'Like a Swiss ski slope:' Uncertainty clouds battered Sasol's investment outlook


A view of Sasol's Secunda plant (Sasol/Supplied)

- **Chemicals and energy giant Sasol is under pressure as the group grapples with several major challenges, including its status as SA's second-biggest emitter after Eskom.**
- **Many market watchers believe the share price is low for good reason, but others see a buying opportunity.**
- **It's yet to be seen if the group's management team, led by new CEO Simon Baloyi, can turn the operational troubles around.**
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The new CEO of Sasol, Simon Baloyi, has been in the hot seat for only one month, but it has already been a bit of a rollercoaster ride.

News of reprieve of certain emissions standards related to sulphur dioxide from Sasol operations bolstered the company share price earlier in April.

But a subsequent production update reporting continued operational issues at Sasol coal mines, affecting synthetic fuels production, provoked a seemingly outsized negative response, and the share has fallen more than 12% in the past month.

At R133 per share currently, the market price is a far cry from the over R600 it fetched in 2014, when investor outlook for the company was at its rosiest.

Now valued at about R85.7 billion, Sasol's shares have slumped by more than 42% in the past year.

But given its decline, is it a good buy?

Jean Pierre Verster, CEO and founder of Protea Capital Management, who decided a year ago that Sasol is uninvestable, still says "no".

He adds:

> The problem with cheap shares is that they can stay cheap and get even cheaper if the company is not a high-quality company, and it actually destroys value. We call that a value trap.

There are a few reasons why believes Sasol is a value trap.

For one, its proprietary Fischer-Tropsch process, which converts coal into petroleum, is a very dirty process.

"A company may be making profits, but if you add in the cost to society and the environment, maybe the company's actually not a net good for society. Maybe it shouldn't exist," he said.

Another turnoff for Verster is execution. "It just seems like things constantly go wrong. The execution at Sasol has not been good," he said. The high turnover in leadership also speaks to the execution risks, he says.

The third concern is the group's gas quandary. Its Pande and Temane gas fields in Mozambique are fast depleting, and Sasol has already warned industrial customers it will no longer supply them from mid-2026. A plan to replace the gas is yet to come together.

Says Verster:

> The alarm bells are ringing.

His final reason is Lake Charles – a multi-billion-dollar investment in the US which turned out to be disastrous for the company when the project experienced delays and enormous cost overruns.

Verster said Sasol not only spent too much money on it, but then sold half the project right at the bottom of the investment cycle when the valuation was very low. "They needed to do that to save themselves from a rights issue … But that obviously, permanently impaired the value," he said.

Through its remaining 50% share in Lake Charles, Sasol produces the raw material from which plastics are made - another product that the world has come to realise is not good for the environment and could be a net cost to society, he said.

"So, the fact that they diversified away from a dirty coal process to, in my mind, a dirty plastics process … they sort of went out of the frying pan into the fire.

"Even though the share might seem optically cheap, it's inevitably a value trap, in my opinion," he said.

Recovery punt?

Petri Redelinghuys of Herenya Capital Advisors is, however, "very bullish" on Sasol, which he believes presents an opportunity currently being overlooked by the market.

"Sasol is a good business. It's had a bad run with a whole bunch of production problems, but I think these are short-term things that can be fixed," said Redelinghuys.

"A much larger component of their earnings is also now from chemicals, and in that market, there's been lower demand for its product." This is due to weakness in Europe and China, which is impacting demand in the highly cyclical chemicals market. Even so, the group "still prints money," he said.

Redelinghuys said there have there been key developments in its favour. The emissions ruling was an important one.

Another hugely positive development is that the group has secured long-term water use licence for its Syferfontein Colliery – another matter, like the emissions issue – which the company successfully took on appeal.

When it comes to shares like Sasol, Redelinghuys believes the market is fixated on the ESG aspects, but if earnings revive to between R50 and R65 a share – as Herenya expects it will – the fair value of the share price will be significantly higher.

"On a six [price-to-earnings ratio], you're looking at R360 rand a share. And historically, Sasol runs at a 10 PE," he said, referring to a measure used by analysts to gauge how expensive a share is.

Underperformance

But Sasfin's David Shapiro said things have just been going the wrong way for Sasol ever since the Lake Charles fiasco.

The $12.8 billion (about R240 billion) spend and the fact and that Sasol is now worth over R80 billion today gives some idea of the value destruction, said Shapiro.

"If you're looking over 10 years, it's just been one disaster after another. The share price, it's been absolutely pummelled," he said, adding:

> If you look at the chart, it looks like a Swiss ski slope, it's just going down. It tells you how people are thinking, and there are more sellers than buyers, as simple as that sounds.

With oil prices bobbing between $80 and $90 a barrel and the rand dollar exchange rate close to 19, Sasol ought to be doing pretty well.

"This is a company that shouldn't be where it is at the moment. It should be doing a lot better," Shapiro said. "Sasol's production facility that takes advantage of that, but we are not seeing those benefits come through."

The issues appear to be structural, he said. "They are always under pressure," he said.

The question now is whether the management team can turn things around, Shapiro said. "At the moment, the market is saying 'nothing's going to change' and is selling them down", he noted.

Abdul Davids, head of research at Camissa Asset Management, said the main concern is around Sasol's balance sheet.

"Excluding the Covid pandemic period, this is the highest level of rand oil prices that Sasol has ever seen. They should be printing money. But the problem is that the balance sheet is constrained because of high debt levels," he said.

Despite an asset sales programme, which ran from 2020 to 2022, its balance sheet never properly recovered from the Lake Charles debacle.

"The asset sales programme wasn't sufficient to really extinguish all the debts. And then with low oil prices, for two or three years, the losses increased," Davids said.

There is concern that it might not be able to service its debt. Added to that is the operational instability which sees the group producing 7 million tonnes of synthetic fuels, down from 7.8 million tonnes just two years ago. Meanwhile, inflation would have pushed up wages and other costs.

"I think there is very little confidence in Sasol's ability to not only operationally improve but also benefit from the positive macroeconomic environment with higher oil prices," Davids said.

The full-year numbers will reveal whether cash flow is sufficient to cover its debt servicing costs, he said.