

November 30, 2010

Market Outperform / Speculative Risk

A visit to the recently acquired U.S. subsidiary, M2P2.

MARKET DATA	11/30/2010
Price	\$2.44
Exchange	NASDAQ
Target Price	\$6.00
52 Wk Hi - Low	\$5.69 - \$2.12
EV(MM)	\$174.6
Market Cap(MM)	\$125.3
Shares Out (MM)	51.4
Public Mkt Float (MM)	26.8
Avg. Daily Vol	843,636.0

BALANCE SHEET METRICS	
Cash (MM)	\$19.1
LTD (MM)	\$0.0
Total Debt/Total Equity	NA
Debt/Capital	NA
Price/Book Value	0.9x
Book Value/Share	\$2.81

EARNINGS DATA (\$)			
FY - Dec	2009E	2010E	2011E
Q1 (Mar)	0.08	0.02A	0.11
Q2 (Jun)	0.03	(0.07)A	0.12
Q3 (Sep)	0.07	(0.43)A	0.13
Q4 (Dec)	0.08	0.03	0.14
Full Year EPS	0.26	(0.44)	0.50

INDICES	
DJIA	10,979.3
SP-500	1,178.2
NASDAQ	2,118.6
Russell 2000	723.4



We are reiterating our Market Outperform rating, estimates and target price of \$6 following a visit to M2P2, AgFeed's recently acquired U.S. subsidiary. M2P2 LLP is a key supplier to Hormel (HRL, Not Rated) and one of the largest pork producers in the U.S., with an annual production capacity of 1,300,000 market hogs. The acquisition is immediately accretive to the company earnings with the estimated top line contribution of approximately \$180 million annually. More importantly, by acquiring M2P2, AgFeed gained a partner that will help it to build a sustainable and profitable business in China.

AgFeed is currently trading at 5x our FY11 our fully diluted EPS estimate of \$0.50. Given the company's genetics program, adoption of western production practices, improving pricing environment for hogs, and the positive impact of M2P2 acquisition, we believe the company's shares are undervalued. We reiterate our Market Outperform/Speculative Risk rating and a price target of \$6 based on the the shares attaining a P/E level of 12x our FY11 fully diluted EPS estimate.

Discussion

M2P2 Acquisition: AgFeed completed the acquisition of M2P2 in September 2010 for an aggregate amount of \$25.6 million consisting of \$11.3 million in cash, 1.2 million in AgFeed common stock, and a promissory note for approximately \$8.9 million. The shares issued to M2P2 are subject to a lock-up period ending on the 18 month anniversary of the closing of the transaction.

AgFeed is now the 23rd largest pork producer in the U.S. Following the acquisition of M2P2, AgFeed has been ranked as the 23rd largest pork producer in the U.S. according to the 2010 U.S Pork Powerhouses, an annual industry ranking published by Meridith Corporation. M2P2, headquartered in Ames, Iowa has three sow facilities (in North Carolina, Colorado and Oklahoma) and finishing facilities in Iowa. The company is a major supplier to Hormel producing 1.3 million market hogs or 345 million pounds of pork annually.

What does AgFeed (and its shareholders) get from this acquisition? Per AgFeed management, the acquisition will add \$180 million in revenues to the company's top line on an annualized basis. Our 4Q10 and FY11 estimates include a \$45 million and \$180 million revenue contribution from M2P2. We believe there is a potential upside to these numbers if AgFeed decides to expand its U.S. operations.

Moreover, we can expect reduced volatility in the company's hog revenues as there is little correlation between the hog cycles in China and U.S. However, the most important contribution that M2P2 brings to AgFeed is the production "know how". M2P2 yields are considerably above AgFeed's comparative metrics in China. We believe AgFeed is gradually incorporating M2P2's production methods, quality controls, and risk management techniques into its China hog operations. This should help AgFeed to build a highly efficient production system able to generate constant flow of verifiably safe pork in China.

What we visited, what we saw, and who we met We visited the North Carolina sow farm, one of the three sow farms owned by M2P2, with a population of 10,000 sows. During our visit we were shown pen-gestation, farrowing (i.e. specialized units for nursing of newborn piglets) and breeding facilities. We also met with the key management personnel of M2P2 – Terry Vogel, VP of Genetics, Quality Control and System Improvements, Brian Melody, VP of Operations, and Mark McCulley, VP of Strategic Relations.

The Company's North Carolina sow farm, built in 2008, is a state of the art facility featuring fully automated feeding systems, sensor/central computer wireless network transmitting data on pig's feed intake and weight gain, systematic data collection and analysis of sows' health, gestation, fertility, breeding, productivity and farrowing units allocation, strict biosecurity protocols, isolation facilities for new gilts (unbred sows), ventilation and temperature controls and responsible and cost-saving waste management.

Substantial efficiencies and yield gains derived from scientific, data-based management of hog production result in larger harvests from the company's U.S. sow base. As China's protein industry evolves away from the traditional small scale production to commercialized, large-scale, data-driven production management, it will have to embrace western production standards and methods. These include animal nutrition programs, biosecurity protocols, better genetics, automated feeding systems and computerized data management.

Ledger agreement with Hormel limits AgFeed's exposure to commodity prices

While M2P2's arrangement with Hormel precludes the company from disclosing the details of the ledger agreement, we understand that the ledger essentially shields the company from the commodity risks guaranteeing certain income per finished pig. This means that when hog prices in the U.S. are low and most producers are losing money, M2P2 will still be profitable. On the flip side of the coin, when hog prices are high, the price per hog that M2P2 receives from Hormel will be below market. Overall we view the ledger agreement with Hormel as a positive as it ensures greater revenue stability and visibility for M2P2.

Learning from the best - How M2P2 is able to produce 26.5 marketed pigs per sow versus China's average of 16.

During our visit, we observed a number of key differences between M2P2 and Chinese production facilities. We believe AgFeed will try to bring the production efficiency at its Chinese operations closer to the U.S. levels through reproducing the M2P2 production system and procedures at its Chinese farms, especially the western-style farms under construction in Dahua and Xinyu.

- **Specialization versus China's Farrow to Finish Production Model:** Typical hog farms in China include producing sows (i.e. breeder pigs that produce piglets) and feeder or finisher pigs (i.e. meat hogs). In contrast, M2P2's sows and finisher pigs are kept at different farms. Specialized sow facilities enable higher yields and multiple separate smaller - scale finishing facilities significantly limit the impact of potential disease outbreaks. The main disadvantage of farrow to finish model is increased risk of contagion that can spread to the most valuable

production asset – sows, preventing the farmers from rapidly rebuilding the hog inventory in the event of disease.

- **Automation and computerized control systems:** Smart operating systems that track, record and analyze each sow's performance (feed intake, weight gain, health, etc.) enable M2P2 to monitor key metrics to ensure that the company is on course to achieving its production targets. Ability to produce a large number of hogs that meet leanness and other physical criteria within a specified time frame is essential for securing long-term supply contracts with large food processors.
- **Productivity:** At 26.5 marketed pigs per sow annually, M2P2 sow productivity significantly exceeds China's average of 16 (and possibly as low as 13 according to the latest data from China Animal Agriculture Association). We believe that the main reason for this production gap is not better nutrition, but superior genetics combined with sound farm management and enhanced swine health. AgFeed is targeting to improve sow productivity at its legacy farms to 18.2 births/sow by the end of 2011. Western-style farms at Dahua and Xinyu, once online, are expected to reach yields of 22-24 piglets per sow. An additional benefit of higher sow productivity is reduced feed costs – fewer sows needed to produce the required number of meat hogs means lower expenditure on feed for sows.
- **Risk management is the key to sustainable operations.** Disease outbreaks are common on pig farms but when dealt with properly tend to have limited impact on productivity. When health issues do occur, aside from treating the sick pigs, M2P2 breeds more sows so as to bring the production to normal levels quickly. Of course, prevention is the best medicine. M2P2 facilities are operated on the "all in-all out basis" meaning that after each group of pigs is finished, the facilities are completely cleaned and disinfected minimizing the odds of pathogen traveling from the preceding group of pigs to the new arrivals.
- **Humane animal husbandry is good not just for our conscience:** While we have been relieved to see sows at the North Carolina sow farm being well cared for and seeming healthy and relaxed, animal welfare is important for reasons beyond charitable. Heat and overcrowding affect animal well-being. Distressed animals do not eat or under eat, and, consequently, fall behind the "weight gain" schedules. Pigs that fail to meet specific weight targets have to be sold at a discount, denting company's revenues.

Risks

- (1) High feed costs (2) Persistently low hog prices (3) Weak consumer demand for pork (4) Swine disease (5) Execution risk (6) Regulatory risk

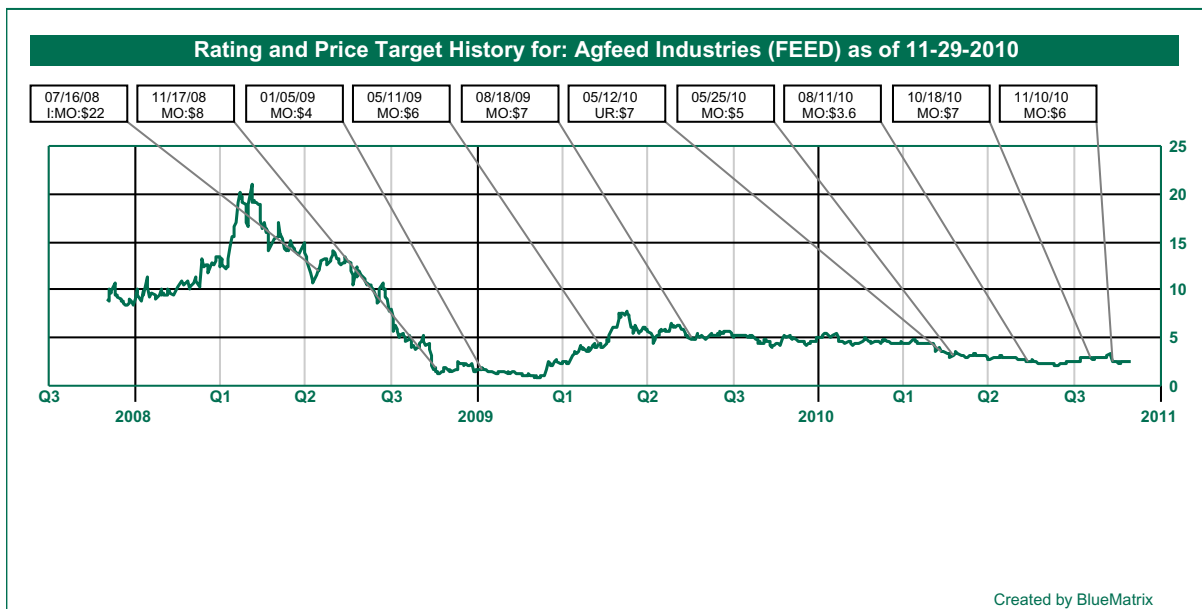
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RETURN ASSESSMENT

- Market Outperform (Buy): The common stock of the company is expected to outperform a passive index comprised of all the common stock of companies within the same sector, as defined by First Call.
- Market Perform (Hold): The common stock of the company is expected to mimic the performance of a passive index comprised of all the common stock of companies within the same sector, as defined by First Call.
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RISK ASSESSMENT

- Speculative - The common stock risk level is significantly greater than market risk. The stock price of these equities is exceptionally volatile.
- Aggressive - The common stock risk level is materially higher than market level risk. The stock price is typically more volatile than the general market.
- Moderate - The common stock is moderately risky, or equivalent to stock market risk. The stock price volatility is typically in-line with movements in the general market.



RATING SUMMARY

Distribution of Ratings Table				
Rating	Count	Percent	IB Serv./Past 12 Mos	
			Count	Percent
Market Outperform(MO)	173	75.50%	47	27.17%
Market Perform(MP)	46	20.10%	5	10.87%
Market Underperform(MU)	5	2.20%	0	0.00%
Under Review(UR)	5	2.20%	1	20.00%
Total	229	100%	53	100%

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