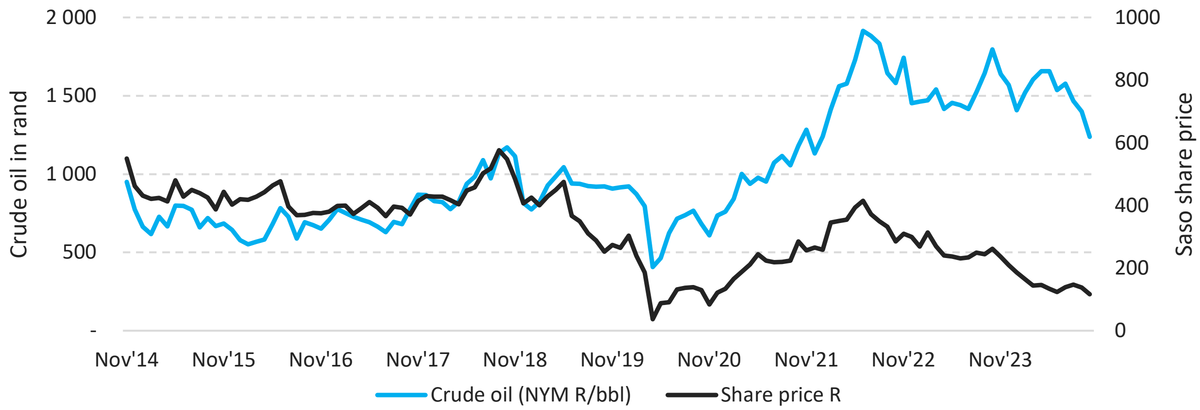
Graph 7: Crude oil including lease condensate production



Source: US Energy information Administration

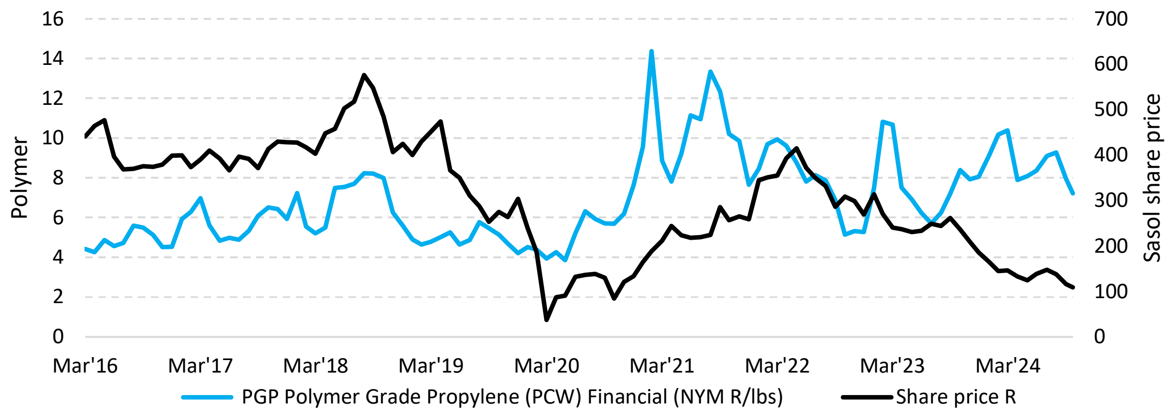
As per the International Energy Agency's October oil market report, oil demand is expected to expand by 900 kb/d in 2024 and 1 mb/d in 2025 compared to non-OPEC+ supply expected to grow by 1.5 mb/d in 2024 and 2025. OPEC+ spare production capacity is also standing at historic highs, barring the exceptional period of covid-19 pandemic. Excluding Libya, Iran and Russia, effective spare capacity exceeded 5 mb/d in September.

Graph 8: Sasol share price versus rand crude oil price



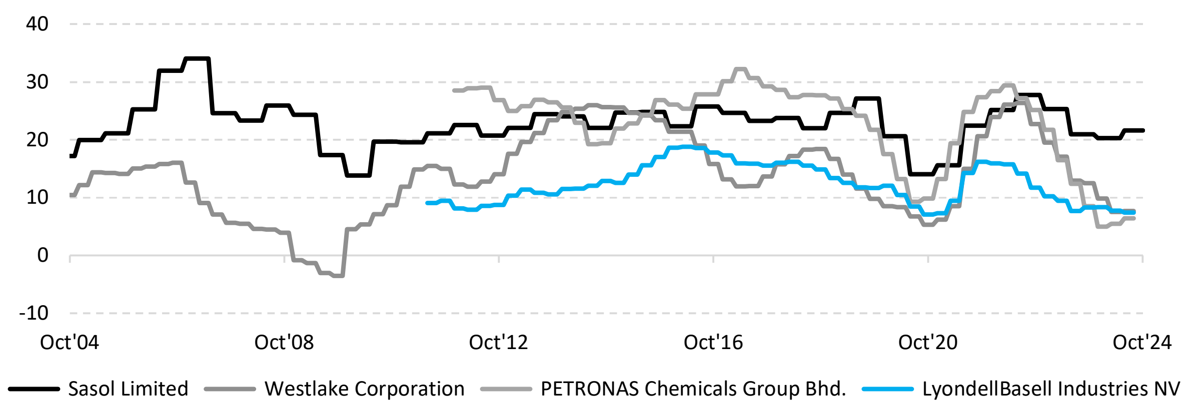
Source: FactSet

Graph 9: Sasol share price versus rand polymer grade propylene price



Source: FactSet

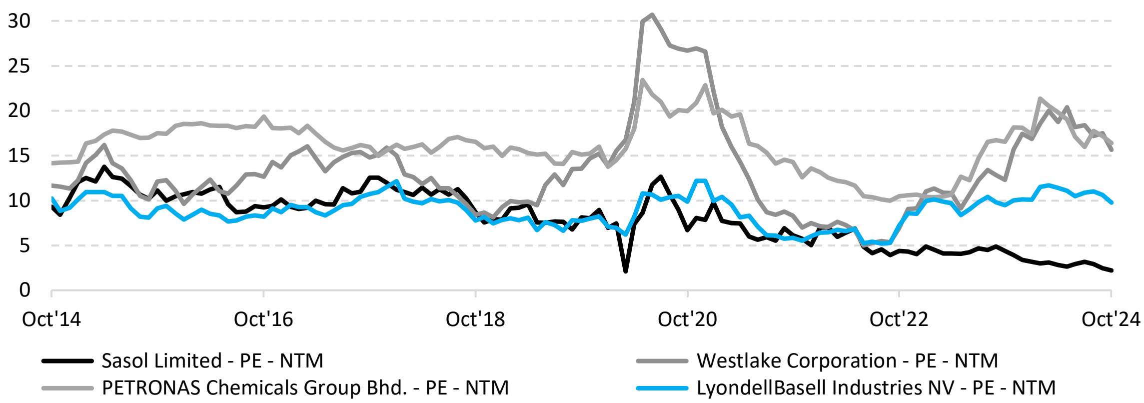
Graph 10: Chemical industry percentage operating margins



Source: FactSet

When comparing Sasol to chemicals industry peers we note that it's not only Sasol that has seen a decrease in its operating margins. We believe that these lower operating margins are cyclical as it relates to customers destocking, a slowdown in demand due to a monetary tightening cycle and excess supply capacity.

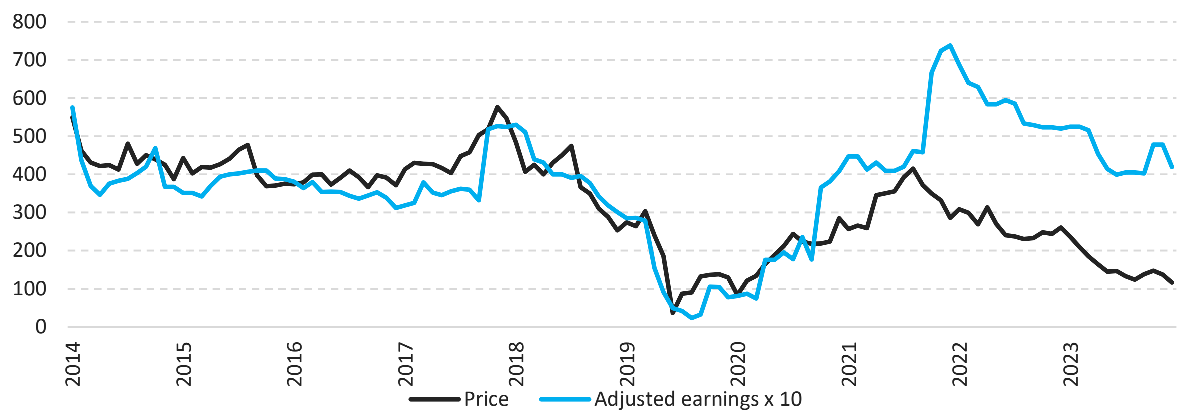
Graph 11: Chemical peers NTM P:E ratios



Source: FactSet

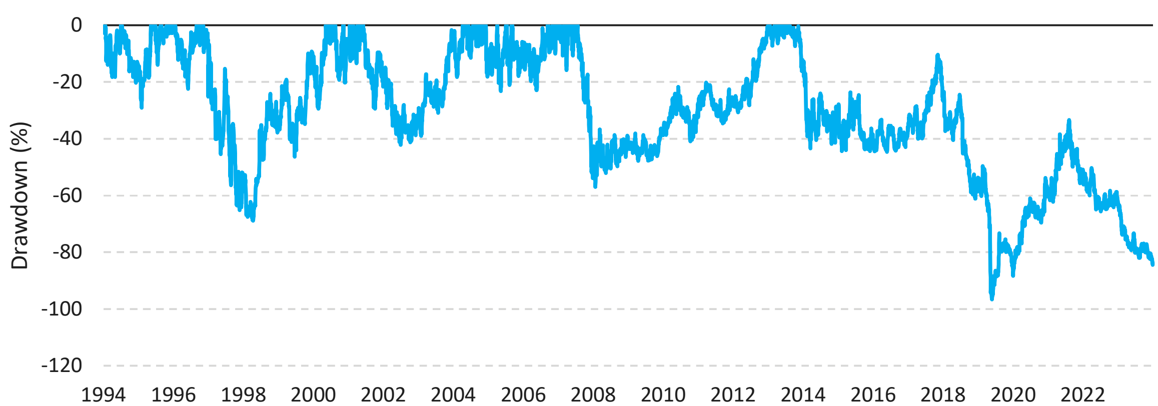
Even though chemical peers have seen a decrease in their multiples like Sasol, they were able to recover more recently (after mid 2022). LyondellBasell Industries especially traded at a similar historical multiple as Sasol but at the moment Sasol it trading at a significant 77% discount to LyondellBasell's forward P:E. Taking this into account combined with Sasol's operating margin relative to peers (graph 10), we see Sasol as having derated too much due to the long term uncertainties in its South African operations which represents about half of the business on revenue basis.

Graph 12: Sasol share price vs its NTM earnings per share x 10



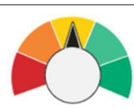
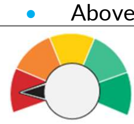
Source: FactSet

Graph 13: Sasol share price historical drawdowns



Source: FactSet

Table 4: Qualitative summary

Factor review	Rating	Description
Growth		Expected 3Y sales CAGR of 3.3%. Earnings growth impacted by once off impairments with the current year loss expected to return to a profitable R35.2 billion over three years. Growth outlook challenged with operational and ESG challenges. Recovery in chemical margins should lead to growth although timing and extent not clear.
Valuation		Trading at deep discounts to its own history, peers and commodity price relationships. Upside to intrinsic value is 83%.
Dividend yield		The forward dividend yield for Sasol Limited is 6.2%. Sasol recently changed its dividend policy to align to cash flows and ensure debt levels remain healthy which could place some pressure on dividends in the near term.
Issuance		Total shares have slightly increased over the years.
Catalyst		• Unexpected rise in gas and oil prices being sustained at a higher level than market expectations. • Unexpected increase in chemical business margins. • Depreciation of the Rand. • Being acquired at a premium to its share price or the return of capital through disposals of assets at low valuation multiples. • Reduction in debt levels. • Stronger production and sales volumes than guided. • Delivering solutions on operational and ESG challenges. • Investments being more successful than anticipated.
Quality of earnings		Earnings are susceptible to large swings from commodity and currency prices. History of once-off items requiring judgement such as impairments and remeasurements contributing to further instability of earnings.
Moat		Moat in South Africa, but not in the global operations.
Management and governance		Management still to prove themselves. CEO was replaced by Simon Baloyi (previously the executive vice president of energy operations and technology) effective April 2024. Simon Baloyi has been 11 years at Sasol. CFO was replaced by Walt Bruns (previous positions includes CFO of Sasol SA and CFO global chemicals business) effective September 2024. Walt Bruns has been 15 years at Sasol.
Balance sheet		Sasol Limited has cash and short-term investments of R49 billion. Total liabilities are R120 billion, of which R4 billion is short-term debt. Net debt to EBITDA is approximately 1.5x. Although debt levels are reasonable in our opinion the volatility of its earnings does create a higher risk.
Risks		• Decline in gas and oil prices. • Appreciation of the Rand. • Lower chemical margins and demand. • ESG risks pertaining to the environment including risks associated with greenhouse gas emissions. • Investments being value destructive. • Disruptions to operations. • Weaker production and sales volumes than guided. • Political and social risks. • Litigation and other legal risks. • Above risks could increase financial risk to repay its debt.
Regulation		Changes in mining, tax and ESG legislation. Sasol faces ESG risks associated with greenhouse gas emissions, particularly in South Africa, which may affect future investment.
ESG		The industry is highly exposed to CO^2 emissions and possible workforce injuries.

Momentum price		Price momentum is negative.
Momentum earnings		In the last three months, earnings for the next financial year have been revised downwards by 7.4%.
Piotroski score		Sasol's Piotroski score ranks 5 out of 9.

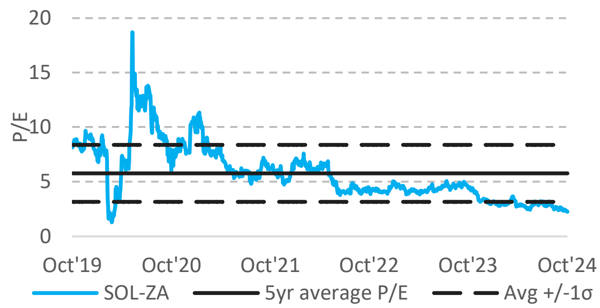
Sources: PSG Wealth research team, FactSet and company financials

Table 5: Company data

52-week high	R240.84
52-week low	R97.93
Market value (bn)	R68.1
Price momentum	Negative
3m earnings revision	-7.4%
Fiscal year end	2025/06/30

Source: FactSet

Graph 14: Price to earnings



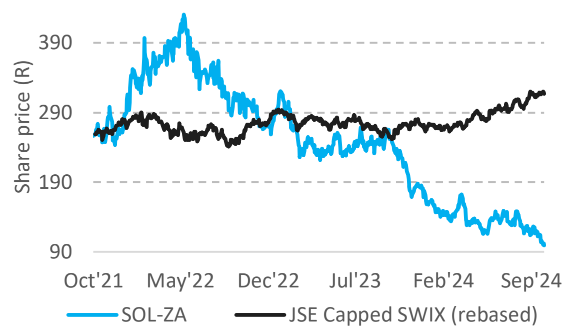
Source: FactSet

Table 6: Valuation multiples

Multiple	*Latest:*	*Last note:*
	Nov-2024	Feb-2024
P/E	2.3x	2.9x
P/S	0.3x	0.3x
P/B	0.4x	0.4x
P/CF	1.4x	1.8x
EV/EBITDA	2.6x	2.7x
EV/EBIT	3.5x	3.5x
EV/SALES	0.6x	0.6x
Dividend yield	6.2%	11.9%
FCF yield	-	21.0%

Source: FactSet

Graph 15: Share price history vs benchmark



Source: FactSet

Table 7: Performance versus benchmark

Period	YTD	MTD	3M	6M	1Y	2Y	3Y	5Y	10Y
Sasol Limited	-43.4%	6.9%	-21.7%	-19.1%	-54.8%	-66.0%	-60.5%	-62.6%	-80.7%
JSE Capped SWIX	12.1%	1.0%	6.9%	12.9%	19.1%	19.6%	20.8%	39.2%	40.9%

Source: FactSet

Table 8: Key financials and ratios

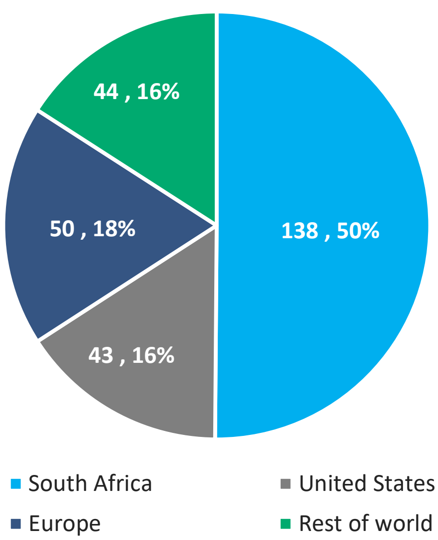
Income statement (ZAR bn)	2019	2020	2021	2022	2023	2024		5Yr CAGR	2025E	2026E
Turnover	203.6	190.4	201.9	272.7	289.7	275.1		6.21%	265.8	281.8
Y/Y growth (%)	-	*-6.5*	*6.1*	*35.1*	*6.2*	*-5.0*			*-3.4*	*6.0*
Gross income	107.2	94.3	111.2	142.6	128.7	127.9		3.59%	-	-
Y/Y growth (%)	-	*-12.1*	*17.9*	*28.3*	*-9.8*	*-0.6*			-	-
Adjusted EBITDA	47.6	35.0	48.4	71.8	66.3	60.0		4.73%	58.2	68.3
Y/Y growth (%)	-	*-26.6*	*38.4*	*48.4*	*-7.7*	*-9.5*			*-3.0*	*17.3*
L/EBIT	8.4	-111.9	16.6	61.4	21.5	-27.3		N.M.	-	-
Y/Y growth (%)	-	*N.M.*	*N.M.*	*269.6*	*-65.0*	*N.M.*			-	-
Net income	4.3	-91.8	9.0	39.0	8.8	-44.3		N.M.	-	-
Y/Y growth (%)	-	*N.M.*	*N.M.*	*331.3*	*-77.4*	*-603.1*			-	-
EPS	7.0	-148.5	14.6	62.3	14.0	-69.9		N.M.	41.4	50.9
Y/Y growth (%)	-	*N.M.*	*N.M.*	*327.9*	*-77.5*	*N.M.*			*N.M.*	*23.1*

Balance sheet and cash flow (ZAR bn)	2019	2020	2021	2022	2023	2024		5Yr CAGR	2025E	2026E
Capex	56.3	35.0	16.4	23.0	30.7	30.3		-11.65%	30.3	28.7
Cash generated by operating activities	51.4	42.4	45.1	56.1	64.6	52.3		0.36%	-	-
Free cash flow	-24.8	-12.2	15.4	18.6	20.4	8.1		N.M.	-	-
Y/Y growth (%)	-	*-50.8*	*N.M.*	*20.7*	*9.8*	*-60.3*			-	-
Cash and ST investments	16.5	35.4	32.7	43.5	55.7	48.9		24.27%	-	-
Total assets	470.0	474.5	360.7	419.5	433.8	365.0		-4.93%	-	-
ST debt	3.8	43.5	7.3	24.2	43.7	3.9		0.86%	-	-
LT debt	127.4	147.5	97.1	82.5	82.3	115.9		-1.86%	-	-

Ratios	2019	2020	2021	2022	2023	2024		5Yr Average	2025E	2026E
Gross margin (%)	52.7	49.5	55.1	52.3	44.4	46.5		49.6	-	-
EBIT margin (%)	4.1	-58.8	8.2	22.5	7.4	-9.9		-6.1	-	-
Net income margin (%)	2.1	-48.2	4.5	14.3	3.0	-16.1		-8.5	-	-
Current ratio	1.6	1.1	1.8	1.4	1.5	2.3		1.6	-	-
Borrowings to shareholders equity	63.8	139.9	82.1	55.7	63.1	82.3		84.6	-	-
ROA (%)	0.9	-19.4	2.2	10.0	2.1	-11.1		-3.3	-	-
ROE (%)	1.9	-49.5	6.1	23.2	4.6	-26.0		-8.3	-	-

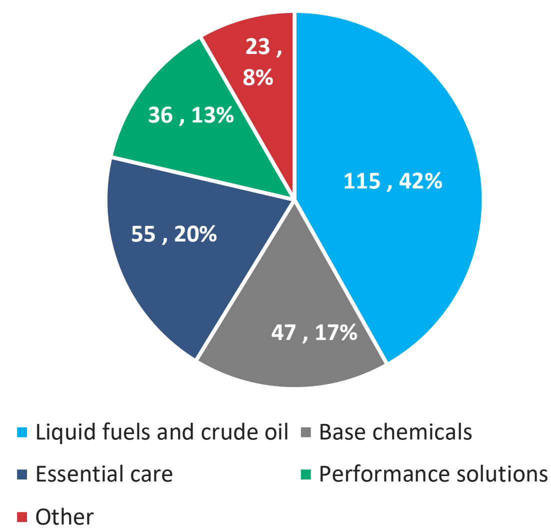
Source: FactSet E = FactSet consensus forecast

Graph 16: Revenue per geography (ZAR bn)



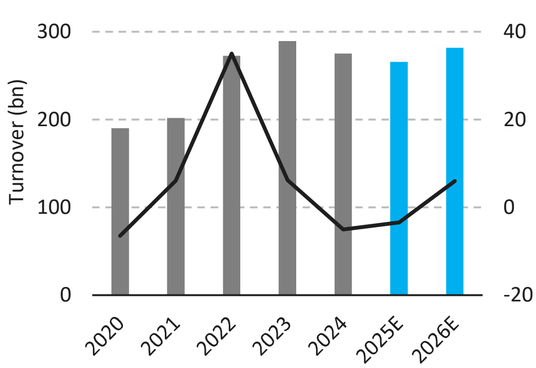
Source: 2024 full year company financials

Graph 17: Revenue per segment (ZAR bn)



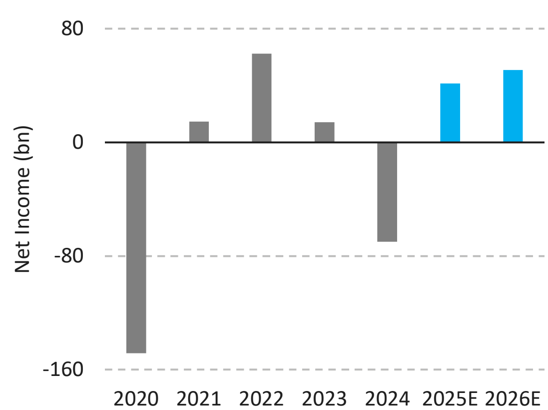
Source: 2024 full year company financials

Graph 18: Annual turnover



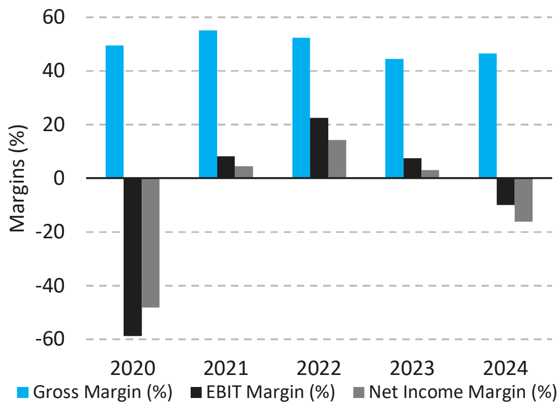
Source: FactSet E = FactSet consensus forecast

Graph 19: Annual earnings per share



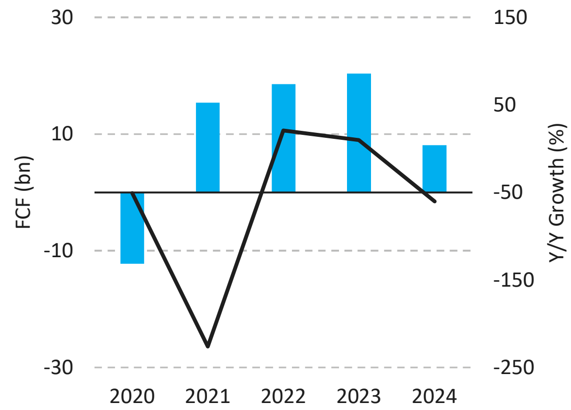
Source: FactSet E = FactSet consensus forecast

Graph 20: Gross, EBIT, net margins



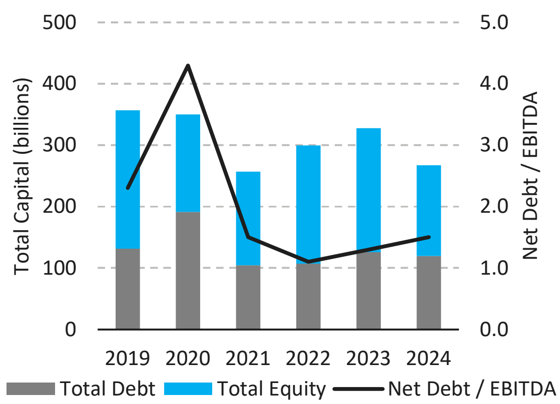
Source: FactSet

Graph 21: Free cash flow



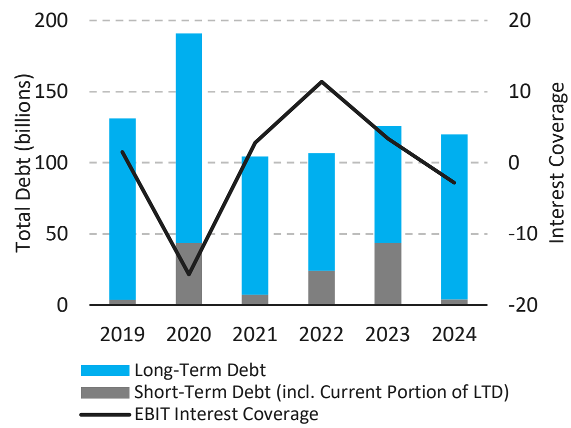
Source: FactSet

Graph 22: Capital structure and net debt/EBITDA



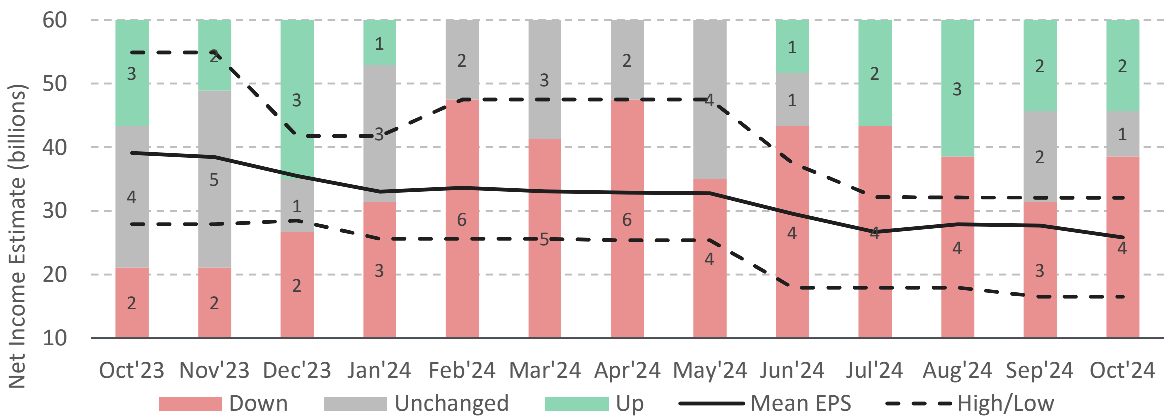
Source: FactSet

Graph 23: Total debt and interest coverage



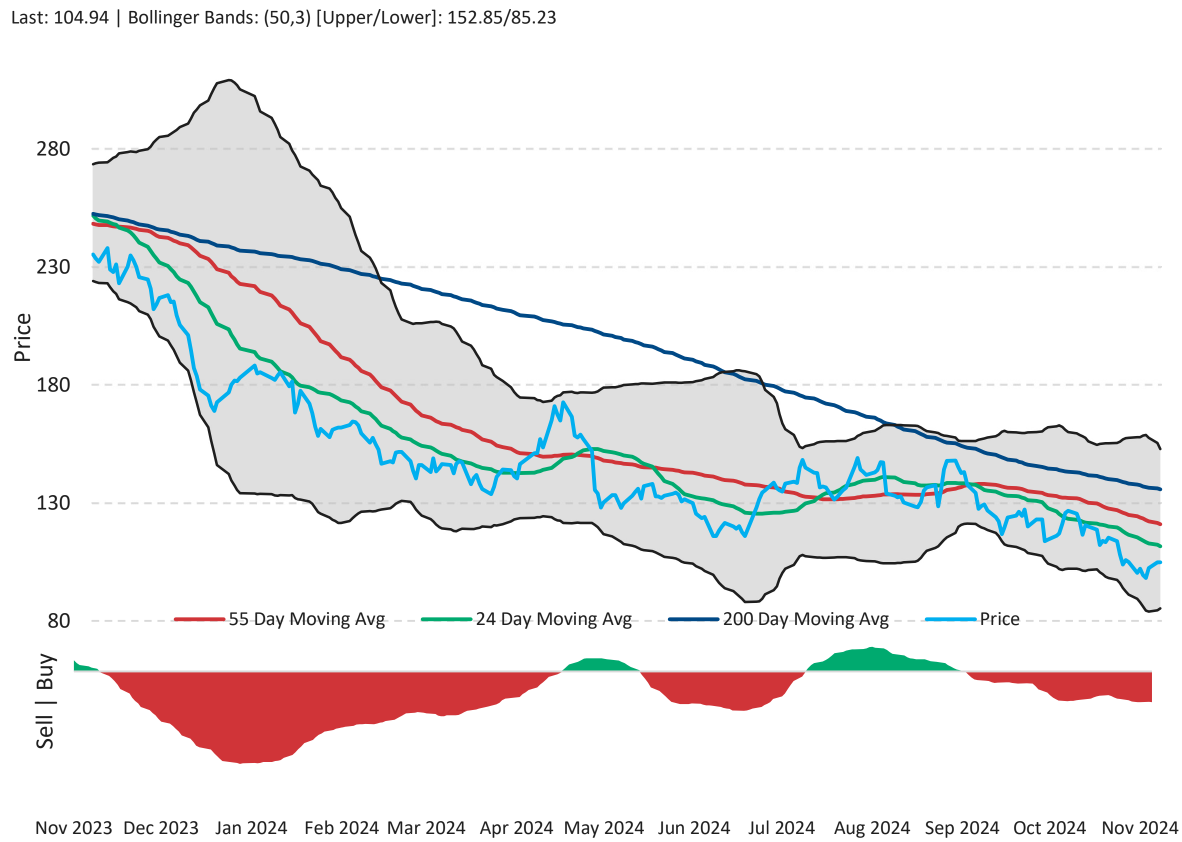
Source: FactSet

Graph 24: Earnings revision



Source: FactSet

Graph 26: Price momentum



Source: FactSet

Contact details

Pierre Muller, CA(SA), CFA
Equity Analyst
+27 (11) 996 5200
Pierre.Muller@psg.co.za

Vaughan Henkel, CFA
Head of Equity Research
+27 (11) 996 5200
Vaughan.Henkel@psg.co.za

The purpose of this document is to provide information and is not available for external distribution.

About PSG Wealth recommendations
PSG Wealth provides medium- to long-term recommendations based on the premium or discount that a company trades at, relative to our estimation of intrinsic value. We expect companies to rerate towards their intrinsic value over a one- to three-year period.

House view guidance: House view guidance is indicative only. Each client's circumstances are different, and it remains critical that indicative guidance is discussed with your portfolio manager or financial adviser.

*Share price as at closing.

Analyst certification
The research analyst who prepared this report certifies that the view expressed herein accurately reflects the research analyst's personal views about the subject, security and issuer and that no part of their compensation was, is or will be directly or indirectly related to specific recommendations or opinions contained in this report.

FSP
PSG Investment Management (Pty) Ltd is an authorised financial services provider. FSP: 44306
PSG Securities Limited is an authorised member of the JSE and authorised financial services provider. FPS: 42996