

COMPANY UPDATE

Formosa Petrochemical Corp. (6505.TW)

Sell

Margin deterioration may lead to substantial net loss in 4Q08**What's changed**

Followed by the 27% mom decline in WTI oil prices in October, there were 25%-43% mom declines for various oil product prices in October. However, as the crude oil inventory cost for FPCC is based on two-thirds of the cost in the previous month and one-third of the cost in the current month, we believe this should lead to a significant net loss for FPCC in October, and expect the losses to continue into November and December if the oil price continues to fall. We remain cautious on the stock.

Implications

Assuming FPCC's crude oil cost in October was around US\$95/bbl, and the October oil product prices reflect the WTI oil price in October (around US\$76/bbl), we estimate FPCC could incur NT\$9-NT\$10 bn in net losses in October (it generally processes around 15 mn barrels of crude oil per month). Therefore, every US\$1/bbl decline in the crude oil price per month should lead to a NT\$500 mn loss for the company, by our estimate. We think there might be 40%-50% downside to our current 2008 net earnings estimate if the WTI oil price stays below the US\$60/bbl level. Even with the accounting method changing from LIFO to weighted average in 2009E, we do not expect much earnings upside unless we see a significant oil price rebound.

Valuation

The stock is currently trading at 9.4X 2009E EV/EBITDA, an 81% premium over the regional median of 5.2X 2009E EV/EBITDA. We maintain our Conviction Sell, with a 12-month SOTP-based target price of NT\$46.00.

Key risks

Sharp rebound in both crude oil and oil product prices in the near term.

Impact on related securities

Given the cross holding structure, we believe there may be 25%-30% downside to our current 2008 net earnings estimates for FPC (1301.TW, Sell), NYPC (1303.TW, Sell), and FCFC (1326.TW, Sell).

INVESTMENT LIST MEMBERSHIP

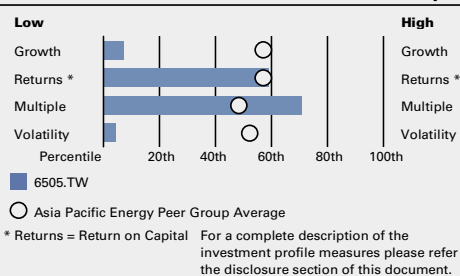
Asia Pacific Sell List

Asia Pacific Conviction Sell List

Coverage View: NeutralTaiwan:
Oil

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Investment Profile: Formosa Petrochemical Corp.

Key data	Current
Price (NT\$)	72.00
12 month price target (NT\$)	46.00
Market cap (NT\$ mn / US\$ mn)	665,892.3 / 20,185.9
Foreign ownership (%)	6.9

	12/07	12/08E	12/09E	12/10E
EPS (NT\$)	7.53	5.94	4.72	3.83
EPS growth (%)	56.5	(21.1)	(20.6)	(18.9)
EPS (diluted) (NT\$)	7.53	5.94	4.72	3.83
EPS (basic pre-ex) (NT\$)	7.53	5.94	4.72	3.83
P/E (X)	9.6	12.1	15.3	18.8
P/B (X)	2.6	2.5	2.4	2.4
EV/EBITDA (X)	9.7	8.8	9.4	10.3
Dividend yield (%)	9.3	6.6	5.2	4.3
ROE (%)	29.3	21.1	16.3	12.8

Price performance chart

Share price performance (%)	3 month	6 month	12 month
Absolute	(9.9)	(24.1)	(24.7)
Rel. to Taiwan SE Weighted Index	48.1	53.8	48.1

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 11/13/2008 close.

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Formosa Petrochemical Corp.: Summary financials

Profit model (NT\$ mn)	12/07	12/08E	12/09E	12/10E	Balance sheet (NT\$ mn)	12/07	12/08E	12/09E	12/10E
Total revenue	699,313.9	899,559.1	885,369.7	887,929.2	Cash & equivalents	10,511.0	10,794.7	10,624.4	13,318.9
Cost of goods sold	(592,541.0)	(791,851.0)	(787,888.2)	(796,974.0)	Accounts receivable	80,040.6	103,449.3	101,817.5	102,111.9
SG&A	(9,764.8)	(12,585.5)	(11,501.5)	(14,198.6)	Inventory	52,368.3	71,964.7	70,829.6	88,792.9
R&D	(8.3)	(8.3)	(8.3)	(8.3)	Other current assets	44,537.9	47,991.2	47,707.4	48,258.6
Other operating profit/(expense)	0.0	0.0	0.0	0.0	Total current assets	187,457.7	234,199.9	230,978.9	252,482.3
EBITDA	96,999.8	95,114.2	85,971.7	76,748.3	Net PP&E	281,963.0	276,205.4	250,600.9	224,389.1
Depreciation & amortization	(20,846.6)	(34,193.0)	(35,346.9)	(36,512.4)	Net intangibles	0.0	0.0	0.0	0.0
EBIT	76,153.2	60,921.3	50,624.9	40,235.9	Total investments	16,462.1	19,892.0	21,198.1	22,734.6
Interest income	126.3	126.3	126.3	126.3	Other long-term assets	5,201.8	6,243.6	7,287.4	8,333.4
Interest expense	(4,259.9)	(4,417.5)	(4,545.2)	(3,574.1)	Total assets	491,084.7	536,540.9	510,065.3	507,939.4
Income/(loss) from uncons. subs.	3,344.1	3,429.9	1,306.1	1,536.5	Accounts payable	21,466.9	35,982.4	35,414.8	35,517.2
Others	3,165.6	1,000.0	1,000.0	1,000.0	Short-term debt	41,752.7	38,186.2	38,186.2	38,186.2
Pretax profits	78,529.2	61,059.9	48,512.0	39,324.6	Other current liabilities	35,132.8	50,573.6	49,779.0	49,922.3
Income tax	(8,918.4)	(6,106.0)	(4,851.2)	(3,932.5)	Total current liabilities	98,352.5	124,742.2	123,380.0	123,625.7
Minorities	0.0	0.0	0.0	0.0	Long-term debt	131,224.4	144,739.7	110,802.6	101,256.5
Net income pre-preferred dividends	69,610.8	54,953.9	43,660.8	35,392.1	Other long-term liabilities	3,309.3	3,336.5	3,428.0	3,524.1
Preferred dividends	0.0	0.0	0.0	0.0	Total long-term liabilities	134,533.7	148,076.1	114,230.6	104,780.6
Net income (pre-exceptionals)	69,610.8	54,953.9	43,660.8	35,392.1	Total liabilities	232,886.2	272,818.3	237,610.6	228,406.3
Post-tax exceptionals	0.0	0.0	0.0	0.0	Preferred shares	0.0	0.0	0.0	0.0
Net income	69,610.8	54,953.9	43,660.8	35,392.1	Total common equity	258,198.6	263,722.6	272,454.7	279,533.1
EPS (basic, pre-except) (NT\$)	7.53	5.94	4.72	3.83	Minority interest	0.0	0.0	0.0	0.0
EPS (basic, post-except) (NT\$)	7.53	5.94	4.72	3.83	Total liabilities & equity	491,084.7	536,540.9	510,065.3	507,939.4
EPS (diluted, post-except) (NT\$)	7.53	5.94	4.72	3.83	BVPS (NT\$)	27.92	28.52	29.46	30.22
DPS (NT\$)	6.70	4.75	3.78	3.06					
Dividend payout ratio (%)	89.0	80.0	80.0	80.0					
Free cash flow yield (%)	9.5	6.7	11.6	7.2					
Growth & margins (%)	12/07	12/08E	12/09E	12/10E	Ratios	12/07	12/08E	12/09E	12/10E
Sales growth	32.1	28.6	(1.6)	0.3	ROE (%)	29.3	21.1	16.3	12.8
EBITDA growth	34.5	(1.9)	(9.6)	(10.7)	ROA (%)	15.0	10.7	8.3	7.0
EBIT growth	42.5	(20.0)	(16.9)	(20.5)	ROACE (%)	17.9	13.7	11.3	9.4
Net income growth	56.5	(21.1)	(20.6)	(18.9)	Inventory days	30.9	28.7	33.1	36.6
EPS growth	56.5	(21.1)	(20.6)	(18.9)	Receivables days	33.8	37.2	42.3	41.9
Gross margin	15.3	12.0	11.0	10.2	Payable days	11.8	13.2	16.5	16.2
EBITDA margin	13.9	10.6	9.7	8.6	Net debt/equity (%)	62.9	65.3	50.8	45.1
EBIT margin	10.9	6.8	5.7	4.5	Interest cover - EBIT (X)	18.4	14.2	11.5	11.7
Cash flow statement (NT\$ mn)	12/07	12/08E	12/09E	12/10E	Valuation	12/07	12/08E	12/09E	12/10E
Net income pre-preferred dividends	69,610.8	54,953.9	43,660.8	35,392.1	P/E (analyst) (X)	9.6	12.1	15.3	18.8
D&A add-back	20,846.6	34,193.0	35,346.9	36,512.4	P/B (X)	2.6	2.5	2.4	2.4
Minorities interests add-back	0.0	0.0	0.0	0.0	EV/EBITDA (X)	9.7	8.8	9.4	10.3
Net (inc)/dec working capital	11,951.7	(10,812.0)	10,723.0	(11,948.2)	Dividend yield (%)	9.3	6.6	5.2	4.3
Other operating cash flow	(3,344.1)	(3,429.9)	(1,306.1)	(1,536.5)					
Cash flow from operations	99,065.1	74,904.9	88,424.6	58,419.8					
Capital expenditures	(21,684.1)	(26,358.9)	(7,166.0)	(7,224.3)					
Acquisitions	3,118.6	0.0	0.0	0.0					
Divestitures	0.0	0.0	0.0	0.0					
Others	(11,233.2)	(2,221.2)	(3,620.2)	(4,122.4)					
Cash flow from investments	(29,798.7)	(28,580.1)	(10,786.2)	(11,346.7)					
Dividends paid (common & pref)	(26,685.8)	(61,932.7)	(43,963.1)	(34,928.6)					
Inc/(dec) in debt	(39,386.7)	15,891.5	(33,845.6)	(9,450.0)					
Common stock issuance (repurchase)	0.0	0.0	0.0	0.0					
Other financing cash flows	0.0	0.0	0.0	0.0					
Cash flow from financing	(66,072.5)	(46,041.2)	(77,808.7)	(44,378.6)					
Total cash flow	3,193.9	283.7	(170.3)	2,694.5					

Note: Last actual year may include reported and estimated data.
Source: Company data, Goldman Sachs Research estimates.

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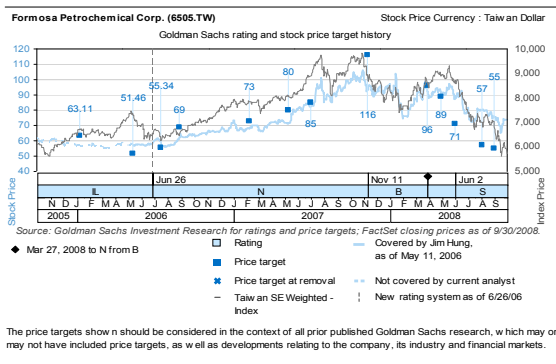
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Price target and rating history chart(s)



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