Morgan Stanley

MORGAN STANLEY RESEARCH
ASIA/PACIFIC

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October 21, 2008

Stock Rating
Equal-weight

Industry View
No Rating

Taiwan Fertilizer Co Ltd

3Q08 Earnings Could Disappoint Again

Quick Comment: We believe Taiwan Fertilizer's (Taifer) 3Q08 results could surprise on the downside again due to lower shipments at its Al Jubail JV. Taifer indicated that the bulk of 2-EH shipments was delayed until October, causing the sales to be booked in 4Q08 instead. As such, despite average urea, 2-EH, and DOP pricings are 33%, 3%, and 4% higher in 3Q08 than that of 2Q08, we estimate that Al Jubail JV's earnings contribution could decline from 2Q08's NT$1.3b to 3Q08's NT$1.2b, missing market expectation of NT$1.5-1.6b. We expect the market to read this negatively as this is the second consecutive quarter that Taifer has missed its earnings. With the earnings of Al Jubail JV failing to reflect the rising product pricings, we believe investors may start to apply a bigger discount to the stock's NAV to incorporate higher execution risk and lower transparency. In view of the likely 3Q08 miss and investors' growing concerns, we believe the stock needs more than just 'undemanding valuation' to perform again. We look for Taifer to trade in the range of NT$40-50 before new catalysts emerge. We hence retain an Equal-weight rating on the stock.

Freefalling Urea Pricing: The latest urea spot price plunged 37% over the past week to US$347.5/ton due to frozen credit market and concerns over an oversupply situation in 2009. Given the larger than expected pricing fall, we see downside to our 2008e urea assumption of US$608/ton (current YTD average is US$587/ton). Both 2-EH and DOP pricings also fell 11% and 8%, respectively. Our view remains intact that Al Jubail JV's earnings should peak in 2H08.

Key Ratios and Statistics

Reuters: 1722.TW Bloomberg: 1722 TT
Taiwan Mid Cap

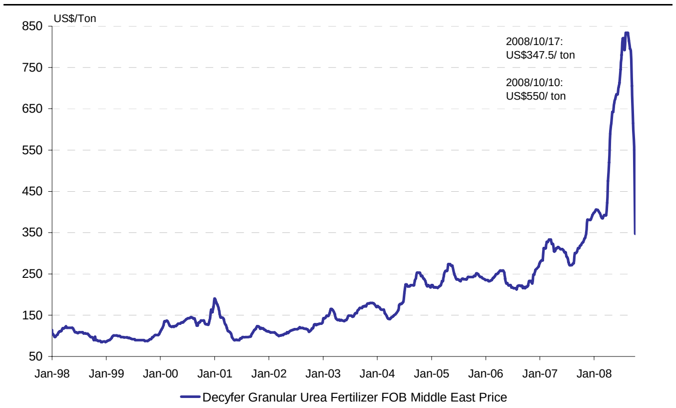
Price target	NT$73.00
Upside to price target (%)	61
Shr price, close (Oct 21, 2008)	NT$45.30
52-Week Range	NT$161.50-40.70
Sh out, dil, curr (mn)	980
Mkt cap, curr (mn)	NT$44,394
EV, curr (mn)	NT$34,842
Avg daily trading volume (mn)	NT$1,477

Fiscal Year ending	12/07	12/08e	12/09e	12/10e
ModelWare EPS (NT$)	3.58	4.75	4.81	5.20
Consensus EPS (NT$)§	3.83	4.55	4.82	4.65
Revenue, net (NT$ mn)	11,799	18,075	19,848	21,397
EBITDA (NT$ mn)	4,418	6,293	6,243	6,735
ModelWare net inc (NT$ mn)	3,508	4,658	4,713	5,096
P/E	22.2	9.5	9.4	8.7
P/BV	1.5	0.8	0.8	0.8
RNOA (%)	9.9	13.8	11.7	11.4
ROE (%)	7.0	8.9	8.8	9.3
EV/EBITDA	15.5	6.4	7.2	7.4
Div yld (%)	3.8	6.6	8.1	8.1
FCF yld ratio (%)	4.0	0.0	4.3	(1.2)
Leverage (EOP) (%)	(26.2)	(15.5)	(7.8)	0.6

Unless otherwise noted, all metrics are based on Morgan Stanley ModelWare framework (please see explanation later in this note).
§ = Consensus data is provided by FactSet Estimates.
e = Morgan Stanley Research estimates

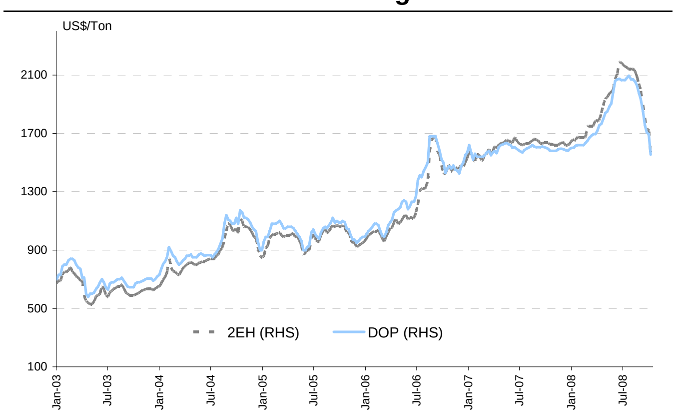
Slow Selling Rate at R13 Residential Project: There has been confusion on the actual selling rate at Taifer's R13 residential project at Nangang District. The latest selling rate guided by management is 40%. However, in reality, Taifer has only sold around 20-25% of the units. Our check suggests that out of the 110 available units, about 20 units are allocated to other private landowners of the R13 site. Hence, these units should not be classified as 'sold'. The total available units for sale by Taifer are only about 90 units, of which only 20 something units are being sold by the presale agent thus far. If the R13 project cannot be closed before end of 2008, we are afraid that Taifer may not be able to book 20% of the project revenue in 4Q08, hence implying a downside of NT$246m in profits or 4% of the company's 2008e pretax income.

Exhibit 1
Urea Price is now 58% off the Peak



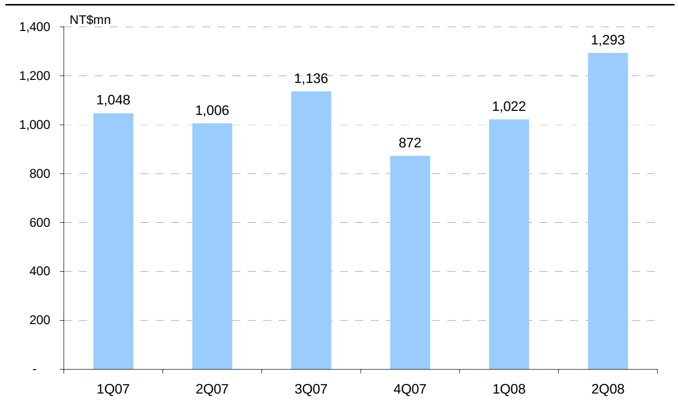
Source: Bloomberg

Exhibit 2
2EH and DOP Price Also Falling



Source: Bloomberg

Exhibit 3
Al Jubail JV Earning Should Peak in 2H08



Source: Company data, Morgan Stanley Research

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Company Description

Established in 1946. Taiwan Fertilizer was originally a state-owned enterprise under the Ministry of Economic Affairs, privatized in 1999, and is now a listed private corporation. The company has core business of producing various types of fertilizers and chemical products and also establishes business operation in optoelectronics and biotechnology to improve overall competitiveness.

Taiwan Mid Cap

Industry View: No Rating

MSCI Country: Taiwan

Asia Strategist's Recommended Weight: 12.5%
MSCI Asia/Pac All Country Ex Jp Weight: 12.6%

MORGAN STANLEY ModelWare	**Morgan Stanley ModelWare is a proprietary analytic framework that helps clients uncover value, adjusting for distortions and ambiguities created by local accounting regulations.** For example, ModelWare EPS adjusts for one-time events, capitalizes operating leases (where their use is significant), and converts inventory from LIFO costing to a FIFO basis. ModelWare also emphasizes the separation of operating performance of a company from its financing for a more complete view of how a company generates earnings.

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(as of September 30, 2008)

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	Coverage Universe		Investment Banking Clients (IBC)		
Stock Rating Category	Count	% of Total	Count	% of Total IBC	% of Rating Category
Overweight/Buy	**892**	**40%**	**292**	**44%**	**33%**
Equal-weight/Hold	**937**	**42%**	**278**	**42%**	**30%**
Underweight/Sell	**387**	**17%**	**90**	**14%**	**23%**
Total	**2,216**		**660**		

Data include common stock and ADRs currently assigned ratings. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations. Investment Banking Clients are companies from whom Morgan Stanley or an affiliate received investment banking compensation in the last 12 months.

Analyst Stock Ratings

Overweight (O or Over) - The stock's total return is expected to exceed the total return of the relevant country MSCI Index, on a risk-adjusted basis over the next 12-18 months.

Equal-weight (E or Equal) - The stock's total return is expected to be in line with the total return of the relevant country MSCI Index, on a risk-adjusted basis over the next 12-18 months.
Underweight (U or Under) - The stock's total return is expected to be below the total return of the relevant country MSCI Index, on a risk-adjusted basis, over the next 12-18 months.
More volatile (V) - We estimate that this stock has more than a 25% chance of a price move (up or down) of more than 25% in a month, based on a quantitative assessment of historical data, or in the analyst's view, it is likely to become materially more volatile over the next 1-12 months compared with the past three years. Stocks with less than one year of trading history are automatically rated as more volatile (unless otherwise noted). We note that securities that we do not currently consider "more volatile" can still perform in that manner.
Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

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Attractive (A): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.
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Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index.
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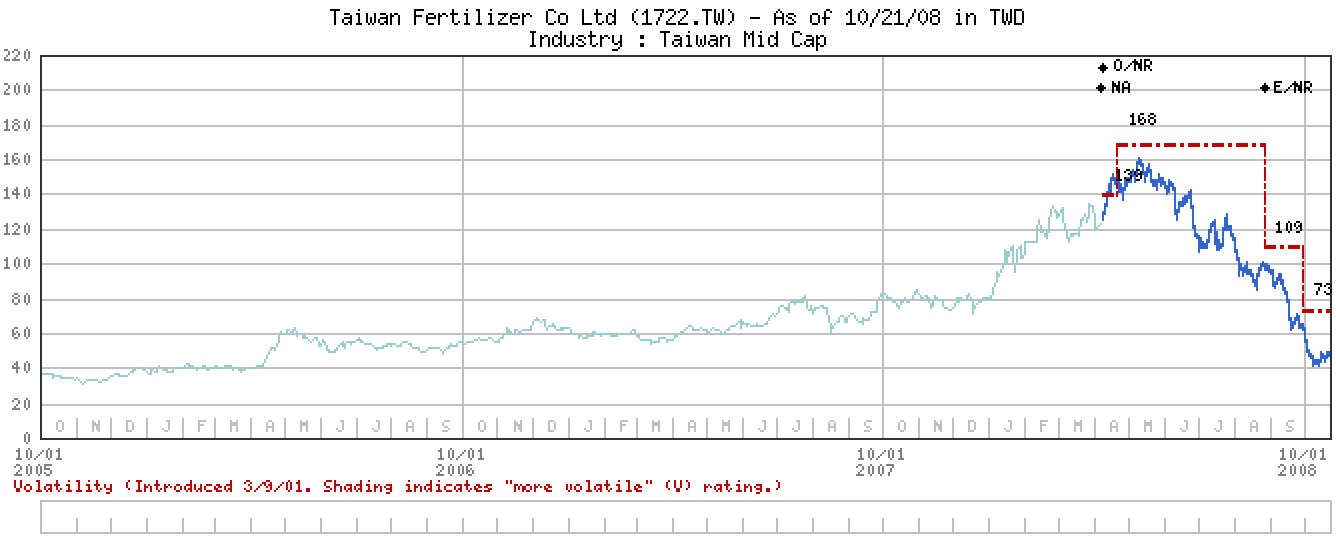
Stock Price, Price Target and Rating History (See Rating Definitions)



Stock Rating History: 4/7/08 : NA; 4/8/08 : O/NR; 8/26/08 : E/NR

Price Target History: 4/8/08 : 139; 4/21/08 : 168; 8/26/08 : 109; 9/29/08 : 73

Source: Morgan Stanley Research   Date Format : MM/DD/YY   Price Target --   No Price Target Assigned (NA)
Stock Price (Not Covered by Current Analyst)   Stock Price (Covered by Current Analyst)
Stock Ratings abbreviated as below (Effective 3/18/02, ratings appear as Stock Ratings/Industry View) ◆
Stock Ratings as of 3/18/02: Overweight (O) Equal-weight (E) Underweight (U) More Volatile (V) No Rating Available (NAV)
Stock Ratings prior to 3/18/02: Strong Buy (SB) Outperform (OP) Neutral (N) Underperform (UP) No Rating Available (NAV)
Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

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Industry Coverage:Taiwan Mid Cap

Company (Ticker)	Rating (as of)	Price (10/21/2008)
Jeremy C Chen		
Far Eastern Textile Ltd. (1402.TW)	E (06/19/2008)	NT$19.45
Taiwan Fertilizer Co Ltd (1722.TW)	E (08/26/2008)	NT$45.3

Stock Ratings are subject to change. Please see latest research for each company.