AFFCO HOLDINGS LIMITED

INDEPENDENT ADVISER'S REPORT

on the merits of the Takeover Offer for the Company by Talley's Group Limited

Prepared by

CAMPBELL MACPHERSON LTD

CORPORATE ADVISORS

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Glossary

AFFCO	AFFCO Holdings Limited
Alliance	Alliance Group Limited
ANZCO	ANZCO Foods Limited
BSA	Bovine Spongiform Encephalopathy or "mad cow disease"
Campbell MacPherson	Campbell MacPherson Limited
Code	the Takeovers Code
Dairy Trust	Dairy Trust Limited
DCF	discounted cash flows
Directors Committee	a committee of the AFFCO independent directors comprising Sam Lewis (Chairman), Michael McCredie and Bob Carter
EBIT	earnings before interest and tax
EBITDA	earnings before interest, tax, depreciation and amortisation
EPS	earnings per share
ETS	Emissions Trading Scheme
EU	European Union
GFC	Global financial crisis
IBD	interest bearing debt
Independent Directors	Sam Lewis (Chairman), Michael McCredie and Bob Carter
Land Meat	Land Meat New Zealand Limited
MAF	Ministry of Agriculture and Fisheries
Non-associated Shareholders	shareholders who are not associated with Talley's or Toocooya
NPAT	Net profit after tax
NPBT	Net profit before tax
NZD	New Zealand Dollar
NZSX	the main board equity security market operated by NZX
NZX	New Zealand Exchange Limited
OCD	Open Country Dairy Limited
Offer	the takeover offer by Talley's for shares in AFFCO
PPCS	PPCS Limited
SPM	South Pacific Meats Limited
Talley's	Talley's Group Limited
Toocooya	Toocooya Trust (and, as the context requires, Toocooya Nominees Limited, as nominee for the trustees of the Toocooya Trust)
USD	United States Dollar
VWAP	Volume weighted average share price

1. OVERVIEW

1.1 Introduction

AFFCO Holdings Limited (**AFFCO,** the **Company**) is a public listed company with principal business activities in the meat processing sector. The Company also holds a 35.45% equity stake in the unlisted New Zealand dairy company Open Country Dairy Limited (**OCD**). AFFCO is listed on the main board of the equity securities market (**NZSX)** operated by NZX Limited (**NZX**).

AFFCO has two substantial security holders (as defined under NZSX Listing Rules), Talley's Group Limited (**Talley's)** which holds 267,035,475 shares representing 52.83% of the voting securities, and Toocooya Nominees Limited (**Toocooya)** which holds 118,564,307 shares representing 23.46% of the voting securities. Talley's has two representatives on the Board of Directors of AFFCO, executive directors Michael and Andrew Talley, and Toocooya has 2 representatives, Arthur Young and Christopher Spencer. The balance of the board currently comprises three independent directors, Sam Lewis (Chairman), Mike McCredie and Bob Carter (**Independent Directors)**.

Talley's has been a long-term holder of AFFCO securities since it first acquired a shareholding in the Company in mid-2001. Since that time it has progressively increased its shareholding in AFFCO through a series of transactions. These transactions have included a partial takeover offer in April 2006 at 39 cents per share which resulted in Talley's increasing their shareholding to 50.01%. Michael Talley and Andrew Talley were subsequently appointed to the Board of AFFCO as Executive Directors. Since that time Talley's has marginally increased its shareholding in AFFCO to its current level of 52.83% through a series of minor on-market share purchases.

On 20 July 2010, AFFCO received formal notice of a proposed full takeover offer from Talley's (the **Offer**). On 6 August 2010 the Offer Document (**Offer Document**) was despatched to shareholders of AFFCO.

The Independent Directors of AFFCO have engaged Campbell MacPherson Limited (**Campbell MacPherson**) to prepare an Independent Adviser's Report (the **Report**) in relation to the Offer by Talley's to acquire 100% of the AFFCO equity securities that it does not currently own.

1.2 The Takeover Offer

The Takeover Offer by Talley's is a conditional full offer to purchase all of the equity securities in AFFCO that is does not already hold. This equates to a total of up to 238,447,719 shares.

The price offered by Talley's for each AFFCO Share is 37 cents per share payable in cash. In the event that Talley's acquires all 238,447,719 remaining shares in AFFCO this would represent a total cash payment by Talley's of approximately $88.23 million to acquire the balance of 47.17% of the voting securities.

Offer Timing

The Offer opened on 6 August 2010 and closes on 6 September 2010 (unless otherwise extended in accordance with the provisions of the Takeovers Code).

Key Conditions

The Offer is subject to a range of conditions typical of a transaction of this type. In general terms these conditions include;

- Restrictions on AFFCO dividends or other distributions;
- Restrictions on the issue of any further securities;
- No material adverse events;
- No material repayment of borrowings;
- No outbreak of animal disease in New Zealand;
- AFFCO business is carried on in the normal and ordinary course;

These conditions are for the sole benefit of Talley's and can be waived by Talley's at its sole discretion. Full details on the conditions are contained within the Offer Document.

It is important to note that the Offer is <u>not</u> conditional on a minimum level of acceptances from AFFCO shareholders.

Pre-bid Agreement

Talley's has entered into a pre-bid agreement with Toocooya dated 11 June 2010, where Toocooya has agreed to accept the Offer to sell all the AFFCO shares it currently holds to Talley's for 37 cents per share. Toocooya currently holds 118,564,307 Shares and will therefore receive a total consideration of approximately $43.9 million assuming that the conditions of the Offer are met (or waived).

As part of the pre-bid agreement Toocooya has consented that, as soon as practicable after the receipt of payment for its AFFCO shares under the Offer, its representatives on the Board of AFFCO (namely Christopher Spencer and Arthur Young) will resign as directors.

1.3 Takeovers Code Requirements

AFFCO is a code company for the purposes of the Takeovers Code (the **Code**). The Code requires an Independent Adviser's Report to be prepared at the request of the target company for the offerees in all takeover offers made under the Code. In every case a report requested by the directors of the target company under Rule 21 of the Code is required to accompany the target company statement.

In its "Guidance Note about the Role of Independent Advisers for the purposes of the Takeovers Code, Third Edition – August 2007" (the **Guidance Note**) the Panel recommends that;

> "advisers do not describe offers as "fair" or "unfair". A comparison of the offer price with the adviser's valuation should probably be made, but this is only one of a number of issues that the adviser may usefully discuss in its report on the merits of the offer.
>
> One exception to this recommendation is where the primary purpose of the report is to provide guidance to shareholders who are certain to, or at least very likely to, have their shares taken under compulsory acquisition as the result of an offer. In such cases it may be appropriate for the adviser to express a view on the "fairness" of the offer price."

In our view, and despite the pre-bid agreement with Toocooya, there remains a material level of uncertainty around Talley's proceeding to compulsory acquisition of all AFFCO shares. We have therefore focused on assessing the "merits" of the Offer without reference to "fairness".

The Independent Adviser's Report is required to be included in the Target Company Statement (**Target Company Statement**) that is required to be sent to the Offeror pursuant to Rule 46 and Schedule 2 of the Code.

1.4 Purpose and Issue of this Report

AFFCO has engaged Campbell MacPherson Limited (**Campbell MacPherson**) to prepare an Independent Adviser's Report (the **Report**) on the merits of the Offer in accordance with Rule 21 of the Code.

Campbell MacPherson was approved by the Takeover Panel on 20 July 2010 to prepare the Report.

We are advised by AFFCO that the Board has formed an independent directors committee (the **Directors Committee**) comprising three directors; Sam Lewis, Bob Carter and Mike McCredie, for the purposes of considering the Offer.

Campbell MacPherson issues this Report to shareholders of AFFCO that are not associated with Talley's or Toocooya (the **Non-associated Shareholders**) to assist them in forming their own opinion on whether or not to accept the Offer.

We note that each shareholder's circumstances and objectives are unique. Accordingly it is not possible to report on the merits of the Offer in relation to each individual shareholder. This Report is therefore necessarily general in nature.

This Independent Adviser's Report is not to be used for any other purpose without our prior written consent.

2. EVALUATION OF THE MERITS OF THE OFFER

The role of an independent adviser under the Takeovers Code is to form an opinion as to the merits of the Offer and in doing so take into account a range of issues other than just valuation. In this Section we summarise the basis of our evaluation and the results of our analysis.

2.1 Basis of Evaluation

Rule 21 of the Code requires an evaluation of the merits of the Offer. There is no legal definition of the term "merits" in New Zealand in either the Code or in any statute dealing with securities or commercial law. In the absence of an explicit definition of "merits", guidance can be taken from:-

- The Takeovers Panel guidance note on the role of Independent Advisers dated July 2003;
- Definitions designed to address similar issues within New Zealand regulations which are relevant to the proposed transaction;
- Overseas precedents; and
- The ordinary meaning of the term "merits".

We are of the view that an assessment of the merits of the Offer should focus on:-

- The rationale for the Offer;
- The value of AFFCO relative to the consideration offered by Talley's;
- The likelihood of alternative offers;
- Other benefits and disadvantages to AFFCO shareholders and the Company; and
- Implications for AFFCO shareholders of not accepting the Offer.

Our opinion should be considered as a whole. Selecting portions of the evaluation without considering all the factors and analysis together could create a misleading view of the rationale underlying the opinion.

2.2 Rationale for the Offer

In preparing this Report, Campbell MacPherson has held separate discussions with AFFCO directors representing the respective interests of Talley's and Toocooya.

Talley's underlying rationale for this Takeover Offer is, in our view, directly related to its agreement to acquire the AFFCO shares held by Toocooya (as announced to the market on 11 June 2010). The Offer is therefore a result of Talley's obligations under the New Zealand Takeovers Code to either make a full offer for all of the shares in AFFCO that it does not already hold or control, or to obtain approval from Non-associated Shareholders (via an ordinary resolution pursuant to Rule 7(c) of the Code) for the acquisition of the Toocooya stake.

Whilst the reasons for, and the negotiation process relating to, the proposed sale of the Toocooya stake in AFFCO remain unknown we consider that, given Talley's already has a majority 52.83% equity interest in AFFCO, it would be the natural buyer of the Toocooya stake for the following reasons;

- It is the only party that would, in theory, be prepared to pay a partial or full "premium for control" for the Toocooya share block.
- Talley's has been a long term shareholder of AFFCO and has pursued a strategy of increasing its equity position in the Company as opportunities have arisen.

- Talley's AFFCO stake is an important part of its wider strategic interests in the New Zealand primary food sector which also include seafood, dairy products and vegetables.
- Talley's level of knowledge of the Company operations and it strategic position in the New Zealand meat industry would be higher than external parties.
- Talley's has a high level of input through its executive directors active within AFFCO.

  Talley's and Toocooya representatives have been together on the board of AFFCO over a long period and the parties are therefore well known to one another.
- Since Talley's acquisition of a majority stake 50.1% in AFFCO in 2006, they have had an increased ability to influence the strategic direction of the Company.

We note that the Offer is not conditional on any minimum acceptance criteria by AFFCO shareholders. This would suggest that Talley's would be comfortable remaining a majority (but not necessarily 100%) owner of AFFCO. We discuss further key issues around Talley's ownership and control of AFFCO in Section 2.7.

We also note that Talley's has been granted an exemption notice by the Panel, "Takeovers Code (Open Country Dairy Limited) Exemption Notice 2010" which provides Talley's with an exemption from rule 6(1) of the Code in respect of any increase in its voting control of OCD resulting from an increase in its shareholding in AFFCO as a consequence of acceptances under the Offer.

2.3 Valuation and Pricing

Campbell MacPherson has undertaken a valuation of AFFCO shares for the purposes of assessing the consideration offered by Talley's of a cash payment of 37 cents per AFFCO share. Full information on our assessed valuation of AFFCO shares is contained in Section 7.

Our valuation analysis has been split into two components comprising the core AFFCO business and AFFCO's 35.45% stake in Open Country Dairy (**OCD**). The principal valuation method applied to the core AFFCO business has been the capitalisation of earnings method using comparable transactions in the New Zealand and international meat sector.

The principal valuation methods applied to the valuation of OCD have been the capitalisation of earnings method using comparable transactions in the New Zealand and international dairy sector and the asset-based method analysing OCD's net tangible assets.

Results for both valuation components have been compared against trading multiples of comparable companies and then added together to arrive at our final assessed valuation for AFFCO.

We note that we have assessed the value of AFFCO (and the value of AFFCO's interest in OCD) inclusive of a premium for control i.e. based on the fair market value (per share) of 100% of the equity in each company. This reflects our view that Talley's direct majority control of AFFCO and its implied collective (direct and indirect via AFFCO) majority control of OCD warrant this approach.

The AFFCO meat business comprises procurement, processing, market and sales of New Zealand meat products mainly to export customers. The Company shows a history of volatile earnings with reported earnings before interest tax and depreciation (EBITDA) ranging from $23.5 million to $79.0 million over the last five full financial years and normalised EBITDA (EBITDA adjusted for abnormal and non-recurring items) ranging from $0.5 million to $59.7 million over the same period.

AFFCO has reinvested significantly in its business over an extended period and has continued to improve its operational efficiency and reduce debt to place itself in a stronger position in an unpredictable market that continues to suffer from processing over-capacity, foreign exchange volatility, weather patterns and other factors that can significantly impact on AFFCO's performance.

Our assessed equity valuation range for the core AFFCO business is $133 million to $179 million. In determining this value range we have taken into account a number of factors including the historical and forecast performance of AFFCO, our assessment of AFFCO's future maintainable earnings, Enterprise Value (EV) to EBITDA ratios of other comparable transactions and comparison of implied AFFCO multiples with trading multiples for selected listed meat companies.

Our assessed indicative valuation range for AFFCO's investment in OCD is $35 million to $48 million. In determining this value range we have taken into account a number of factors including the historical and forecast performance of OCD, our assessment of OCD's future maintainable earnings, Enterprise Value (EV) to EBITDA ratios of other comparable transactions, comparison of implied multiples with trading multiples for selected listed dairy companies and an asset-based valuation using net tangible assets as a proxy for market value.

We note that our valuation of AFFCO's interest in OCD is indicative only as we have had limited access to OCD financial information and did not have access to OCD management, operations or business forecasts. Furthermore OCD is at a growth stage in its development and the determination of future maintainable earnings is challenging given the volatility of earnings experienced by OCD and other participants in the New Zealand dairy sector. We do note however that a number of international investors have or are considering investing in the New Zealand dairy sector at this time.

Based on combining our assessed value for the core AFFCO business of $133 million to $179 million with our indicative assessed value for AFFCO's investment in OCD of $35 million to $48 million, we consider that the total fair market equity value for AFFCO is in the range of $172 million to $225 million. This equates to 34.0 to 44.4 cents per AFFCO Share (midpoint 39.2 cents per share).

2.4 Consideration Offered by Talley's

The consideration offered by Talley's is an all-cash offer of 37 cents per AFFCO ordinary share. There is no other component to the offer price.

The consideration falls at the lower end of our valuation range for AFFCO of 34.0 to 44.4 cents per share and is marginally lower than the recent volume weighted average price (**VWAP**) of minority parcels of AFFCO shares trading on the NZSX as shown below.

AFFCO Consideration vs Recent Share Price			
$ per share			
Assessed Valuation range	0.340	to	0.444
Offer consideration		0.37	
Recent Trading of Minority Share Parcels on the NZSX			
Current share price (28 July 2010)		0.370	
VWAP since Toocooya pre-bid agreement announcement		0.379	
VWAP 1 month prior		0.375	
VWAP 3 months prior		0.377	

Sources: Campbell MacPherson and NZSX data

We note that (in the absence of any takeover activity in a stock) minority parcels of shares traded on an exchange would be expected to trade at a discount (known as a minority discount) to the full underlying value for 100% of the shares. The midpoint of our valuation range is 39.2 cents per share which represents a small premium of 6.0% above the Offer price and a small premium of 4.0% above the 3 month VWAP prior to announcement of the Toocooya pre-bid agreement.

2.5 Likelihood of a Higher Offer

We believe that it is highly unlikely that Talley's would increase their Offer or extend the closing date of the Offer. Our reasons for this view are;

- The pre-bid agreement with Toocooya requires Talley's to make a full takeover offer under the Code. We do not believe that Talley's are strongly motivated to acquire additional shares in AFFCO as a result of the Offer.
- The pre-bid agreement with Talley's provides that Toocooya's obligations to accept the Offer will not be affected by any variation of the Offer made in accordance with the Code (e.g. an increase in the Offer price). However we see no strong motivation for Talley's to increase the Offer price.
- Under the Takeovers Code Talley's cannot offer a different price to different minority shareholders in respect of the Offer.
- There is no indication since the announcement of the Toocooya pre-bid agreement, or since the issue of the Takeover Notice, of any material increase in the share price above the current offer price.
- We understand that Talley's and Toocooya took some months to finalise their agreement and settle on price.

2.6 Potential for Alternative Transactions

The Independent Directors of AFFCO have not received any other approaches from third parties to acquire the Toocooya stake or a significant shareholding in the Company. The Independent Directors Committee advises that it has not engaged an external corporate advisor to seek out any alternative offers for Toocooya's shares in AFFCO.

We consider it unlikely that an existing top 10 shareholder or new investor would seek a strategic stake at this time. Underlying reasons include:-

- There is considerable commentary on the need for restructuring of the New Zealand meat industry and particularly sheep meat capacity;
- International meat processors are familiar with the industry structure in New Zealand and to date chosen not to invest in New Zealand processing capacity or companies;
- The high New Zealand dollar has eroded meat industry returns;
- The New Zealand capital market is currently constrained making it difficult for many companies to raise debt and equity capital;
- New Zealand has a large exposure to international sheep meat markets and cross border processing investment tends to be in beef capacity;
- Talley's have held majority control of AFFCO since 2006 and Talley's representatives also hold key executive director roles within the business.

In summary an alternative transaction is unlikely although a third party could seek to accumulate a 10.1% stake to block compulsory acquisition by Talley's.

A recent example of this is the case of Horizon Energy Distribution Limited (**Horizon**). This company is listed on the NZSX and since 2000 has had a major cornerstone shareholder Eastern Bay of Plenty Energy Trust (**EBOPET**) with a 77% stake. Recently a new investor, Marlborough Lines Limited, acquired a 12.5% stake on-market thereby preventing EBOPET from securing more than 90% of Horizon without Marlborough Lines Limited approval.

2.7 Impact on Ownership and Control

Shareholder Voting

Ordinary resolutions require approval of more than 50% of the votes cast by shareholders. Special resolutions require approval of more than 75% of the votes cast by shareholders. A shareholder holding more than 25% of a company is able to block special resolutions. A shareholder holding more than 50% of the voting securities of a company is able to pass (or block) ordinary resolutions. A shareholder holding more than 75% of the voting securities of a company is able to pass special resolutions (in each case assuming the shareholder is eligible to vote).

A shareholder's ability to influence voting on ordinary or special resolutions may be impacted by other legal and regulatory factors such as the Companies Act, Takeovers Code, NZSX Listing Rules, and the Company's constitution.

The typical powers that can be exercised by an ordinary resolution of shareholders include:

- adoption of financial statements;
- voting directors in or out;
- appointment of auditors;
- alteration of shareholder rights; and
- decisions involving remuneration and other benefits.

The typical powers that can be exercised by a special resolution of shareholders include:

- adopting, altering or revoking the company's constitution;
- approval of a major transaction;
- approval of an amalgamation; and
- placing the company into liquidation.

Situation Prior to the Toocooya Pre-bid Agreement

Prior to the Toocooya pre-bid agreement Talley's held a beneficial interest in 52.83% of the voting securities of AFFCO. Talley's also has two representatives on the Board of AFFCO both of whom are Executive Directors and who are active in the day-to-day running of the AFFCO business. Therefore we observe that Talley's has significant strategic and operational influence over the affairs of AFFCO.

We also note that Talley's holds a 17.04% direct equity interest in OCD, the same company in which AFFCO holds a 35.45% equity interest.

Taking the above factors into account on a collective basis, we consider that Talley's already has a high level of control of AFFCO. The current Toocooya shareholding in AFFCO of 23.46% does in our view provide some degree of negative control in that it is likely that Toocooya could block a special resolution of the Company provided that other shareholders (equivalent to at least further 1.54% of those voting on the resolution) also voted against the resolution. However, by virtue of its pre-bid agreement, Toocooya has now agreed to sell its shares to Talley's under the Offer, and therefore the potential for a remaining shareholder to exercise a degree of negative control over AFFCO is likely to be negligible.

Potential Control Outcomes of the Offer

In the event that the Offer proceeds and is not withdrawn for any reason, there are two key potential control outcomes as outlined below:-

a) Talley's holds or controls 90% or more of the AFFCO shares

If Talley's holds or controls 90% or more of the voting securities of AFFCO as a result of the Offer then it will be able to proceed to compulsory acquisition of the remaining shares in the Company (**Compulsory Acquisition**).

Under the Takeovers Code Talley's would be required to issue a notice to the remaining shareholders within 30 days of the closing date of the Offer notifying them of Talley's decision to either compulsorily acquire their shares or advising them that Talley's does not wish to compulsorily acquire their shares but they have the right to sell their shares to Talley's within 21 days of receiving the notice (**Voluntary Sale**). Upon expiry of the 21 day period Talley's would then be free (if they chose) to purchase additional AFFCO shares from remaining AFFCO shareholders on a willing buyer/willing seller basis at a mutually agreed price (e.g. via trading of AFFCO shares on the NZSX).

<u>Consideration Payable under Compulsory Acquisition/Voluntary Sale</u>

The acquisition price is determined the same way regardless of whether the shares are purchased via Compulsory Acquisition or Voluntary Sale.

The Takeovers Code requires that, if the Offeror (Talley's) achieves the 90% threshold by virtue of acquiring 50% of the securities of a class subject to the Offer as a result of the Offer (in each case excluding shares held by associates of the Offeror), then it can move to acquire the remaining holding of that class at the same price as the Offer.

If the Offeror achieves the 90% threshold, but not as a result of acquiring 50% of the securities of a class subject to the Offer as a result of the Offer, then the price payable on Compulsory Acquisition (or Voluntary Sale) will be determined by an Independent Adviser based on the Adviser's assessment of a fair and reasonable price. That new price will apply unless shareholders of 2% or more of a class of equity securities or 10% or more of the outstanding securities in a class object to the price to be paid. In this event, an independent expert will be required to determine the price to be paid and outstanding security holders will be bound by the expert's determination.

In the event that Talley's reach the 90% threshold as a result of the Offer, then it is highly likely that the shares acquired under the Offer would represent more than 50% of the shares subject to the Offer. The price payable by Talley's if they choose to proceed to Compulsory Acquisition (or if Talley's purchased further shares as a result of Voluntary Sale) would therefore be the Offer price i.e. 37 cents per share.

<u>Likelihood of Compulsory Acquisition</u>

The decision to proceed to Compulsory Acquisition is at the option of the Offeror. Our discussions with a Talley's representative on the Board of AFFCO suggest that it is likely, but not certain, that, in the event Talley's held 90% or more of the shares in AFFCO, Talley's would exercise its right to compulsorily acquire the remaining outstanding AFFCO shares. Talley's has confirmed that no decision has been made by it in this regard.

In the event that Talley's does proceed to Compulsory Acquisition then AFFCO ordinary shares would be delisted from the NZSX.

<u>Control Implications for Non-associated Shareholders</u>

In our view, regardless of whether Talley's proceeds to Compulsory Acquisition or not, it will (in the event it holds 90% or more of the voting securities) effectively have complete control of AFFCO, its strategic direction including decisions regarding the distribution and/or allocation of future cashflows.

b) Talley's holds or controls more than 75% but less than 90% acceptance

The Takeover Offer is not conditional on any minimum acceptance conditions by AFFCO shareholders and a pre-bid agreement already exists with Toocooya to sell their shares to Talley's. Therefore, provided the Offer becomes unconditional, Talley's will hold, at the completion of the Offer, at least 385,599,782 shares in AFFCO representing 76.28% of the voting securities.

In the event that Talley's does not hold or control more than 90% of the shares in AFFCO at the conclusion of the Offer, then it will not have the ability to proceed to Compulsory Acquisition. In this situation we anticipate that AFFCO ordinary shares would continue to be listed on the NZSX.

However, by virtue of holding more than 50% of the voting securities of AFFCO, Talley's would continue to be able to "creep" towards the 90% threshold at a rate of up to 5% per annum, (after a twelve month stand-down period from the closing of the Offer) as permitted under the Takeovers Code. We note that Talley's has taken partial advantage of the creep provisions of the Code since it acquired 50.01% of AFFCO shares in 2006 to increase its holding to its current level of 52.83%. In the event that Talley's chose to exercise the "creep" provisions of the Code, it could potentially reach the 90% threshold for Compulsory Acquisition within three years.

<u>Control Implications for Non-associated Shareholders</u>

In our view, regardless of the extent to which Talley's holds between 76.28% and 89.99% of the shares of AFFCO, it will effectively have a very high level of control of AFFCO, its strategic direction and decisions regarding the distribution of future cashflows.

Minority shareholders may struggle to realise full value in future from their AFFCO shares as Talley's appear to be patient long term investors who already control AFFCO. The remaining influence of Non Associated Shareholders would likely be provided by statutory protections under the Code, Companies Act and NZSX listing rules, etc.

Constraints on the Control of AFFCO's Investment in OCD

AFFCO is a listed Issuer on the NZSX and is therefore also subject to NZSX Listing Rules (**Listing Rules**). Listing Rule 9.2 governs material transactions with related parties and provides certain restrictions on Talley's in respect of their control of OCD via their investment in AFFCO. In the event of a material transaction pursuant to NZSX Listing Rule 9.2.1 Talley's would be deemed a related party of AFFCO under NZSX Listing Rule 9.2.3 and would therefore be unable to enter into a material transaction (as defined by Listing Rule 9.2.2) without first obtaining the approval by ordinary resolution of shareholders not associated with Talley's. For example, this restriction would apply in the event that Talley's sought to acquire or otherwise transfer any AFFCO asset (including, where applicable, AFFCO's shares in OCD) having an Aggregate Net Value in excess of 10% of the Average Market Capitalisation of AFFCO as defined under the Listing Rules.

2.8 Other Advantages to AFFCO and the Non-associated Shareholders

In our view, acceptance of the Offer presents other potential advantages to AFFCO shareholders, these include:-

- The Offer may provide AFFCO shareholders an opportunity to sell now for cash rather than wait for a future offer. Talley's is a privately owned family company and it is highly unlikely in our view that Talley's would offer third parties the opportunity to hold shares in the Talley's Group.

- The acquisition of Toocooya's AFFCO shareholding by Talley's may remove a share overhang in the market.

- The ability to easily buy or sell minority parcels of AFFCO shares is limited due to a lack of trading volume. The Offer therefore presents an opportunity for Non-associated Shareholders to sell their shares which (particularly for larger minority share parcels) might otherwise have been more difficult or taken longer to achieve via direct trading on the NZSX.

- Given the capital intensive nature of the meat industry, the AFFCO director's approach has been to retain any surplus cash in the business (i.e. not pay dividends). Therefore those shareholders seeking a regular dividend payment may choose to take advantage of the Offer to sell their shares and then investigate alternative investment options.

2.9 Other Disadvantages to AFFCO and the Non-associated Shareholders

In our view, acceptance of the Offer presents some risks and potential disadvantages to AFFCO shareholders, these include:-

- In our view AFFCO has been cautious when discussing its 35.45% investment in OCD in the various AFFCO NZSX releases and shareholder reports. A greater awareness of OCD's number two status in the New Zealand dairy sector may attract new investors into AFFCO and improve liquidity of the stock.

- OCD is an early stage dairy processor having successfully commissioned three new plants. As this business consolidates it is likely, in our view, that earnings will improve in the longer-term.

- Many of AFFCO's existing shareholders are farmers who supply the Company with livestock. Retaining their shareholding aligns the interests between farmer, processor and exporter and this alignment will be lost in respect of those shareholders who accept the Offer.

- Retaining an AFFCO shareholding may deliver synergies in future from other Talley's investments in export food businesses.

- AFFCO management in the past five years has worked hard to streamline the business, improve operational performance and reduce costs. This may result in improved financial performance in the future.

- The New Zealand dollar has shown significant volatility during the global financial crisis and any long-term devaluation of the NZD against other key currencies such as the USD and the Euro could significantly improve returns for exporters such as AFFCO;

- AFFCO is continuing to increase its processing capacity (e.g. adding a third shift at Awarua) in the South Island which reduces its exposure to North Island livestock supply.

- AFFCO has low levels of term core debt and a strong balance sheet and is therefore well placed to withstand external shocks.

- The Independent Directors of AFFCO have advised that they do not intend to accept the Offer in respect of the shares they own.

2.10 Implications of Non-Acceptance of the Offer

The Offer is not conditional on any minimum acceptance level by AFFCO shareholders, and therefore, as discussed in Section 2.7 those shareholders who choose not to accept the Offer will either;

- remain as minority shareholders in a listed AFFCO i.e. if Talley's do not reach the required minimum 90% shareholding or;

- if Talley's reach the required minimum 90% holding of voting securities, then Talley's can proceed to Compulsory Acquisition of the remaining shares at the same price as the Offer price or any remaining shareholder can require Talley's to purchase their shares at the same price as the Offer price.

2.11 Acceptance or Rejection of the Offer

The decision to accept or reject the Offer is a matter for each individual AFFCO shareholder to decide based on their own unique set of circumstances. These unique circumstances include their own views as to value, risk profile, future share market conditions, meat and dairy sector prospects, changing land use in New Zealand, desire for liquidity, tax considerations, exchange rate fluctuations, etc.

Each AFFCO shareholder must fully consider their own specific situation, possible consequences, and consult their own professional advisor as appropriate.

2.12 Concluding Remarks

In summary we consider that the Offer has a number of actual and potential advantages that Non-associated Shareholders should give careful consideration to in forming their view on whether to accept or reject the Offer, these include;

- The Offer price of 37 cents per share falls within our assessed full underlying value of AFFCO shares in the range of 34.0 to 44.4 cents per share.

- The Offer comprises an all cash consideration that may appeal to some shareholders.

- AFFCO'S largest shareholder (after Talley's), Toocooya, has already accepted the Offer price of 37 cents per share under its pre-bid agreement.

- By virtue of acquiring the Toocooya stake, Talley's will hold a minimum of 385,599,782 shares upon completion of the Offer. This will equate to 76.28% of the voting securities of AFFCO and will enable Talley's to further consolidate their control of the Company, including the ability to pass special resolutions (requiring more than 75% approval of those voting on the resolution). The ability of remaining minority shareholders to influence the Company going forward is therefore, in our view, likely to be very limited.

- In our view the recent non-payment of dividends by AFFCO is likely to continue as the Company continues to reinvest in ongoing capital expenditure commitments and/or retain a strong balance sheet. Those Non-associated Shareholders seeking a regular dividend payment should consider reinvesting elsewhere.

- The New Zealand meat industry continues to face a number of well publicised challenges including falling livestock numbers, over-capacity, high NZD exchange rate, threat of animal diseases and other factors that are likely to continue to cause volatility in earnings of AFFCO in the future and may negatively impact on returns to AFFCO shareholders.

- Whilst there are a number of potential opportunities for AFFCO Non-associated Shareholders to benefit from retaining their shares (see below), we are cautious about the ability of minority shareholders to actually crystallise (i.e. receive) any benefits or value that may accrue in the future. Our caution in this regard reflects a number of factors including :

    a) Talley's has been a long term holder of AFFCO as part of its wider New Zealand food production portfolio and appears unlikely, in our view, to sell the Company in the foreseeable future. Minority shareholders are therefore unlikely to receive a "premium for control" that could be payable in the event of sale of the Company.

    b) Trading and liquidity of AFFCO shares on the NZSX is already limited and could potentially reduce further as a result of the Offer.

    c) Talley's are unlikely, in our view, to offer any premium for control in the future in order to acquire further shares in AFFCO unless they are required to pay such a premium under the regulatory requirements of the Takeovers Code or Companies Act.

    d) Challenges in the New Zealand meat sector have probably turned off investors and sharebrokers from AFFCO.

- We are unable to assess or quantify the likelihood that an existing shareholder and/or new investor would seek a 10.1% stake in AFFCO to prevent compulsory acquisition and thereby try to extract a higher price from Talley's.

Balanced against these factors are a number of actual and potential disadvantages of the Offer. These include;

- The Offer price of 37 cents per share is at the lower end of our assessed value range for AFFCO shares of 34.0 to 44.4 cents per share and is 5.6% below our valuation mid-point of 39.2 cents per share. This implies that those shareholders who do not sell may benefit from upside available within this range.

- The Offer price essentially reflects the recent share price of minority parcels of AFFCO shares traded on the NZSX. These parcels have traded at a VWAP of 37.7 cents per share in the 3 months prior to the announcement of the Toocooya pre-bid agreement on 11 June 2010.

- AFFCO has undertaken significant capital expenditure (e.g. SPM, OCD) over the last decade to reduce costs, improve its operations and establish a nationwide presence to improve its industry position and capability. These factors may result in improved financial performance in the future. However, there is no guarantee that this will be the case.

- AFFCO provides one of the few opportunities for public company investors (outside of farmer shareholders) to have exposure to the New Zealand meat and dairy industry. AFFCO shareholders may wish to retain their stake based on their expectations of the dairy sector and potential benefits to AFFCO from OCD's future performance.

- The Independent Directors of AFFCO have each indicated that they do not intend to accept the Offer in respect of their personal beneficial interests in AFFCO shares.

- Many AFFCO shareholders are believed to be farmers who also supply the Company with livestock. Farmer shareholders may wish to retain an equity stake in their preferred livestock processor.

- AFFCO holds a significant minority stake in OCD which provides current shareholders in AFFCO with exposure to the New Zealand dairy processing sector. Our indicative valuation of this investment is in the range of $38 million to $45 million. OCD currently has three milk processing facilities and is at a relatively early stage of its development. In our view OCD has the potential to deliver further value to AFFCO shareholders in the future through both capital gains and (in the longer term) dividend payments by OCD to AFFCO. However, the timing and quantum of any increase in value is unable to be quantified at this time.

- Despite the failure of the Silver Fern Farms and the PGG Wrightson proposed merger transaction, future consolidation of the major companies operating in the New Zealand meat sector remains a possibility. Ideally this would involve at least one of the large cooperatives Silver Fern Farms and/or Alliance as a means of reducing processing over capacity. There is potential that AFFCO could participate in such consolidation or otherwise benefit from it. This could potentially deliver future benefits for AFFCO shareholders.

3. PROFILE OF THE NEW ZEALAND MEAT INDUSTRY

3.1 Overview

The red meat industry has been a key contributor to New Zealand's exports since the 1880's. Initially the main export market was the United Kingdom with beef exports to the USA growing since the 1950's. The meat industry produces 15% of New Zealand's exports by value, 27% of New Zealand's primary sector revenue and 4% of New Zealand's gross domestic product. The export of red meat and related products in the 2009 June year generated export revenues of circa NZ$6.5 billion. These products are exported to more than 115 countries.

New Zealand has circa 14,000 sheep, cattle and deer farmers supplying over 20 meat production and export companies, with processing plants located throughout the country. Most farms in New Zealand are owned and operated by farming families. The average number of stock units per farm is approximately 4,700. In the past decade there has been a significant change of pastoral land use with previously livestock farmed land being converted to dairying, forestry, horticulture or viticulture.

The red meat industry is a significant employer with over 53,000 employees including 24,000 directly employed in the meat processing sector. There are more than 60 licensed meat processing plants operating around New Zealand and the majority of these are focused on export markets.

Sheep, cattle and deer are raised on New Zealand's natural grass fed pastoral systems. This leads to seasonal production highs and lows. For example, lamb production is high in the summer months and for cattle in the March to May months. The grass growing cycle is longer in the warmer northern part of the country than the cooler areas in the lower South Island.

A key source of competitive advantage is that New Zealand livestock is free from BSE, foot and mouth and other major livestock diseases. This is due to stringent border controls, New Zealand's geographical isolation and the pasture based diet for New Zealand raised livestock.

AFFCO is a top four player in the New Zealand red meat industry and processes/exports a range of sheep meat, beef, venison and related by-products for export and local consumption.

3.2 Key Products

Beef

The short term outlook for New Zealand beef remains challenging as the global economic downturn has created changes in consumer choices. Typically the demand for prime beef has contracted with consumers trading down to cheaper cuts, alternative meats and processed beef products.

Beef export revenue has been estimated by MAF to decline in the year to June 2010, partly as a return to historical levels after the heavy kill following the 2008 drought .Traditionally the USA market represents one third of New Zealand's beef exports followed by Japan, the EU, South Korea, Indonesia and Taiwan. In the Asian markets New Zealand has strong competition from Australian, Brazilian and USA beef suppliers so New Zealand market share is a function of the relative strength of the kiwi dollar and Asian preference for soft, fatty beef produced by cattle finishing systems.

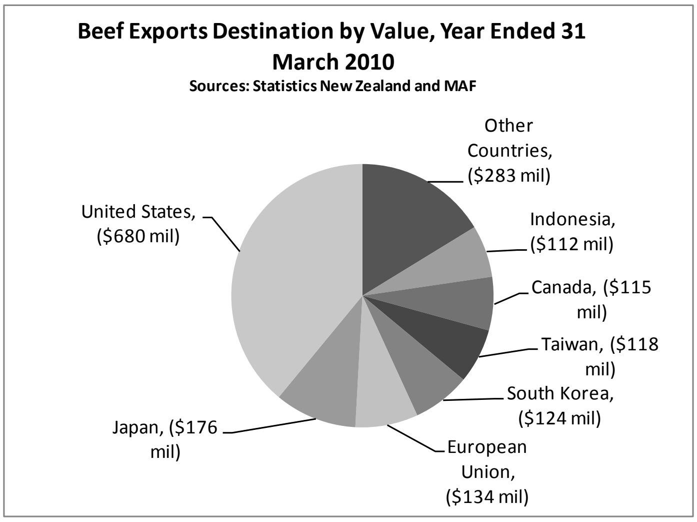
Beef Prices, Export Volume and Value, 2007 - 2014								
	Actual				Forecast			
Year to 30 June	2007	2008	2009	2010	2011	2012	2013	2014
Schedule manufactured beef price (cents/kg)	212	210	222	200	207	219	249	287
Schedule prime beef price (cents/kg)	322	333	370	334	319	338	384	442
Export volume (000 tonnes)	357	357	371	356	370	373	377	378
Export Value ($ mil)	1710	1658	2005	1704	1781	1918	2216	2551

Note

1. 2010 figures are estimated

Sources: Beef and Lamb New Zealand Limited, Statistics New Zealand and MAF.

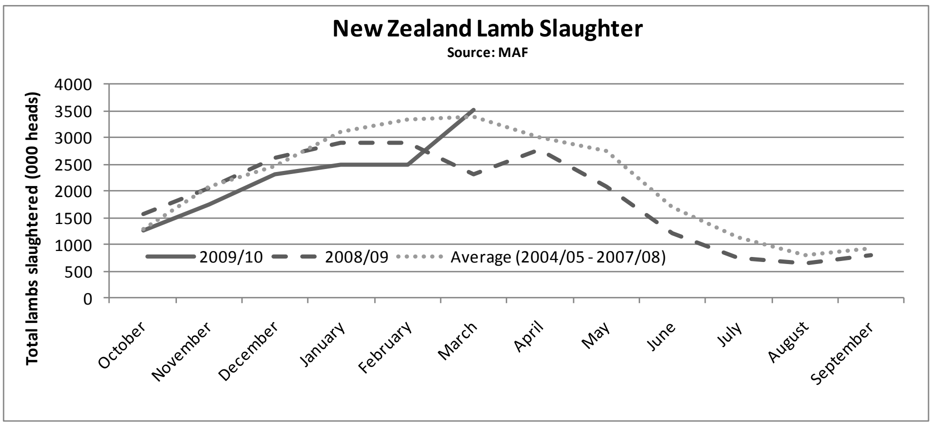
Beef cattle numbers were estimated at 4.1 million at 30 June 2009 of which 1.1 million were beef breeding cows and heifers. 72% of total beef cattle were located in the North Island. In addition beef is produced from cull dairy cows and bobby calves (i.e. veal). The total volume of beef exported in 2009 was 356,000 tonnes and the total value of these beef exports was $1.79 billion. Beef exports by market are shown below.



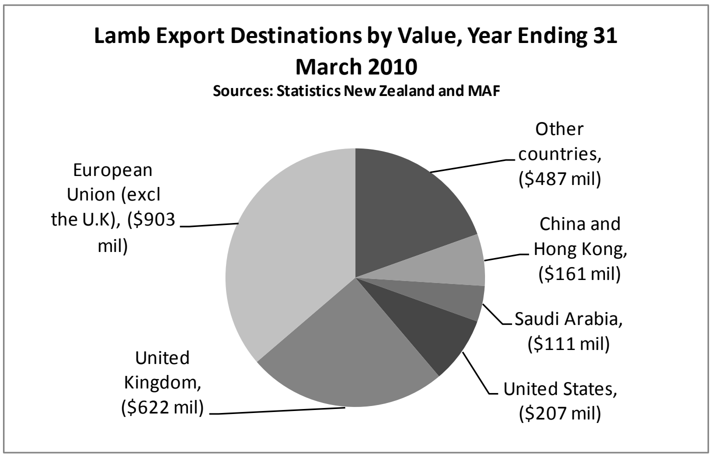
Sheep Meat

International lamb prices have remained relatively strong, due to reduced world supply and stable demand. MAF believe that reduced stock numbers worldwide will offset any reduction in demand from the global economic downturn. As the international economy slowly improves commentators predict that the developing economies are likely to increase their sheep meat consumption. This is particularly relevant to those developing Islamic countries and Halal slaughtered meat products.

In recent years the lamb kill in New Zealand has declined dramatically, as shown below:



Lamb export revenues to the EU were around 60% of NZ's total lamb export revenues in the year to June 2009. The United Kingdom is traditionally the single largest market and the weak UK pound has significantly lowered returns from lamb exports there in kiwi dollar terms.



Sheep production in New Zealand has fallen in the aftermath of the 2008 drought when sheep numbers declined by 11%. At 30 June 2009 it was estimated that New Zealand had 32.4 million sheep, down a further 5% from 2008, which comprised 22.2 million breeding ewes. After a number of years of weak returns, sheep farmers are retaining ewe hoggets to stabilise their breeding flocks. In a recent MAF report they state that ewe slaughter numbers for the six month period to 28 February 2010 were 16 percent down on the same period the previous year.

The total value of sheep meat exported in 2009 was 323,000 tonnes with a value of $2.6 billion, as shown below:

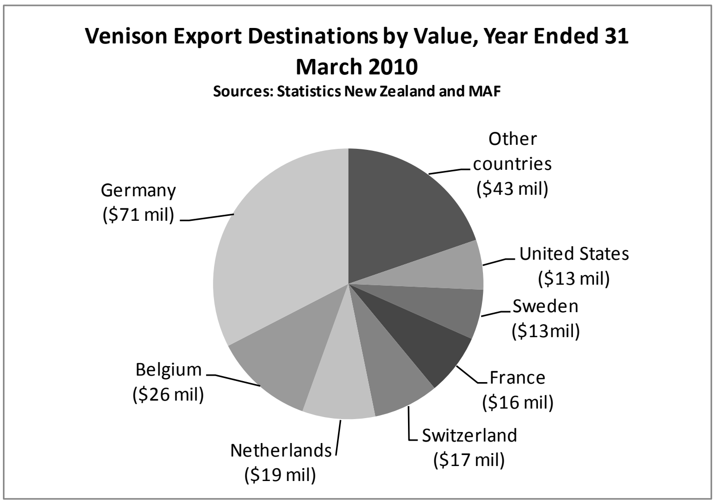
Lamb Prices and Export Volumes and Volume, 2007 - 2014

	Actual				Forecast			
Year to 30 June	2007	2008	2009	2010	2011	2012	2013	2014
Lamb schedule price (cents/kg)	323	314	492	444	413	433	494	570
Export volume (000 tonnes)	334	329	317	323	321	325	328	331
Export value ($ mil)	2165	2172	2631	2570	2460	2586	2927	3370

Note
1. 2010 figures are estimated
Sources: Beef and Lamb New Zealand Limited, Statistics New Zealand and MAF.

Venison

New Zealand is the world leader in deer farming and venison production for export. Estimated 2010 venison exports are likely to be $207 million, well down from $294 million achieved the previous year. New Zealand venison exports go mainly to Europe and Germany alone accounts for around 35-40% by total export volume and value. After five years of contraction, deer herds in New Zealand are forecast to stabilise. Venison has a niche international market and supply from New Zealand has fallen more rapidly than demand because of a sharp reduction in deer livestock numbers.



At June 2009 New Zealand had fallen to 1.2 million head of farmed deer which is 600,000 below the 2004 peak. Venison meat represented circa 80% of the total sector value exports.

Venison Prices, Export Volumes and Values, 2007 - 2014

	Actual				Forecast			
Year to 30 June	2007	2008	2009	2010	2011	2012	2013	2014
Venison schedule price - AP Stag (cents/kg)	513	654	875	765	731	728	718	787
Venison export volume (000 tonnes)	24	22	17	14	14	15	16	16
Venison value ($ mil)	252	288	294	207	200	219	250	271

Note

1. 2010 figures are estimated

Sources: Statistics New Zealand, Agri-Fax and MAF

Related By-Products

The 2009 export revenue generated from red meat by-products was circa $1.2 billion. Key by-products exported include hides, skins, edible offal, meat and bone meal, casings, tallow fats and oil, etc. The meat processors go to great lengths to maximise the economic value from each carcass.

3.3 Industry Structure

The four largest meat processors in New Zealand are:

i) Silver Fern Farms Ltd (**Silver Fern**)

ii) Alliance Group Ltd (**Alliance**)

iii) ANZCO Food Ltd (**ANZCO**); and

iv) AFFCO.

A brief overview of each company is provided below.

Silver Fern Farms Limited

Silver Fern was established in 1948 as the Primary Producers Co-operative Society and is a Dunedin based public company. Its shares and bonds are traded on the Unlisted Exchange. In total Silver Fern operates 22 plants in New Zealand and is the single largest meat processor and exporter in the country .The Silver Fern plant network includes five beef plants, five venison plants and two leather plants. Over recent years the company has struggled with high levels of debt and excess killing capacity. Since 2007 Silver Fern has closed eight processing plants or chains.

On 30 June 2008, Silver Fern and NZX listed PGG Wrightson Ltd proposed a partnership whereby PGG would be allotted new shares equivalent to 50% of Silver Fern's total share capital for $220 million. This transaction was not completed because PGG could not obtain the funding required to complete it. Silver Fern reported Group revenue of $784 million for their half year period to February, 2010 and expect to achieve $1.9 billion for the full year.

Silver Fern has in the past issued bonds to raise debt and $75 million of these bonds mature in December 2010. The company has recently stated that the new tax changes including no depreciation on buildings with a life over 50 years would result in a one –off tax expense of $20 million in the September 30 2010 year.

Alliance Group Limited

The Alliance Group has been operating for over fifty years as a farmer co-operative and is based in Invercargill. The Company has circa 5500 farmer shareholders who supply more than 85% of the livestock processed. Alliance claims to produce 30% of New Zealand's sheep meat production, 10% of beef production and 20% of venison production from its nine processing plants in the South Island and lower North Island.

During 2007/8 Alliance and Silver Fern considered the potential benefits of a merger to improve financial returns. However, Alliance believed that small step consolidation, including a merger with Silver Fern would not bring the required benefits. Alliance proposed a single entity through which 80% of New Zealand's livestock supply is managed from farm to market (i.e. pasture to plate).

ANZCO Foods Limited

ANZCO is jointly owned by Itoham Foods Inc, Nippon Suisan Kaisha Ltd, and directors and management with each group owning more than 25% of the company. Itoham Foods is Japan's second largest processed meat company with annual sales of US$10 billion. Nippon Suisan is Japan's largest seafood company and both Japanese companies are listed on the Tokyo Stock Exchange.

ANZCO had annual revenue in FY09 of $1.19 billion and a network of nine processing plants in the South Island and lower North Island.

AFFCO

An overview on AFFCO is set out in Section 4 below.

Key Industry Drivers

The New Zealand meat sector is characterised by four dominant producers and over twenty five niche players. The product range varies from commodity grades to value add speciality meat cuts. Key industry drivers include:-

- On farm performance and cost structure.
- Climatic conditions (e.g. droughts).
- Changing land use patterns.
- Level of New Zealand livestock numbers and processor demand for supply.
- Meat processor performance and cost structure.
- The value of the New Zealand dollar versus international trading currencies.
- International demand for red meat as a source of protein.

Traditionally the New Zealand meat industry has made a significant contribution to export earnings and employment. Generally the meat industry has struggled in terms of profitability for many years often due to factors beyond the participants control such as droughts and exchange rates. MAF believes the meat sector has considerable potential for growth due to the advantages associated with New Zealand's agricultural production practices and systems including food quality, sustainability, animal welfare and energy use.

Financial returns have been poor and many players have to continually reinvest to keep their plants up to export standard. Privately owned meat companies retain profits or pay to shareholders as dividends while farmer owned cooperatives tend to pay out all the "profits" through livestock procurement and supplier rebates. Two of the largest meat producers are farmer owned cooperatives so the potential for significant industry changes lies in the farmer's hands as they own circa 60% of the meat processing capacity and nearly 100% of livestock supply.

The meat industry has evolved in a climate of uncertainty, e.g. for farmers, uncertainty of climate, feed and stock. Farmers are also uncertain about future livestock returns and killing space availability. On the other hand meat processors are conditioned due to the uncertain supply and quality of livestock from season to season. Meat processers have to compete strongly for supply to obtain livestock and fulfil their export customer order obligations. Finally, meat workers have seasonal/variable incomes, changing land use patterns has resulted in some plants closing and plant labour are also exposed to changes in livestock volumes and increasing automation in processing plants .

In a 2009 report on the meat industry labour market, the Department of Labour identified a number of key issues to address including:

- Retention and recruitment with a high churn of new employees in their first season.
- An ageing workforce.
- The reputation of the industry as a poor employer.
- Meat processing is perceived as a higher risk industry (for health and safety)
- Annual employee incomes are seasonal , variable and less reliable, and;
- The need to develop ways to improve productivity.

3.4 Industry Regulations

Market Access

Since the Second World War it has become common place for governments of developed economies to provide economic protection for their domestic farming sectors. This protection comes in a variety of forms including tariffs, import quotas, production subsidies, etc. Key examples include the UK, EU and USA.

Due to the GATT Uruguay round of global trade negotiations New Zealand obtained country specific tariff quota access to:-

i) Export 227,884 tonne of New Zealand origin sheep meat and goat meat to the European Union at zero duty.

ii) New Zealand may also compete to supply beef to the EU under the most favoured nation global quota of 116,703 tonnes.

iii) Export 213,402 tonnes of New Zealand origin beef and veal to the USA at a preferential tariff rate; and

iv) New Zealand has quota to supply 29,600 tonnes of beef and veal to Canada.

In summary then market access to export meat markets is not only a factor of typical supply and demand market forces but also political intervention and the power of domestic farming groups to lobby for import restrictions on meat products from low cost meat producers such as New Zealand.

Meat Inspection Services

Unlike other export industries, while the meat companies employ their own staff to kill and process livestock, they are also required to have present veterinarians who are employed by the NZ Food Safety Authority (NZSFA) to audit compliance with the company risk management plans and systems. NZFSA staff also sign off on the export documents required for the designated export market. NZSFA is presently merging its activities with MAF. Furthermore, each export plant will host employees from AsureQuality, a State Owned Enterprise that provides meat inspection services to approve or reject meat products for human consumption.

Animal Diseases

New Zealand holds an enviable position as a leading meat exporter because of its disease free status. The incidence of Foot and Mouth disease (FMD) and Bovine Spongiform Encephalopathy (BSE or Mad Cow disease) in other countries has been of benefit to our exporters. For example in the UK more than 179,000 cattle were infected by BSE and 4.4 million slaughtered during the eradication programme. Until 2003, Japan was the top importer of US beef but after the discovery of BSE in US cattle all imports of US beef into Japan were stopped for a period. Alongside Australia and the USA, Brazil is a growing beef exporter although ongoing FMD related market restrictions are continuing to hinder Brazil's export sales growth.

4. PROFILE OF AFFCO HOLDINGS LIMITED

4.1 Background and History

AFFCO was first established in 1904 when the Auckland Farmers Freezing Co-operative Company was founded. Subsequent acquisitions and mergers have enabled AFFCO to become the fourth largest meat processor and exporter in New Zealand. AFFCO now operates nine plants in the North Island and two plants in the South Island processing sheep, lamb, beef, bobby calves and venison products.

AFFCO previously had a cooperative farmer ownership structure and listed on the NZSX in May 1995 following a debt restructure and public issue of 100 million ordinary shares at 50 cents. The Company now has 505,483,194 ordinary shares on issue. AFFCO's record of paying dividends has been sporadic with shareholders last receiving a 1 cent per share final dividend for the financial year ended September 30, 2006.

AFFCO employs circa 3,500 staff at the peak of the season and exports to more than 100 countries with key markets including the USA, Europe and Asia.

4.2 Board of Directors

The directors of AFFCO are as follows;

- Sam Lewis – Independent non executive chairman
- Andrew Talley – Executive Director
- Michael Talley – Executive Director
- Bob Carter – Independent non executive Director
- Mike McCredie- Independent non executive Director
- Christopher Spencer – Non executive Director
- Arthur Young – Non Executive Director
- Peter Talley – Alternate Director for Andrew and Michael Talley.

The following Directors are also directors of Talley's:

- Andrew Talley
- Michael Talley
- Peter Talley

The following Directors are also directors of Toocooya:

- Christopher Spencer
- Arthur Young

The senior managers of AFFCO include Hamish Simson, Chief Executive Officer and Nigel Stevens, Chief Financial Officer. Hamish Simson joined AFFCO as CEO of AFFCO's domestic operations. Later he assumed a role (nominated by Talley's) as an executive director of AFFCO with additional responsibilities in relation to special projects. Prior to joining AFFCO in November 2009, Nigel Stevens had been employed for 15 years by the Talley's Group.

4.3 Ownership Structure

AFFCO currently has a single class of equity (ordinary shares) traded on the NZSX. There are currently 505,483,194 AFFCO ordinary shares on issue with a total of 5,266 shareholders. The names, number of shares held and percentage holding of the top ten shareholders as at 21 July 2010 is set out below:-

AFFCO Ten Largest Shareholders as at 21 July 2010			
Shareholders	**Notes**	**Shares**	**%**
Talley's Group Limited		267,035,475	52.83%
Toocooya Nominees Limited		118,564,307	23.46%
National Nominees New Zealand Limited		14,238,639	2.82%
Kilmacrennan Farm Limited		8,909,443	1.76%
Citibank Nominees (NZ) Limited		7,273,821	1.44%
FNZ Custodians Limited		7,151,770	1.41%
Hugh Green Investments Limited		5,076,147	1.00%
Garth Barfoot		3,750,000	0.74%
Custodial Services Limited		2,210,426	0.44%
Accident Compensation Corporation		1,718,830	0.34%
Subtotal		435,928,858	86.24%
Others		69,554,336	13.76%
Total Shares on Issue		**505,483,194**	**100.00%**

Source: AFFCO, Companies Office.

Substantial security holders of AFFCO are Talley's with 267,035,475 shares (52.83%) and Toocooya with 118,564,307 shares (23.46%). No other shareholders hold more than 5% of the voting securities of the Company.

Toocooya is controlled by family interests of the late Peter Spencer who have diversified investment interests including finance, property and farming.

4.4 Operations

AFFCO processes meat both for the domestic market and export customers. In the 2009 financial year AFFCO exported approximately 110,000 tonnes of meat and by-products. We summarise below the operations at the various plant locations around New Zealand.

AFFCO Processing Sites	
Location	**Operations**
Moerewa	Beef, lamb, calves, sheep
Wiri	Ovine tannery
Horotiu	Beef, calves
Rangiuru	Beef, lamb ,calves, sheep, deer
Wairoa	Beef, lamb ,calves, sheep
Napier	Bovine tannery
Wanganui (Land Meats)	Domestic processor – beef, lamb
Wanganui (Imlay)	Beef, lamb, calves, sheep
Manawatu	Beef
Malvern*	Beef, lamb
Awarua*	Lamb, calves, sheep

* These plants are owned and operated by South Pacific Meats Limited
Source: AFFCO

Over the past five years AFFCO has continued to reinvest in upgrading various plants and acquiring new equipment. This capital expenditure is to produce a range of new products and/or keep up with stringent food safety requirements. In 2005 the Horotiu beef plant was rebuilt at a cost of $18 million and the new Awarua plant in Southland was opened in late 2005. The Company is considering expanding its Malvern plant at Burnham, south of Christchurch.

AFFCO owns 70% of South Pacific Meats Ltd (**SPM**) and Talley's owns the remaining 30%. SPM was established to build a market presence in the South Island and increase exposure to prime lamb and bobby calves. SPM operates as a toll processor and charges AFFCO for killing, handling and storage. In turn AFFCO retains control of livestock procurement and meat /by-product marketing.

AFFCO supplies a global customer base spread over six continents. This customer base includes retail food chains, supermarket operators, restaurants, leather merchants etc. Wholly owned subsidiary Land Meats New Zealand Ltd (**Land Meats**), based in Wanganui, supplies the majority of AFFCO products into the New Zealand domestic market. This operation sources livestock to meet customer demand 52 weeks of the year with a product range that includes chilled and frozen beef, lamb, mutton, goat and pork, etc. A specialist rennet plant operates at Eltham.

AFFCO also operates two specialist tanneries at Napier (Wet blue bovine hides) and Wiri (Wet blue and pickled ovine pelts and wet salted calf skins).

In March 2007 AFFCO formed a subsidiary Dairy Trust Ltd (**Dairy Trust**) for the purpose of investing in dairy related businesses. Dairy Trust was subsequently renamed Open Country Dairy Limited (OCD). Further information on OCD is set out below in Section 5.

AFFCO and other meat industry processors operate in volatile domestic and international markets. We summarise below some of the key business risks they face:-

- Climatic conditions such as drought and heavy rainfall can have a major effect on the volume and/or quality of livestock available to the meat processor;
- New Zealand raised livestock is pasture fed and pastoral growth is typically seasonal;
- Certain red meats produced contain higher fat levels than others which may deter some consumers;
- Meat processing sites are often large scale industrial operations that are highly unionised with long standing work practices that are slow to change;
- AFFCO produces products for human consumption and maintaining rigorous food safety systems are paramount;
- Traceability of a specific meat product to a particular farm supplier and unique animal identification is becoming more important;
- Changes in New Zealand land use patterns (i.e. switch to dairying, horticulture etc.) has reduced total sheep flock numbers and the cattle herd size resulting in some parts of the country having excess livestock processing capacity;
- Industry deregulation over the past twenty years has seen new processer entrants join the market which has intensified the competition for livestock to process ;
- Livestock farmers have come under intense on-farm cost and margin pressure;
- There is a lack of vertical integration of the supply/value chain from the paddock to the consumer;
- New Zealand competes with a range of other meat export countries including Australia and Brazil;
- Market access to certain markets is heavily regulated through , tariffs , non trade barriers (e.g. health certificates) and/or import volume quotas;
- Animal health status of New Zealand meat product could be seriously harmed by an outbreak of BSE, Foot and Mouth disease, etc.

- Over 80% of New Zealand meat products are exported and sold in foreign currencies which can lead to revenue fluctuations in New Zealand dollars;
- In the main New Zealand meat exporters are commodity producers and price takers with little ability or market power to determine selling prices.

4.5 Consolidated Financial Results

AFFCO provides its annual report and audited financial statements based on the financial year ending 30 September. The Company also provides interim half year accounts for the 6 month period ending 31 March. It is important to note that the seasonal nature of earnings from AFFCO means that first half results are often considerably superior to those in the second half of the financial year.

Financial performance

A summary of the financial performance of AFFCO for the financial year ended 30 September 2008 (**FY08**), 30 September 2009 (**FY09**) and the half year ended 31 March 2010 (**H1 FY10**) is provided below.

AFFCO Holdings Limited - Summary Historic Financial Performance				
NZ$000's	Notes	6 months to 31-Mar-10	Year to 30-Sep-09	Year to 30-Sep-08
Revenue		547,507	1,080,519	1,081,952
Gross profit		**67,779**	**114,049**	**134,697**
Other operating income		1,518	6,175	28,297
Operating and administrative expenses		(51,215)	(97,830)	(98,205)
Operating profit / (loss)		**18,079**	**22,394**	**64,789**
Financing income / (expense)		1,814	(1,564)	(5,743)
Share of profit / (loss) of associates	1	1,989	4,363	(1,580)
EBIT		**23,283**	**26,746**	**65,354**
NPBT		**21,882**	**25,193**	**57,466**
NPAT		**15,915**	**25,365**	**60,194**

Notes
1 Contribution from Open Country Dairy

Improved selling prices in offshore markets in FY09 were largely negated by appreciation of the NZD resulting in flat AFFCO NZD year-on-year revenues.

Recent operating performance has been relatively strong despite the challenges of the global financial crisis (**GFC**) and its impact on key export markets for New Zealand beef and lamb. FY08 delivered net profit after tax (**NPAT**) of $60.2 million (inclusive of non-recurring items of $19.4 million principally relating to revaluation of AFFCO's investment in OCD). The strong operating result was assisted by drought conditions in several parts of the country and increases in kill of capital stock due to the conversion of land to dairy and cropping.

The FY09 year saw the full impact of the GFC with subdued demand for high value cuts from the US, EU and North Asia markets which resulted in reduced prices. Exchange rate volatility was severe with a 12 month high/low cross of $0.7250/$0.5051 against the USD. Despite this AFFCO performed relatively well with revenue almost identical to FY08 and NPAT of $25.3 million. The Company also benefited from a positive contribution of $4.4 million from its share of profit from its investment in OCD.

Financial Position

AFFCO Holdings Limited - Summary Historic Financial Position				
NZ$000's		As at	As at	As at
	Notes	31-Mar-10	30-Sep-09	30-Sep-08
Current Assets				
Cash		14,149	18,041	3,727
Inventories		113,424	67,071	62,964
Receivables		116,649	46,632	78,471
Other		11,837	9,722	2,354
		256,059	141,466	147,516
Current Liabilities				
Borrowings		78,079	30,082	18,101
Accounts payable and accruals		88,074	41,730	55,939
Other		7,842	2,816	16,525
		173,995	74,628	90,565
Working Capital		**82,064**	**66,838**	**56,951**
Non-Current Assets				
Property, plant and equipment		219,152	220,599	225,740
Investments in associates		64,540	62,551	58,188
Other		9,938	9,960	7,173
		293,630	293,110	291,101
Non-Current Liabilities				
Borrowings		16,097	16,147	30,000
Other		2,735	2,853	2,469
		18,832	19,000	32,469
Net Assets		**356,863**	**340,948**	**315,583**

Net assets of AFFCO increased from $316 million in FY08 to $341 million in FY09. This was achieved by significantly reducing the level of creditors and reducing long term debt. This also resulted in an improved cash position up from $3.7 million in FY08 to $18 million in FY09.

The Company has in place overdraft, term debt and seasonal debt facilities with a consortium of three established banks. Short term debt was higher as at H1 FY10 at $78 million, due to annual seasonal funding of increased stock and debtors levels through the peak of the production cycle.

AFFCO's investment in OCD is a significant asset on the balance sheet. As at March 2010 AFFCO's share of OCD had a book value of $64.5 million.

The AFFCO financial position currently includes a deferred tax asset of $7.8 million as at 31 March 2010. We note that recent changes to the depreciation rates on buildings are expected to result in a negative adjustment to that deferred tax asset. We are advised that AFFCO is awaiting final confirmation of the details of the new tax regulations before determining the quantum of this one-off adjustment.

Cash Flow

AFFCO Holdings Limited - Summary Historic Cash Flow			
NZ$000's	6 Months to	Year to	Year to
	31-Mar-10	31-Mar-09	31-Mar-08
Net cash flow from/(used in) operating activities	(47,020)	29,111	49,091
Net cash flow from/(used in) investing activities	(5,851)	(9,417)	(20,724)
Net cash flow from/(used in) financing activities	47,946	(1,890)	(27,500)
Net increase/(decrease) in cash & cash equivalents	(4,925)	17,804	867
Closing cash and cash equivalents	**12,800**	**17,725**	**(79)**

AFFCO delivered positive operating cash flows of $49.1 million in FY08 and $29.1 million in FY09. Significant cash was also reinvested back into the business with capital expenditure commitments in relation to the Wairoa plant and other equipment purchases across the Company designed to improve carcass yields, product presentation etc.

Negative operating cashflow for H1 FY10 reflects the peak processing period where high levels of livestock purchases are funded by seasonal debt facilities as shown in the cash flow from financing activities. Cash flow from operating activities will become positive for the second half of the financial year when the processed stock is sold, and this is also when the seasonal debt is repaid.

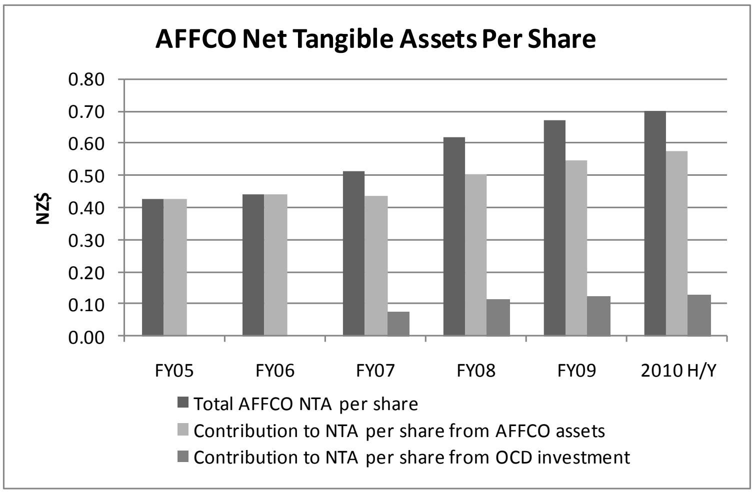
Selected Financial Ratios

Selected financial ratios are shown below for AFFCO for FY08 and FY09.

AFFCO Holdings Limited - Selected Financial Ratios	Notes	Year to 30-Sep-09	Year to 30-Sep-08
NTA per share	1	0.67	0.62
Return on assets	2	6.15%	14.90%
Pre tax return on equity	3	7.39%	18.21%
Pre tax earnings per share ($)		0.05	0.11
Dividends per share ($)		0.00	0.00

Notes
1 Includes impact of investment in Open Country Dairy
2 EBITDA/Total Assets
3 NPBT/Total Equity

As at FY09 AFFCO had net tangible assets (NTA) per share of 67 cents. Increases in NTA per share have reflected both increased net assets of AFFCO and the positive impact of the investment in OCD. A summary five year graph of FY05 to FY09 NTA per share is shown below.



Source: AFFCO financial reports

4.6 Capital Expenditure

AFFCO has reinvested significantly in capital expenditure on plant and equipment over the last five years. As shown below capital expenditure significantly exceeded depreciation from FY05 to FY08.

AFFCO Estimated Capital Expenditure vs Depreciation					
($m)	FY05	FY06	FY07	FY08	FY09
CAPEX	39.2	25.9	27.3	20.8	10.2
Depreciation	10.9	12.5	13.9	13.7	13.8

Source: AFFCO

This reinvestment slowed in FY09 to a level more closely aligned to annual depreciation and a similar trend is expected for FY10.

4.7 Investment in Open Country Dairy

AFFCO holds 41,000,100 shares in OCD representing 35.45% of the total voting securities of OCD. Further information on this investment is provided in Section 5 of this report.

4.8 Potential Impact of ETS

We have discussed the potential impact of the New Zealand emissions trading scheme (**ETS**) with AFFCO senior management. AFFCO is yet to determine the full extent of the impact of the ETS on its business which in any event would not come into effect until 2012.

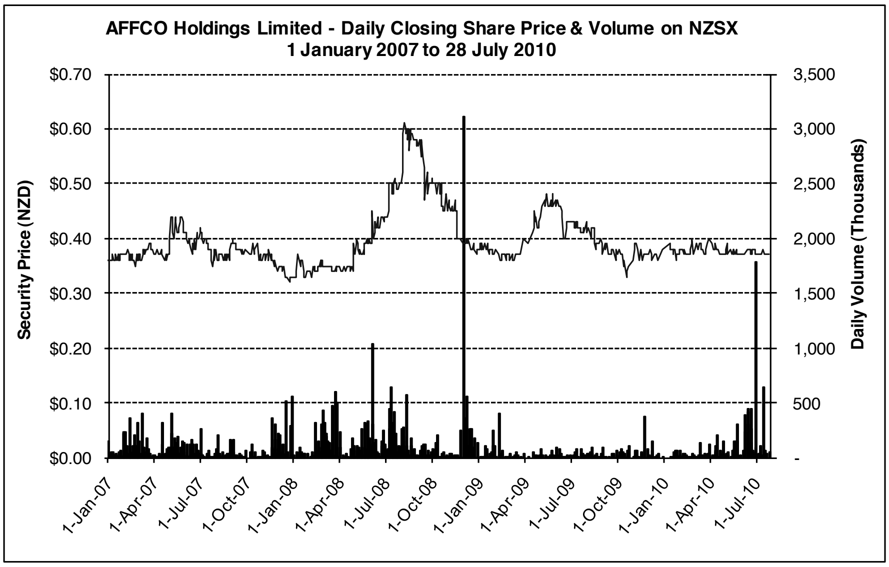
4.9 Related Party Arrangements

AFFCO performs certain management, operational and administrative services for OCD and charges OCD for these services on normal commercial terms. These charges were $304,000 in FY09. From time to time AFFCO has also sold plant, property and equipment to OCD.

As discussed, Talley's is a major shareholder in AFFCO and also makes sales to AFFCO on normal commercial terms (FY09 $2,327,000). Talley's also charges an annual fee of $300,000 for various management services provided to AFFCO in respect of Andrew Talley and Michael Talley.

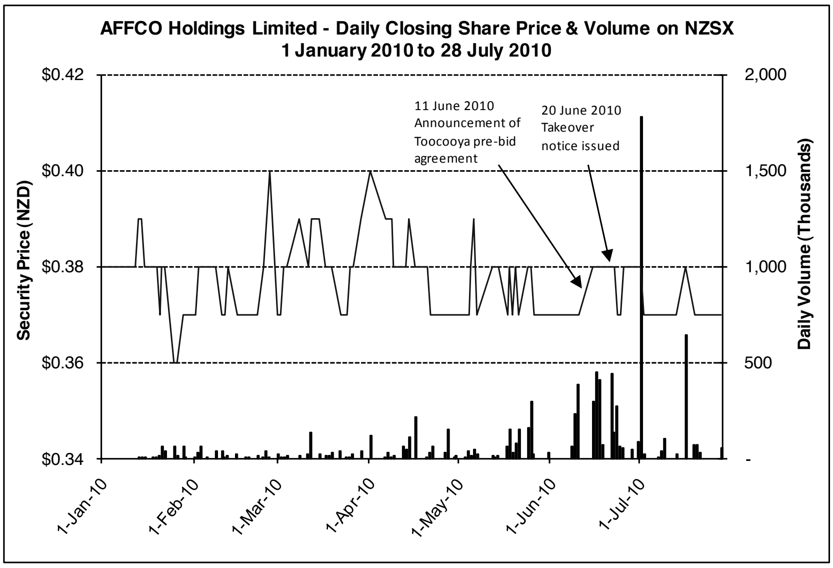
4.10 AFFCO Share Price History

AFFCO ordinary shares are currently trading at 37 cents per share as at 28 July 2010. A long term share price graph covering the period since 1 January 2007 is shown below. AFFCO's share price peaked during this period at 61 cents per share in August 2008 as a result of the strong financial performance of the Company during that period.



AFFCO shares have traded in a narrower range over the past 12 months between 33 cents and 43 cents per share. Only 2.2% of the current total shares on issue have been traded on market over the last 12 months indicating that there is low liquidity and trading in the stock.

The announcements in relation to the Toocooya pre-bid agreement and Talley's requirement to make a full takeover offer for the Company have had very little impact on the share price. Immediately prior to the Toocooya announcement on 11 June 2010, AFFCO shares were already trading at 37 cents per share (the same price as the Offer). Since 11 June 2010 the shares have traded in a very narrow range of 37 cents to 38 cents per share as shown below.



5. PROFILE OF OPEN COUNTRY DAIRY LIMITED

5.1 Background

OCD was first established in March 2007 as Dairy Trust Limited (**Dairy Trust**) a wholly owned subsidiary of AFFCO. In order to capitalise Dairy Trust AFFCO conditionally agreed to transfer certain interests in real estate at Moerewa, Horotiu and Wanganui and certain plant and equipment to Dairy Trust in consideration of the issue by Dairy Trust of 26,000,000 shares (plus GST of $3,250,000) and AFFCO also agreed to subscribe for a further 15,000,000 Dairy Trust Shares for an issue price of $1 per share. Also during March 2007 other parties agreed to subscribe for 30% of new Dairy Trust shares for cash at $1.34 per share with AFFCO holding 70% of the company.

Dairy Trust was established to undertake dairy-based initiatives with the combined strategy of:-

i) Seeking opportunities for direct investment in established companies operating in the New Zealand dairy sector; and
ii) Developing, owning and managing a small number of dairy plants in New Zealand.

Takeover of Open Country Cheese Ltd

OCD's first strategic initiative was to seek to acquire up to 100% of Open Country Cheese Ltd (**OCC**). At the time OCC was a Waikato based manufacturer of premium quality cheeses which it supplies to both New Zealand and international export markets. In May 2007 Dairy Trust made a takeover offer for 100% of the ordinary shares in OCC with the consideration offered of 1.68 Dairy Trust shares for every one OCC share held. This offer delivered Dairy Trust a 52.4% stake in OCC. A cornerstone shareholder of OCC at the time was Singaporean food company Olam International Ltd (**OLAM**) with 19.9%.

In August 2008 Dairy Trust announced a full cash takeover for all the shares it didn't own in OCC at $2.75 per share. This offer represented a premium of 31% to the pre-announcement trading price on the Unlisted share exchange platform of $2.10 per share. The takeover offer was supported by OLAM who had entered a pre-bid agreement to accept the offer for its entire 19.9% shareholding. The OLAM pre-bid agreement with Dairy Trust included a number of terms and conditions including OLAM agreeing to subscribe for 22,525,000 new ordinary shares in Dairy Trust for $3.49 per share. In October 2008 Dairy Trust completed the full takeover of OCC and in early 2009 Dairy Trust was renamed Open Country Dairy Ltd. (**OCD**). The issue of new OCD shares to OLAM resulted in AFFCO reducing it interest in OCD from 44.03% to 35.45%.

Development of New Processing Facilities

The second strategic initiative was to progressively develop the three sites acquired from AFFCO and one site from Invercargill City Council for the purpose of constructing and operating dairy processing facilities. The sites which Dairy Trust acquired from AFFCO were on buffer land surplus to AFFCO's meat processing operations. In acquiring these sites Dairy Trust also secured an interest in certain land and buildings together with easements over and a shared interest in the regulatory consents which allow for the use of effluent and water treatment facilities. Dairy Trust also acquired an industrial site at Awarua, south of Invercargill from the Invercargill City Council and entered into an effluent sharing agreement with South Pacific Meats Ltd (70% owned by AFFCO).

5.2 New Zealand Dairy Industry

The dairy industry is New Zealand's largest export earner with annual revenues estimated at NZ$9.94 billion for the year ended 30 June 2010. New Zealand exports its dairy products to over 150 countries around the world and has been successful in progressively diversifying its customer base away from traditional markets such as the USA and Europe, and into new higher growth markets in Asia, Latin America and other developing economies.

Fonterra dominates the production and export of New Zealand dairy products. However, it has been joined in more recent times by a number of new companies seeking to benefit from New Zealand's reputation as a high quality disease-free dairy exporter. These companies include OCD, Tatua Cooperative Dairy Company Ltd, Westland Cooperative Dairy Company Ltd, Synlait Ltd and NZ Dairies Ltd, and others are expected in the future.

Fonterra's dominant market position is regulated to some extent by the Dairy Industry Restructuring Act 2001 (**DIRA**) which (amongst other things) requires Fonterra to supply up to 5% of the raw milk it collects each year to other milk processors at a specified price. We understand that OCD secures over 90% of its raw milk from its own suppliers and the balance from Fonterra under the DIRA.

Raw milk production has increased substantially over recent years due to dairy farm conversions and other factors. Production of milk solids has increased 9% since 2007 to reach 1.43 million tonnes in the year to 31 May 2010 and is forecast to continue to grow to over 1.7 million tonnes by 2014.

Raw milk costs to other dairy producers such as OCD are effectively driven by the market price paid by Fonterra for its milk supplies. Fonterra delivers its returns to cooperative members via the price it pays farmers for raw milk and the dividend to farmer shareholders. Improving international dairy prices this year have resulted in an improved Fonterra forecast payout of $6.10 per kg of milk solids and a forecast distributable profit of 40-50 cents per share.

5.3 OCD Operations

OCD currently has three dairy processing facilities located at Waharoa and Wanganui in the North Island and Awarua, near Invercargill in the South Island. The combined milk processing capacity of the three sites is some 800 million litres of milk per annum which makes OCD the second largest dairy processor in New Zealand (after Fonterra) with exports to over 45 countries.

OCD acquired the Waharoa processing plant as part of the acquisition of OCC. The factory was originally a cheese plant with full production commencing in September 2004. Further site development included a whey plant (2006), an anhydrous milk fat plant (2007) and a whole milk powder plant (2008).

The Awarua factory was commissioned in September 2008 and produces whole milk powder. This plant has the capacity to process 200 million litres of milk per annum producing 30,000 tonnes of whole milk powder products. The Wanganui factory was commissioned in August 2009 and has a similar capacity and product range as the Awarua plant.

5.4 Directors and Key Shareholders

OCD currently has a Board of nine directors including one director nominated by AFFCO (Sam Lewis) and one director nominated by Talley's (Andrew Talley). Laurie Magrain is the Independent Chairman. The Company is tightly held with the top five shareholders controlling approximately 92% of the voting securities. AFFCO is the largest OCD shareholder with 35.45% followed by OLAM with 24.75%, Talley's with 17.04%, Dairy Investment Trust Fund Limited with 10.50% and Balle Bros Capital Limited with 4.36% of the voting securities.

OCD is a public unlisted company with more than 50 shareholders and is therefore deemed to be a Code Company under the New Zealand Takeovers Code.

5.5 Summary Financial Information

Summary financial information on OCD is provided below based on publicly available audited financial statements. We note that the company has only produced accounts since 2008 and the financial periods used have varied (15 months to May 2008 (FY08) followed by 14 months to July 2009 (FY09). Financial accounts for FY10 are yet to be released by the company.

Open Country Dairy Limited - Summary Historic Financial Performance			
NZ$000's	Notes	14 months to Jul-09	15 months to May-08
Revenue		299,396	136,788
Gross profit		50,067	2,815
Operating profit / (loss)		37,794	(4,212)
EBIT		**14,046**	**2,350**
NPBT		6,973	446
NPAT		**4,900**	**(937)**

OCD more than doubled revenue in FY09 reaching almost $300 million. Since this time the new Wanganui plant has been commissioned adding additional capacity and this is expected to further increase revenues in FY10. The progressive development of processing capacity has also led to an improvement in EBIT up from $2.4 million in FY08 to $14 million in FY09.

Open Country Dairy Limited - Summary Historic Financial Position			
NZ$000's	Notes	As at Jul-09	As at May-08
Current Assets			
Cash		2,613	7,823
Inventories		16,685	11,655
Receivables		18,654	27,977
Other		10,539	10,293
		48,491	57,748
Current Liabilities			
Borrowings		10,000	34,288
Accounts payable and accruals		35,985	32,752
Other		545	38,305
		46,530	105,345
Non-Current Assets			
Property, plant and equipment		206,918	151,301
Other		66,020	32,128
		272,938	183,429
Non-Current Liabilities			
Borrowings		70,000	-
Other		5,554	3,487
		75,554	3,487
Net Assets		**199,345**	**132,345**

As at 31 July 2009 OCD had net assets of almost $200 million and property, plant and equipment with a book value of $207 million. The Company also had significant current term debt facilities totalling $80 million.

Open Country Dairy Limited - Summary Historic Cash Flow		
NZ$000's	14 months to Jul-09	15 months to May-08
Net cash flow from/(used in) operating activities	23,682	(16,728)
Net cash flow from/(used in) investing activities	(114,911)	(66,106)
Net cash flow from/(used in) financing activities	124,184	52,352
Net increase/(decrease) in cash & cash equivalents	32,955	(30,482)
Closing cash and cash equivalents	**2,400**	**(30,482)**

OCD delivered positive cash flow from operating activities in FY09 of $23.6 million. However this was overshadowed by cash invested of $114.9 million. The latter included acquisition of property, plant and equipment totalling $67.5 million and acquisition of the remaining 47.6% of OCC it did not already own for a consideration of $49.56 million ($2.75 per OCC share).

Cash used in investing activities was largely financed through issue of new share capital to the value of $78.5 million and net additional borrowing of $45.7 million.

6. PROFILE OF TALLEY'S GROUP LIMITED

6.1 Overview

The Talley's Group was founded in 1936 by Ivan Talijancich who established a fishing company in Motueka in the South Island. Over the past seventy five years Talley's has diversified into the production and/or processing of a broad range of food products including red meat, dairy products, seafood, vegetables, aquaculture and ice-cream. Talley's is a private family-owned company and is considered to be the largest privately owned food exporter in New Zealand with interests comprising:-

- Talley's Group Ltd (100%)
- AFFCO Holdings Ltd (52.8%)
- South Pacific Meats Ltd (30%)
- Amaltal Fishing Company Ltd (100%)
- Open Country Dairy Ltd (17%)

The Talley's Group is owned by the family interests of Peter and Michael Talley.

6.2 Investments

Meat
Talley's currently holds a 52% stake in AFFCO and have two board nominees Andrew Talley and Michael Talley. Both the Talley's representatives on the AFFCO Board are executive directors and are fully involved in the strategic and operational affairs of that Company. South Pacific Meats Ltd (SPM) opened its new sheep and lamb processing plant at Awarua in Southland during September 2005. Talley's directly owns 30% of SPM with AFFCO owning the balance.

Vegetables
This division began in 1978 and produces a range of frozen products from plants in Ashburton and Blenheim. These products are produced for domestic and export markets. Talley's also produces frozen french fries at a plant located in Ashburton.

Ice-Cream
Talley's has operated an ice-cream plant in Motueka since 1995.

Dairy
Talley's has 17.04% direct equity stake in Open Country Dairy Ltd. OCD now processes over 800 million litres of milk per year at plants in Waharoa, Awarua and Wanganui.

Seafood and Deep Sea Fishing
The Talley's Group was founded on the seafood industry and operates a network of fish processing plants supplied by deep sea and inshore fishing vessels. Some vessels are company owned while others are independent contractors.

The Deep Sea Seafood Division is based at Port Nelson which operates a fleet of freezer trawler vessels which produce frozen at sea products. Aquaculture operations include the farming and processing of green lipped mussels. Inshore seafood factories are located at Westport, Timaru and Motueka. Other shellfish processed for local and export markets include oysters, cockles and scallops. Talley's has a significant investment in deep water fleet including five freezer trawlers, two joint venture longliners, one purse seine freezer vessel, and three fresh fish trawlers.

6.3 Financial Information

Talley's is a privately owned company and there is no publically available information regarding their financial performance and position.

7. VALUATION OF AFFCO HOLDINGS LIMITED

7.1 Introduction

Talley's has launched an Offer to acquire up to 100% of AFFCO ordinary shares. The consideration for the Offer will comprise a cash payment of 37 cents per share. A key aspect in assessing the merits of the Offer is the assessment of the AFFCO value per share against the consideration offered by Talley's.

For the purposes of valuation, Campbell MacPherson has assessed AFFCO on the basis of two key business assets:

- The value of the core AFFCO business of meat processing and sales, and;
- The indicative value of AFFCO's investment in OCD.

Sections 7.3 through 7.7 provide our valuation of the core AFFCO business (excluding OCD). Our indicative value of AFFCO's investment in OCD is contained in Section 7.8.

The total value of AFFCO is equal to the sum of the value of its core business together with the value of its investment in OCD.

7.2 Valuation Basis and Methodology

Talley's already has significant control of AFFCO by virtue of its current 52.83% stake in the equity of the Company. Therefore, in our view the value to Talley's of acquiring additional shares should reflect the ongoing consolidation of Talley's control position and therefore those shares should attract a premium for control (or to put it another way, those shares should not be subject to any minority discount since the acquirer already has more than a minority holding).

Under this scenario we consider that the appropriate valuation approach is to assess the full underlying value of 100% of AFFCO shares on the basis of their fair market value. Fair market value is defined as;

"The price that would be negotiated in an open and unrestricted market between a knowledgeable, willing but not anxious buyer and a knowledgeable, willing but not anxious seller, both acting at arm's length."

A range of valuation methods can be applied to determine fair market value, including:

- Discounted cash flow.
- Capitalisation of earnings / dividends.
- Net asset value / liquidation value.
- Industry-specific techniques.

Where a company is valued based on its operating performance as a going concern, the resulting value may require adjustment for the market value of other non-operating or surplus assets held by the company, such as land or other investments.

A brief summary of potential valuation methods is outlined below.

Discounted Cash Flow

In the Discounted Cash Flow (**DCF**) method, forecast cash flows are discounted back to the present at a rate that reflects the company's weighted average cost of capital (**WACC**). The resulting net present value (**NPV**), adjusted for any surplus assets, represents the value of the company to both debt and equity holders, also known as the enterprise value (**EV**). The value of equity can then be obtained from deducting long-term debt from EV.

The DCF method is usually calculated in a two-stage process combining the NPV of expected future cash flows over an explicit forecast period plus a terminal value representing the NPV of cash flows beyond that period.

The DCF method requires management to prepare detailed long-range cash flow projections for the business, together with an assessment of the appropriate cost of capital or “discount rate” that should be applied to determine the present value of those cash flows. AFFCO’s financial performance is volatile and the Company does not prepare long-range forecasts. Valuation of AFFCO using the DCF method is therefore not applicable.

Capitalisation of Earnings Method

The capitalisation of earnings method is an adaptation of the DCF method. It requires an assessment of the future maintainable earnings of the business and a selection of a capitalisation rate (or earnings multiple) appropriate to that particular business for the purpose of capitalising the earnings figure. This method is based on the principal that comparable companies engaged in similar business activities will have similar operating and financial risks and returns and can therefore be valued using a similar multiple of earnings.

The advantage of an earnings-based method over the DCF method is that earnings multiples can often be directly observed in the market. A multiple is often applied to earnings before interest, tax, depreciation and amortisation (**EBITDA**) or earnings before interest and tax (**EBIT**) in order to determine the enterprise value (**EV**) of the business.

The EV represents the value of the business as a whole and a deduction is then made for net debt to determine the equity value of the business and the value per share.

Comparable multiples are generally derived using two key sources of information;

- Earnings multiples based on recent sale price of comparable companies.
- Earnings multiples based on the current share price of comparable companies

Comparable transaction data is generally the best guide to determining the fair market value of a Company since it includes a premium for control. However, this data is often confidential and can be difficult to obtain due to its commercial sensitivity. Earnings multiples calculated using the current share price of comparable companies are generally easier to obtain but are less relevant since they reflect the value of minority parcels of shares traded on the market.

Capitalisation of Dividends Method

The capitalisation of dividends method is similar to a capitalisation of earnings approach and is generally used to value minority equity shareholdings. This method involves a direct determination of the equity value of a company using an assessment of the future maintainable dividends. The future maintaining dividends are capitalised using an appropriate dividend yield to determine the value of equity and value per share. AFFCO has not paid a dividend for a number of years nor is there any indication that it will do so again in the near future. The capitalisation of dividends method is therefore not applicable to AFFCO shares at this time.

Asset-based Methods

Valuation based on the net assets of Company is generally only applicable where the value of those assets is independent of the Company concerned or where the performance of a Company is at a sufficiently low level that the net present value of its future cash flows does not exceed the value of the assets employed.

Asset based methods are generally applicable in circumstances where the assets can be employed elsewhere to achieve greater returns and/or where there is clear market evidence (e.g. due to comparable transactions) that other similar businesses are selling for their net asset value.

AFFCO plant and equipment is specifically designed for meat processing and is therefore of limited use elsewhere. Processing assets are also costly to sell or close due to the significant costs associated with transfer or redundancy of staff. On this basis we do not consider that AFFCO should be valued using the net assets method.

Industry-Specific Techniques

Different industries may develop their own informal approaches or “rule of thumb” valuation methods that can be applied to companies in their industry as a means of “reality check” against other formal valuation methodologies.

We have discussed this with AFFCO management and they are not aware of any widespread “rule of thumb” methods available that they would apply to the New Zealand meat industry.

7.3 Valuation Approach

Taking into account the available information on AFFCO and other market participants in the New Zealand and international meat industry we consider that the most appropriate method to value AFFCO is to utilise capitalisation of earnings.

Capitalisation of earnings methodologies are generally most appropriate for established companies with stable earnings. Whilst AFFCO is a well established company, its historic earnings show high levels of volatility. This volatility is reflective of the New Zealand meat industry where gross margins are impacted by a combination of factors including seasonality in procurement of livestock, changes in international demand and price, changes in foreign exchange rates, weather and other factors.

In order to address this volatility we have assessed AFFCO earnings over a wide period covering the last five years. This period has included significant volatility in both New Zealand and international markets, both in terms of sharemarket valuations, commodity prices, foreign exchange fluctuations and underlying economic conditions.

We have also taken into account our assessed value of the surplus assets relating to the core AFFCO business, in particular surplus land and working capital adjustments to reflect the seasonal variation in debt facilities.

We have compared our valuation based on capitalisation of earnings against other earnings multiples and against the net book value of the underlying tangible assets.

7.4 Future Maintainable Earnings

Our assessment of future maintainable earnings is based on the historical operating EBITDA of AFFCO net of adjustments for abnormal and non-recurring items and excluding the impact of OCD. The resulting “normalised EBITDA” should therefore reflect the underlying operating earnings of AFFCO without the influence of financing effects or “one-off” impacts on earnings.

As discussed we have selected the last five years as an appropriate period to review the normalised EBITDA. Whilst this period is somewhat longer than usual, we consider it provides the most useful guide to future maintainable earnings because;

- AFFCO earnings are inherently volatile from year to year due to factors previously discussed.
- Weather issues (e.g. drought) in one year can impact the Company for several years due to changing livestock kill patterns.

- The impact of the global financial crisis on reducing both price levels and demand for high value cuts in FY09.

Our summary analysis of normalised historic EBITDA is provided in the table below.

AFFCO EBITDA Analysis						
NZ$000	**Notes**	**FY05**	**FY06**	**FY07**	**FY08**	**FY09**
Revenue		968,883	958,668	949,407	1,081,952	1,003,235
EBITDA	1	36,558	31,886	23,534	78,970	36,698
Adjustments: abnormal and non-recurring items		1,458	1,804	(22,943)	(19,249)	533
Normalised EBITDA	2,3	38,016	33,690	591	59,721	37,231
Normalised EBITDA 5 year average		33,850				
Normalised EBITDA 3 year average		32,514				
Normalised EBITDA FY09		37,231				

Notes

1. Excluding contribution from investment in Open Country Dairy
2. FY07 EBITDA was negatively impacted by foreign exchange volatility and livestock pricing.
3. FY08 EBITDA was postively impacted by weakness in the NZD and increased beef and lamb volumes.

The average prior five year normalised EBITDA for AFFCO (excluding OCD) is $33.85 million. This compares with the average prior three year normalised EBITDA of $32.51 million and the most recent full year (FY09) EBITDA of $37.23 million.

The Independent Directors of AFFCO have indicated that they believe the current management team have delivered significant operational gains in recent years focussed on improving meat yields and operating efficiencies. As discussed in Section 4.6 this has been backed by significant reinvestment by the Company in upgrading and extending processing plant capability. We believe that these improvements are likely to flow through to improved operating performance in the future compared with average historical results.

We have also taken into account the year-to-date (**YTD**) performance of the business and discussions with management regarding their internal forecasts for the full FY10 financial year ending 30 September 2010 and other factors such as the introduction of the emissions trading scheme and changes to taxation depreciation rules.

Having given due regard to all of these factors we assess the future maintainable EBITDA of AFFCO to be in the range of $35 million to $40 million as shown below.

AFFCO Assessed Future Maintainable Earnings [1]		
	Low	**High**
EBITDA ($m)	35.0	40.0

Notes

1. Excluding contribution from investment in Open Country Dairy.

7.5 Earnings Multiple Analysis

Campbell MacPherson has undertaken an analysis of earnings multiples on selected comparable transactions in the domestic and international meat processing sector. The transactions have been selected based on their relevance to AFFCO and the availability of transaction multiples.

Selected transactions are shown in the table below.

Meat Industry Comparable Transaction Analysis						
Acquirer/Target	Notes	Date	Target Domicle	Enterprise Value (EV)	EV/Historic EBITDA	Completed
Mafrig/Seara Alimentos		Sep-09	Brazil	USD 900m	7.0	yes
JBS/Smithfield		Oct-08	USA	USD 565m	8.1	yes
PGG Wrightson/Silver Fern Farms	1	Aug-08	NZ	NZD 550m	6.3	no
JBS/Tasman Group		May-08	AU	USD 150m	7.0	yes
JBS/National Beef		Mar-08	USA	USD 970m	10.4	no
Smithfield Food/Premium Standard Farms		Sep-06	USA	USD 787m	5.9	yes
Talleys/AFFCO	2	Apr-06	NZ	NZD 283m	5.3	yes
PPCS/Richmond		Jul-04	NZ	NZD 285m	5.5	yes
Average					6.9	
Average International					7.7	
Average New Zealand					5.7	

Notes

1. Based on Independent Advisers Report assessed EV and average 3 year historical EBITDA.
2. Assessed EV/EBITDA based on Independent Advisers Report on the transaction.

Sources: Company announcements, presentations, annual reports and media reports.

The average EV/EBITDA multiple for our selected transactions was 6.9. The data was noticeably split between international transactions completed at higher multiples (average EV/EBITDA of 7.7) and New Zealand transactions at lower multiples (average EV/EBITDA of 5.7). In our view this reflects the lack of significant overseas investment in the New Zealand meat industry to date (i.e. international pricing of these assets has yet to flow through to the New Zealand market.) ANZCO is currently the only significant meat processor with a material degree of foreign cornerstone shareholders and other major players are either cooperatives (Alliance, Silver Fern Farms) or tightly held by New Zealand investors (AFFCO).

A number of the international transactions have involved Brazilian meat companies such as JSB and Marfrig consolidating both in their domestic market and through acquisition of offshore targets. In addition to the transactions shown above, JBS (through its Australian subsidiary) has made a number of other smaller acquisitions in Australia in 2009 and 2010 including the Tatiara Meat Company for A$30.1 million and the pending acquisition (subject to regulatory approval) of Rockdale Beef for A$28 million. Earnings multiples in respect of these acquisitions were not disclosed.

Significant transactions in the New Zealand meat industry have been notably absent since the failed partial acquisition of Silver Fern Farms by PGG Wrightson in August 2008. Appetite for acquisitions by local players has likely been subdued by the lack of capital due to tightening of bank funding and limited equity capital available for these types of transactions. These factors are also likely to have impacted on meat company values since the attempted Silver Fern Farms transaction.

Of particular note in the table above is the partial takeover of AFFCO by Talley's in April 2006. The independent advisers report prepared for AFFCO shareholders assessed that AFFCO should be valued using an EV/EBITDA multiple of 5.0 to 5.5 times. This was based on analysis of comparable New Zealand transaction data available at the time together with other relevant information.

In forming our assessment of the appropriate EV/EBITDA multiple to apply to our valuation of AFFCO, we have taken into consideration all of the above transactional data together with trading multiples of listed meat companies in New Zealand and overseas and other factors such as the potential for further New Zealand meat industry consolidation, the attractiveness of AFFCO as a takeover/merger target, the likelihood of offshore investors acquiring New Zealand meat processors in the future and the current state of New Zealand's capital markets.

Having given due regard to all of these factors we assess the appropriate EV/EBITDA multiple to apply to AFFCO to be in the range of 5.25 to 5.75 with the midpoint of 5.5.

7.6 Other Valuation Inputs and Adjustments

Other valuation inputs and adjustments relevant to our capitalisation of earnings valuation of AFFCO comprise;

- Assessment of the value of surplus assets (if any) currently held by AFFCO.
- Assessment of the appropriate level of AFFCO net interest-bearing debt to deduct from the Enterprise Value of the business to arrive at a value range for AFFCO equity.

Surplus Assets

AFFCO has a considerable property portfolio consisting of land and buildings mainly associated with or adjacent to its meat processing operations and facilities. These properties include substantial buffer zones around existing plants which, whilst not always in use by the Company, are considered part of the strategic assets of AFFCO. Following discussions with management we consider there are no properties that could be classed as surplus assets for the purposes of valuation.

Net Debt

Campbell MacPherson has assessed the net debt applicable to the valuation of AFFCO at $50.5 million inclusive of current term debt, average seasonal debt and cash as at 30 June 2010.

7.7 Value of AFFCO (Excluding Investment in Open Country Dairy)

Based on the inputs and assumptions outlined above, Campbell MacPherson has assessed the Enterprise Value of AFFCO (Excluding its investment in OCD) in the range of $193 million to $240 million.

Adjusting for net debt and seasonal funding we have assessed the equity value of AFFCO in the range of $146 million to $194 million.

AFFCO Assessed Value (excluding investment in Open Country Dairy)		
	Low	**High**
Future Maintainable EBITDA ($m)	35.0	40.0
Assessed EBITDA Multiple	5.25	5.75
Enterprise Value	**184**	**230**
less Net Debt (as at 30 June 2010) ($m)	(32.5)	(32.5)
Seasonal Funding adjustment ($m)	(18)	(18)
Surplus land adjustment ($m)	-	-
Equity Value	**133**	**179**
AFFCO shares on issue (m)	505	505
Value per AFFCO share ($)	**0.264**	**0.355**

Our equity valuation for AFFCO (Excluding its investment in OCD) equates to a value of 26.4 cents to 35.5 cents per share based on the current AFFCO ordinary shares on issue.

Implied Earnings Multiples

Our assessed valuation range for AFFCO implies the following historical earnings multiples as shown in the table below.

AFFCO Holdings Limited - Multiples Implied by Assessed Valuation *		
	EV	
	Low	High
Enterprise Value ($ million)	184	230
	Multiples (times)	
Normalised EBITDA	Low	High
FY05	4.8	6.1
FY06	5.5	6.8
FY07	311	389
FY08	3.1	3.9
FY09	4.9	6.2

* Excluding investment in OCD.

This compares with trading multiples for selected listed companies as shown below.

Selected Meat Company Trading Multiples				
Company	Reporting Date	Currency	EV (millions)	Historic EV/EBITDA
Blue Sky Meats Ltd	Mar-10	NZD	27	9.8
JBS SA	Dec-09	Reals	32,540	25.3
Smithfield Foods Inc	May-10	USD	4,962	16.9
Tyson Foods Inc	Sep-09	USD	9,198	10.7
Hormel Foods Corp	Oct-09	USD	5,715	8.7
Average				**14.3**
Average (excl JBS SA)				**11.5**

Sources: Company announcements, presentations, annual reports and media reports.

International comparable companies are much larger and trade on higher multiples. The only New Zealand company, Blue Sky Meats Ltd, currently trades at a historic EV/EBITDA of 9.8. This multiple is higher than we would expect and reflects the poor earnings performance of the company due to reduced kill numbers in the most recent financial year.

Given the lack of comparable Australasian company trading multiples we are comfortable that our assessed EV/EBITDA multiple of 5.25 to 5.75 is reasonable for AFFCO.

7.8 Indicative Valuation of AFFCO Investment in Open Country Dairy

Background and Limitations

OCD is not listed on the NZX and our valuation of AFFCO's investment in OCD has been made using only limited historical information available on OCD from Companies Office filings and confidential summary management accounts. The level of confidence applied to our valuation of OCD is necessarily considerably lower than that applied to the core AFFCO business where we have been provided access to detailed up-to-date financial and operating information by AFFCO management.

Valuation Basis and Methodology

A discussion of available valuation methodologies is provided in Section 7.2.

OCD is a relatively new company that has grown rapidly through acquisition of OCC, start-up processing plants and organic growth. Recent publicly available financial information is therefore limited and must be reviewed in the context of the ongoing development of the company as it establishes itself in the New Zealand dairy industry.

On a theoretical basis the optimal method to value OCD would be the DCF method. However, our lack of access to management long-range forecasts for OCD precludes our use of this method. We are also aware that a number of other new entrants to the industry have underperformed against forecasts and we are therefore wary of the accuracy of any such long range forecasts.

Our preferred methodology for estimating the value of AFFCO's investment in OCD is the capitalisation of earnings method. Whilst not ideal for OCD, this method does have the benefit of using currently available financial reports of OCD to develop an estimate of future maintainable earnings and an appropriate earnings multiple based on comparable transactions.

We are conscious that, given the relatively early stage of development of OCD, recent earnings performance may not necessarily reflect the longer-term future maintainable earnings of the company. We also note that the property, plant and equipment are relatively new and therefore the net tangible assets of the business may, in our view, provide a reasonable estimate of the value of the Company that can be compared against our capitalisation of earnings valuation. Furthermore, the New Zealand dairy industry does not suffer from the over-capacity inherent in the meat sector that precludes use of asset-based valuation methods in the latter.

Our indicative valuation of OCD therefore uses both the capitalisation of earnings and asset-based valuation methods.

Valuation Approach

AFFCO currently holds a 35.45% stake in OCD. As a 52.83% shareholder in AFFCO, Talley's therefore indirectly holds a 18.73% stake in OCD. In addition, Talley's also holds a further 19,703,822 shares in OCD representing a 17.04% direct stake. On this basis Talley's holds a total (direct and indirect) beneficial ownership of OCD equal to 35.77% of the voting securities of OCD.

From a control perspective, Talley's has control (by virtue of its majority stake in AFFCO and its direct shareholding in OCD) over 52.49% of OCD. In our view this effectively means that Talley's should be able to negotiate a control premium in the event they wished to exit their (indirect and direct) investment in OCD, despite the fact that they hold a minority beneficial interest.

We also note that the pre-bid agreement with Toocooya means that (in the event that the Offer proceeds) Talley's will increase their beneficial interest in OCD to at least 44.08% and would also further consolidate their control of AFFCO shares in OCD.

Having given due regard to the above factors we consider that it is appropriate to value AFFCO's investment in OCD inclusive of a premium for control reflecting its pro-rata share of the value of 100% of the equity in OCD.

Capitalisation of Earnings Analysis

<u>Future Maintainable Earnings</u>

Our assessment of future maintainable earnings is based on the following key sources of information

- FY08 and FY09 operating EBITDA of OCD net of adjustments for abnormal and non-recurring items.
- Confidential summary management accounts for FY10 year to date as provided by OCD to AFFCO.

Our summary analysis of normalised historic EBITDA is provided in the table below.

Open Country Dairy EBITDA Analysis			
NZ$000	**Notes**	**FY08**	**FY09**
Revenue	1	137,787	299,396
EBITDA		5,245	22,243
Adjustments: abnormal and non-recurring items	2	-	(970)
Normalised EBITDA		**5,245**	**21,273**

Notes

1 FY09 is a 14 month period ending July 2009, FY08 is a 15 month year ending May 2008.

2 FY09 adjustments include gain on sale of farm and settlement for loss of product

We have estimated the future maintainable earnings of OCD in the range of $22 million to $29 million. In determining this range we have taken into account the following factors;

- FY08 EBITDA was based on limited trading and ongoing development of new processing capacity.
- FY09 EBITDA excluded the impact of the new Wanganui dairy plant which we understand was commissioned in August 2009.
- The FY09 period covered an extended period of 14 months. We have assumed, due to seasonal timing, that impact on EBITDA of these additional two months was minimal.
- Budget and actual performance for current year-to date and OCD management forecasts for the full 12 months of FY10.
- The potential impact of the final Fonterra milk solids payout as a benchmark for the final payout by OCD to its farmers and the impact of a higher payout on OCD FY10 EBITDA.
- The current stage of development of the Company and the likely ongoing volatility of earnings.
- The evolving New Zealand dairy industry structure and competitive forces.

Earnings Multiple Analysis

Campbell MacPherson has undertaken an analysis of earnings multiples on selected comparable transactions in the domestic and international dairy sector. The transactions have been selected based on their relevance to OCD and the availability of transaction multiples. Selected transactions are shown in the table below.

Dairy Industry Transaction Analysis						
Acquirer/Target	**Notes**	**Date**	**Target Domicile**	**Enterprise Value (EV)**	**EV/Historic EBITDA**	**Completed**
Lactalis/Ebro Foods		Mar-10	Spain	Euro 630m	9.0	Yes
Murray Goulburn/Warrnambool	1	Feb-10	AUS	AUD 276m	8.5	No
National Foods/Dairy Farmers		Aug-08	AUS	AUD 884m	12.1	Yes
Dairy Trust/Open Country Cheese	2	Jul-08	NZ	NZD 176m	7.3	Yes
Saputo/Alto Dairy		Apr-08	US	USD 160m	8.2	Yes
Average					9.0	
Average excluding National Foods/Dairy Farmers					8.2	

Notes

1 EBITDA based on normalised average excluding the loss made in 2009

2 EBITDA multiple based on FY09 EBITDA projection.

Sources: Company announcements, presentations, annual reports and media reports.

The average EV/EBITDA multiple for our selected transactions was 9.0. We note that the National Foods acquisition of Dairy Farmers in 2008 was transacted at a much higher multiple of 12.1x EBITDA. In our view this reflects the larger scale of this transaction and the low cost of capital of National Foods Japanese owner Kirin Holdings. Excluding this transaction the average historic EV/EBITDA was 8.2.

As discussed in Section 5, the New Zealand dairy industry has been active in recent years as raw milk production has increased and Fonterra's monopoly position has been challenged (in a modest way) by new dairy companies and the construction of new milk processing facilities. Unfortunately, none of these companies has yet progressed to a listing on the NZSX. Synlait considered a listing in late 2009 but was unable to gain sufficient support from the local investment community and has recently announced that Chinese company Bright Dairy & Food is to acquire a 51% stake in Synlait Milk for $82 million. Synlait is made up of three entities, Synlait Ltd, Synlait Milk and Synlait Farms, which were reported to have lost approximately $42 million in 2009.

The independent advisers report dated September 2008 prepared for Open Country Cheese Limited (**OCC**) shareholders assessed a value range for OCC that implied an EV/EBITDA multiple of 7.1 to 7.7 based on FY09 projected EBITDA and a "steady state" EV/EBITDA multiple of 5.5 to 6.0. We note that the steady state scenario assumed significant future improvements to earnings as a result of growth of OCC. We have applied the higher FY09 implied multiple to our analysis as we consider this more accurately reflects the basis upon which we have assessed future maintainable earnings for OCD in our analysis. We also note that OCD is a considerably larger company than OCC was at the time of the OCC full takeover by OCD.

We note that international transactions generally take place at higher multiples than those in New Zealand.

In forming our assessment of the appropriate EV/EBITDA multiple to apply to our indicative valuation of OCD, we have taken into consideration all of the above transactional data. Having given due regard to all of these factors we assess the appropriate EV/EBITDA multiple to apply to OCD to be in the range of 7.0 to 8.0.

Indicative Valuation Result based on Capitalisation of Earnings

Based on the inputs and assumptions outlined above, Campbell MacPherson has indicatively assessed the enterprise value of OCD using the capitalisation of earnings method in the range of $154 million to $232 million. After relevant adjustments we have indicatively assessed the equity value of OCD in the range of $31 million to $109 million.

Our indicative equity valuation for OCD using this method equates to an implied value for AFFCO's investment in OCD of 2.1 cents to 7.6 cents per AFFCO share.

Asset-based Analysis

OCD has developed a significant asset base including substantial freehold land and three dairy processing facilities. Published accounts for FY09 indicate the book value of property, plant and equipment as at 31 July 2009 was approximately $207 million as shown below.

Open Country Dairy - Property, Plant and Equipment	
NZ$000	**31-Jul-09**
Land	22,641
Buildings	39,564
Plant and Equipment	109,795
Capital Work in Progress	34,918
Total Book Value	**206,918**

Using recent management accounts we have estimated the current net tangible asset (**NTA**) base of OCD at approximately $127 million or $1.10 per OCD share. This equates to an implied value for AFFCO's investment in OCD of $45.2 million or 8.9 cents per AFFCO share.

We note that the most recent interim accounts for AFFCO indicate a book value for its investment in OCD of $64.54 million. This equates to a book value of $1.57 per OCD share. AFFCO calculates its book value of OCD based on IFRS which requires periodic adjustments to value based on share trades/transactions during the relevant period and accrued contribution from earnings of OCD. We are of the view that the historic book value of OCD in the AFFCO accounts is not necessarily an accurate indicator of the market value of that asset at the present time.

The Independent Directors of AFFCO are not aware of any recent share trades in OCD that would provide a meaningful contribution to our assessment of value.

Assessed Indicative Value of AFFCO Interest in OCD

Having given due regard to the results of our indicative valuation analysis using the capitalisation of earnings and asset-based methods we consider that the appropriate indicative equity valuation range for OCD is in the range of $109 million to $127 million or 94c to 110c per OCD share.

This equates to a pro-rata contribution from AFFCO's OCD investment of 7.6 to 8.9c per AFFCO share.

Open Country Dairy - Results of Indicative Valuation		
	Low	**High**
Assessed Equity Value	**109**	**127**
OCD shares on issue (m)	116	116
Value per OCD share ($)	0.94	1.10
Value of AFFCO's Holding in OCD ($m)	38.48	45.16
Value of AFFCO's holding in OCD per AFFCO share ($)	**0.076**	**0.089**

Implied Earnings Multiples

The indicative equity valuation range for OCD implies an Enterprise Value for OCD of $232 million to $251 million. This equates to an implied historic FY09 EV/EBITDA multiple of 10.9 to 11.8 as shown below.

Open Country Dairy - Multiples Implied by Assessed Indicative Valuation		
	EV	
	Low	**High**
Enterprise Value ($ million)	232	251
	Multiples (times)	
Normalised EBITDA	**Low**	**High**
FY08	44.2	47.8
FY09	10.9	11.8

There are no listed comparable companies in New Zealand. However Fonterra has an implied EV/EBITDA of 7.4 based on its last fair value share calculation in July 2009. Other selected dairy or related companies in Australia and Canada trade at implied historic EV/EBITDA multiples of circa 7 – 10 as shown below.

Comparable Company Historic Trading Multiple Analysis				
Company	**Notes**	**Domicile**	**Enterprise Value**	**EBITDA Multiple**
Warrnambool Cheese and Butter	1	AUS	AUD 234	7.2
Goodman Fielder		AUS	AUD 2,849	7.6
Saputo		Canada	CAD 6,871	10.2
Fonterra	2	NZ	NZD 10,908	7.4
Freedom Nutritional Products	3	AUS	AUD 46	10.1
Average				**8.5**

Notes

1 EBITDA based on normalised average excluding the loss made in 2009

2 EV based on fair value share calculation as at 31 July 2009

3 EBITDA excludes restructuring costs

Sources: Company announcements, presentations, annual reports and media reports.

Given the larger scale of these companies and other factors such as their general later stage of development we consider that our assessed indicative value range for OCD is reasonable.

7.9 Assessed Value of AFFCO

We have combined our assessed valuation of AFFCO (excluding its investment in OCD) with our indicative valuation of AFFCO's investment in OCD. The resulting equity valuation range for AFFCO is $172 million to $225 million or 34.0 to 44.4 cents per AFFCO share (midpoint 39.2 cents per share).

A summary table of our results is shown below.

AFFCO Assessed Value		
$ million	**Low**	**High**
Assessed value of AFFCO (Excluding Investment in OCD)	133	179
Asssessed value of AFFCO's Investment in OCD	38	45
Total Assessed Equity Value	**172**	**225**
Shares on Issue	505	505
Value per AFFCO share ($)	**0.340**	**0.444**

APPENDIX I. SOURCES OF INFORMATION

I.a Sources of Information

The statements and opinions expressed in this Report are based on the following main sources of information:

- AFFCO Holdings Limited annual reports for the financial years 2005 through 2009
- AFFCO Holdings Limited interim report for 2010.
- Takeover Notice from Talley's Group Limited dated 20 June 2010.
- Takeover Offer by Talley's Group Limited dated 6 August 2010.
- Open Country Dairy Limited published annual accounts for the 2008 and 2009 financial year.
- Summary confidential financial information on Open Country Dairy Ltd for year-to date 2010.
- Various public company reports and public statements and industry reports in the public domain, including but not limited to:
  - Meat: The Future, MAF, 2009.
  - Situation and Outlook for New Zealand Agriculture and Forestry, MAF, 2010
  - A New Zealand Meat Industry Labour Market and Skills Plan, MIA, 2009.
  - Sheep & Beef Mid Season Update, Meat and Wool New Zealand, 2009-10.
  - Meat and Wool Sector General Outlook, Meat and Wool New Zealand, 2009.
  - MIA 2008 Annual Report.
  - Export Meat Production Estimates, Beef and Lamb New Zealand, 2010.
- Securities data from NZX and Bloomberg.

During the course of preparing this Report, we have had discussions with and/or received information from the independent directors of AFFCO, senior management of AFFCO and the Company's legal adviser.

The Independent Directors Committee of AFFCO have confirmed that we have been provided for the purpose of this Independent Adviser's Report with all information relevant to the Offer that is known to them and that all the information is true and accurate in all material aspects and is not misleading by reason of omission or otherwise.

Including this confirmation, we have obtained all the information that we believe is necessary for the purpose of preparing this Independent Adviser's Report.

In our opinion, the information set out in this Independent Adviser's Report is sufficient to enable the Independent Directors and Non-associated Shareholders to understand all the relevant factors and to make an informed decision in respect of the merits of the Offer.

I.b Reliance on Information

In preparing this Report we have relied upon and assumed, without independent verification, the accuracy and completeness of all information that was available from public sources and all information that was furnished to us by AFFCO and its advisers.

We have evaluated that information through analysis, enquiry and examination for the purposes of preparing this report but we have not verified the accuracy or completeness of any such information or conducted an appraisal of any assets. We have not carried out any form of due diligence or audit on the accounting or other records of AFFCO. We do not warrant that our enquiries would reveal any matter which an audit, due diligence review or extensive examination might disclose.

I.c Disclaimer

We have prepared this Report with care and diligence and the statements in the Report are given in good faith and in the belief, on reasonable grounds, that such statements are not false or misleading. However, in no way do we guarantee or otherwise warrant that any forecasts of future profits, cash flows or financial position of AFFCO will be achieved. Forecasts are inherently uncertain. They are predictions of future events that cannot be assured. They are based upon assumptions, many of which are beyond the control of AFFCO and its directors and management. Actual results will vary from the forecasts and these variations may be significantly more or less favourable.

We assume no responsibility arising in any way whatsoever for errors or omissions (including responsibility to any person for negligence) for the preparation of the Report to the extent that such errors or omissions result from our reasonable reliance on information provided by others or assumptions disclosed in the Report or assumptions reasonably taken as implicit.

Our evaluation has been arrived at based on economic, exchange rate, market and other conditions prevailing at the date of this Report. Such conditions may change significantly over relatively short periods of time. We have no obligation or undertaking to advise any person of any change in circumstances which comes to its attention after the date of this Report or to review, revise or update our Report.

I.d Indemnity

AFFCO has agreed that, to the extent permitted by law, it will indemnify Campbell MacPherson and its directors and employees in respect of any liability suffered or incurred as a result of or in connection with the preparation of this Report. This indemnity does not apply in respect of any negligence, wilful misconduct or breach of law. AFFCO has also agreed to indemnify Campbell MacPherson and its directors and employees for time incurred and any costs in relation to any inquiry or proceeding initiated by any person. Where Campbell MacPherson or its directors and employees are found liable for or guilty of negligence, wilful misconduct or breach of law Campbell MacPherson shall reimburse such costs.

APPENDIX II. QUALIFICATIONS, DECLARATIONS & CONSENTS

II.a Qualifications

Campbell MacPherson is a New Zealand investment bank and corporate finance advisory firm. It advises on mergers and acquisitions, prepares independent expert's reports and provides valuation advice.

The persons in the Company responsible for issuing this Report are Stephen Burns, Tony Haworth and Alistair Ward.

Campbell MacPherson has significant experience in the independent investigation of transactions and issuing opinions on the merits and fairness of the terms and financial conditions of the transactions.

II.b Independence

Campbell MacPherson does not have at the date of this Report, and has not had, any shareholding in or other relationship with AFFCO that could affect our ability to provide an unbiased opinion in relation to this transaction.

Campbell MacPherson has not had any part in the formulation of the Offer, or any aspects thereof. Our sole involvement has been the preparation of this Report.

Campbell MacPherson will receive a fixed fee for the preparation of this Report. This fee is not contingent on the conclusions of this Report or the outcome of the Offer. We will receive no other benefit from the preparation of this Report.

II.c Declarations

Advance drafts of this Report were provided to the Independent Directors Committee for their comments as to factual accuracy as opposed to opinions, which are the responsibility of Campbell MacPherson alone. Changes made to the Report as a result of the circulation of the drafts have not changed the methodology or conclusions reached by Campbell MacPherson.

Our terms of reference for this engagement did not contain any term which materially restricted the scope of the Report.

II.d Consents

We consent to the issuing of this Report in the form and context in which it is to be included in the Target Company Statement to be sent to AFFCO shareholders. Neither the whole nor any part of this Report, nor any reference thereto may be included in any other document without our prior written consent as to the form and context in which it appears.

6 August 2010
Campbell MacPherson Ltd.

APPENDIX III. COMPARABLE TRANSACTIONS

Meat Industry Transactions

PPCS/Richmond Limited
PPCS is New Zealand's leading procurer, processor and marketer of sheep, lamb, beef and venison. Richmond was an international food company that was primarily involved with the processing, procurement and distribution of meat products. Key export destinations for Richmond include the Middle East, North America, Europe, Asia and the United Kingdom. In 2004 PPCS Successfully acquired 100% of Richmond.

Talley's Group Limited/AFFCO Holdings Limited
Profiles on AFFCO and Talley's are contained in this Report. Talley's undertook a partial takeover offer for AFFCO in 2006 which resulted in Talley's increasing its equity holding in AFFCO to 50.01%.

PGG Wrightson Limited/Silver Fern Farms Limited
PGG Wrightson is one of New Zealand's leading providers to the agricultural sector, offering a wide range of products, services and solutions to growers, farmers and processors in New Zealand and internationally. Silver Fern Farms was established when PPCS changed its name to Silver Fern Farms. Silver Fern Farms is New Zealand's leading procurer, processor and marketer of sheep, lamb, beef and venison.

JBS S.A/Smithfield Foods Inc
JBS is the largest Brazilian multinational food company, dedicated to producing chilled and fresh beef, processed beef, and fresh and chilled pork, as well as beef and pork by-products. Smithfield engages in the processing of pork and production of Hogs. These products are sold to supermarket chains, wholesale distributors, the food services industry and institutional customers. In 2008 JBS successfully acquired Smithfield.

Marfrig/Seara Alimentos S.A
Marfrig is a Brazil-based company engaged in the processing and distribution of meat and poultry products. Seara is one of Brazil's largest meat processors, Seara produces frozen, refrigerated, pre-cooked, and processed chicken and pork for the worldwide retail and wholesale food and foodservice markets. Its products include whole chickens, chicken cuts, sausage, pork, smoked ham, cold cuts and salami. In September 2009 Marfrig Acquired Seara from Cargill Inc.

JBS S.A/Tasman Group Holdings Pty Ltd
Tasman Group Holdings Pty. Ltd. operates as a meat processor in South-Eastern Australia. It also supplies meat products to the domestic and export customers in the retail, food services, and manufacturing sectors. The company offers beef and veal products. In May 2008, Tasman Group was acquired by JBS S.A.

JBS S.A/National Beef
National Beef is one of the largest beef processing companies in the United States, processing and marketing fresh beef and beef by-products across the U.S. and internationally. In March 2008 JBS S.A. announced it was to acquire National Beef. However, the transaction was not completed due to competition issues.

Smithfield Food/Premium Standard Farms Inc
Premium Standard Farms provides integrated pork products for the retail, wholesale, foodservice and export markets, as well as to further processor customers. It operates in two segments, Pork Processing and Hog Production. The Pork Processing segment sells fresh and value-added pork products to food retailers, distributors, wholesalers, further processors, pharmaceutical, and animal feed manufacturers in both domestic and international markets. Smithfield foods acquired Premium Standard Farms in September 2006.

Dairy Industry Transactions

Lactalis Group/Ebro Foods
Lactalis' primary activity is the sale of milk, cheese, butter, and cream, with its flagship brand being Président; its other top brands include Bridel, Locatelli, Société, Sorrento, and Valmont, which are distributed in circa 150 countries worldwide. Ebro Foods (formerly Ebro Puleva) is the leading company in the Spanish food processing sector. Ebro Foods is the world's largest producer of rice and the second biggest producer of pasta (its Panzani brand is the market leader in France). It is also the largest manufacturer of value-added dairy products in Spain. Lactalis acquired the dairy division of Ebro Foods in March 2010.

Murray Goulburn Co-Operative/Warrnambool Cheese and Butter Factor Company Holdings Limited
Murray Goulburn processes over 35% of Australia's milk supply into products which are sold on both domestic and export markets. Murray Goulburn's International business accounts for approximately 9% of world dairy trade and they trade in over 100 countries. Warrnambool Cheese and Butter engage in the manufacturing, processing and sale of cheese, milk powder, butter, cream, whey protein concentrate and bulk and processed milk. Murray Goulburn proposed to merge with Warrnambool Cheese and Butter on February 2010, the offer was declined by the Board.

National Foods Limited/Dairy Farmers Co-Operative
As one of Australia's biggest dairy companies, National Foods markets milk under brands such as the PURA, Farmers Union, Big M, King Island, and Masters flavoured milks. The company is the market leader in fresh dairy foods including Berri juice, Yoplait yogurt, and Tasmanian Heritage (cheese). National Foods also sells specialty cheese and gourmet foods. Dairy Farmers is one of the largest and oldest dairy manufacturers in Australia, established in 1900, supplying products to local and international markets such as Eastern Europe, the Middle East and Asia. Nation Foods acquired Dairy Farmers in August 2008.

Dairy Trust Limited/Open Country Cheese Limited
Dairy Trust (subsequently renamed Open Country Dairy Limited) was established by AFFCO in March 2007 as a vehicle designed to invest in the New Zealand dairy industry. Open Country Cheese is a New Zealand manufacturer of premium quality cheeses which it supplies to both New Zealand and international export markets. Dairy Trust increased its stake in Open Country Cheese to 100% in July 2008 by way of a full takeover offer.

Saputo Inc/Alto Dairy Co-Operative
Saputo is one of the largest dairy processors in the world. It produces, markets and distributes a wide array of products of the utmost quality, including cheese, fluid milk, yogurt, dairy ingredients and snack-cakes which are sold in more than 40 countries. Alto Dairy produces Italian-style cheeses such as mozzarella and provolone, and also American-style cheeses including; Cheddar varieties, Monterey Jack, Muenster, Fontina and Gouda. In addition, the firm produces whey products. Saputo acquired Alto Dairy in April 2008.