


Cereplast Inc.

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MARKET DATA

Symbol	CERP
Exchanges	OTCBB
Current Price	\$0.125
Price Target	\$1.12
Rating	Speculative Buy
Outstanding Shares	298.4 Million
Market Cap.	\$37.3 Million
Average 3M Volume	278,471

Source: Yahoo Finance, Analyst Estimates



CERP daily


Company Introduction

Cereplast Inc. (OTCBB: CERP) develops, manufactures and markets bio-based resins designed to supplement or even replace conventional petroleum-based plastics in a wide range of converting applications. CERP's resins are made from renewable resources such as corn, wheat, tapioca and potato starches. The Company markets two families of bio-based resins: Cereplast Compostables™ and Cereplast Hybrid Resins™. Cereplast Compostables™ resins are renewable, ecologically-sound substitutes for petroleum-based plastics, targeting primarily single-use disposables. Cereplast Hybrid Resins™ are also bio-based with a starch content of at least 50%, targeting durable applications such as automotive industry applications.

Since CERP's resins replace a significant amount of petroleum-based content with starches, costs are not as influenced by volatile fossil fuel prices. Also, Cereplast resin manufacturing requires less heat than traditional plastics manufacturing, further reducing manufacturing costs. In addition, CERP's resins offer comparable or superior performance and environmental benefits resulting from reduced petroleum consumption.

Changing Business Model

In May 2009, CERP announced a new strategic plan that better leverages its proprietary product development capabilities and marketing strengths. To accelerate growth, the Company plans to focus on product development and marketing the core strengths that position CERP as a leader in proprietary bio-plastics.

CERP's bio-plastic resins were specifically formulated for

compatibility with existing plastic manufacturing processes. Because of a worldwide glut of plastics compounding capacity, the Company plans to reduce costs by ending manufacturing and instead contracting with large plastic compounders to produce its bio-based resins. These relationships will also provide sufficient capacity to service substantial new contracts with major customers such as Georgia-Pacific and Dorel.

The Company is focusing its resources on higher value-added aspects of its business such as product development and assisting customers with implementing its bio-based plastic solutions. The same business model, which is widely used in the semiconductor industry, allows for maximum flexibility and innovation and rapid adaption to a constantly changing market.

CERP is already exploring ways to reduce its in-house manufacturing capacity at its Hawthorne, Calif., headquarters and its Seymour, Ind., manufacturing facility.

Operating Highlights

Product development and intellectual property

CERP is developing and commercializing two lines of resins: Cereplast Compostables™ and Cereplast Hybrid Resins™, commercially available since Q4 2006 and the Q3 2007, respectively.

Cereplast Compostables™ resins are renewable, ecologically-sound substitutes for petroleum-based plastics. They replace nearly 100% of the petroleum-based additives used in traditional plastics with plant starches. CERP has 15 grades of compostable resins in its product portfolio. These products address the needs of plastic converters serving the foodservice disposable packaging market.

Cereplast Hybrid Resins™ are bio-based and replace 50% or more of the petroleum content in conventional plastics with plant starches. This new hybrid line significantly expands the number of potential market applications for CERP resins. Cereplast Hybrid Resins™ may replace traditional petroleum-based plastics in automotive, consumer electronics, toys, medical, entertainment packaging, furniture, cosmetic packaging, consumer goods and construction applications.

CERP has reported significant progress in developing, extending and enhancing its two product lines since our initial report. Two new standard hybrid resin formulations have been developed for injection molding and sheet extrusion applications, and products based upon these formulations are being prepared for market launch.

In addition, development work on a compostable extrusion coating resin for coated paper applications is in the final phase of customer trials and expected to launch commercially in Q2 2009. Technical development of a compostable foam resin is also well advanced. Pilot scale trials with several customers are underway and commercial product launch is anticipated by year-end.

Additional technical projects focus on lowering the cost of Cereplast formulations, broadening the hybrid resin product line with “natural” based fibers and blends in addition to starches, improving processing economics and yields and improving



the economics and performance of compostable products.

Growing IP portfolio

The Company's intellectual property portfolio is a critical success factor. In 2008, CERP registered several new trademarks in different international classes covering packaging and plastic resin; its most significant marks, Cereplast Compostables® and Cereplast Hybrid Resins®, have been registered in the United States and in several international markets.

At present, CERP has about 24 mark registrations on file in the U.S. and abroad. The Company has filed for patent protection of its proprietary resin formulation technology in the U.S. and abroad and has been granted or filed a total of 48 patents worldwide.

Customer development agreements

As of December 31, 2008, more than 165 companies have requested and been provided with samples of CERP's bioplastic resin, and 95 customers have purchased resin for trials and testing. Of these, 65 customers have advanced to prototype testing and qualification of more than 110 different product applications. Twenty customers, including WNA, Alcoa, Genpak, Innoware, Penley, Solo, Cadaco, Jatco, Dentek, CSI-Cosmolab and Pace Industries, have commercialized and introduced more than 85 different bioplastic products using CERP resins. According to CERP management, the current commercialization "pipeline" represents more than \$20 million in potential annual sales realizable within the next 12 months.

The Company announced several new customer agreements during Q4 2008 and Q1 2009, including:

- An agreement with A. Schulman to distribute Cereplast Compostables® and Hybrids Resins® to converters and manufacturers in France, Benelux and Spain. The agreement will enable A. Schulman to launch new offerings based on bio-based materials to customers interested in more environmentally friendly solutions. A. Schulman is a leading international supplier of high-performance plastic compounds and resins used as raw materials in a variety of markets.
- A supply agreement with DenTek, a leading oral care company, whereby CERP will provide bioplastic resin for DenTek's new Natural Floss Picks, the first biodegradable/compostable floss pick on the market.
- An agreement to supply Absorbent Specialty Products with bioplastic resin for its new "Bio-Bones" bone replacement prosthetics.
- A supply agreement with Warner Manufacturing Company, whereby CERP will provide bio-plastic resin for Warner's new biodegradable painting accessories.
- An agreement to supply Dorel Juvenile Group USA, a division of Dorel Industries Inc., with bio-plastic resin for its Safety 1ST Nature Next™ reduced carbon footprint juvenile products. Dorel has launched four new products in this line, including a bathtub and step stool, using CERP's Hybrid Resins® as a replacement for conventional oil-based polypropylene.
- An agreement to supply Compostables® resin to Georgia-Pacific Professional Food Services Solutions for the manufacture of Dixie EcoSmart beverage solutions.

Production

CERP's manufacturing plant in Seymour, Ind., has 50 million pounds of annual bioplastic resin production capacity with the possibility to expand up to half a billion pounds. The facility is mechanically completed but currently in standby mode pending the outcome of several major customer contract discussions.

Industry Outlook

Bioplastics market

Global plastics consumption is forecast to grow more than 5% annually and exceed 500 billion pounds in 2010. This means that global plastics consumption is growing by more than 15 billion pounds per year. The bioplastics market is growing more rapidly as these products have begun to replace conventional plastics.

Bioplastics are used in the food packaging, medical, toys and textile industries. With new innovations expected in the near future, there will be additional applications for bioplastics in automobiles and electronics, where plastics play a major role. A new market report from Helmut Kaiser Consultancy reveals that the worldwide bioplastics market will grow 20% to 30% annually to 5 million tons in 2015 from 200,000 tons in 2006.

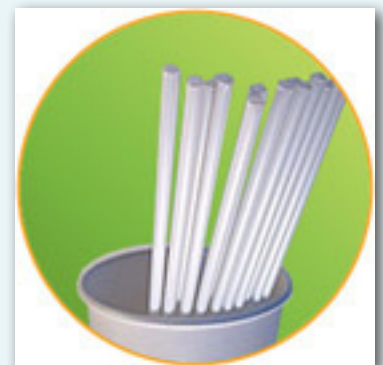
Bioplastics presently represent approximately 10%-15% of the total plastics market and will increase market share to 25%-30% by 2020. The plastics market itself is huge, reaching more than \$1 billion in 2007 and will rise to more than \$10 billion by 2020. More than 500 bioplastics processing companies are already operating and more than 5,000 companies are expected to compete by 2020.

According to Packaging Digest, bioplastics must overcome several hurdles before their use becomes as prevalent as traditional, petroleum-based products. Cost, performance, moisture-barrier properties, recycling, and food crop feedstock all must be improved to make bioplastics truly competitive. Despite this, several long-term trends will likely drive increasing use of bioplastics; these variables include volatile oil prices, energy security concerns, environmental benefits' favorable regulatory initiatives and the improving performance and competitiveness of bioplastic resins.

Oil prices

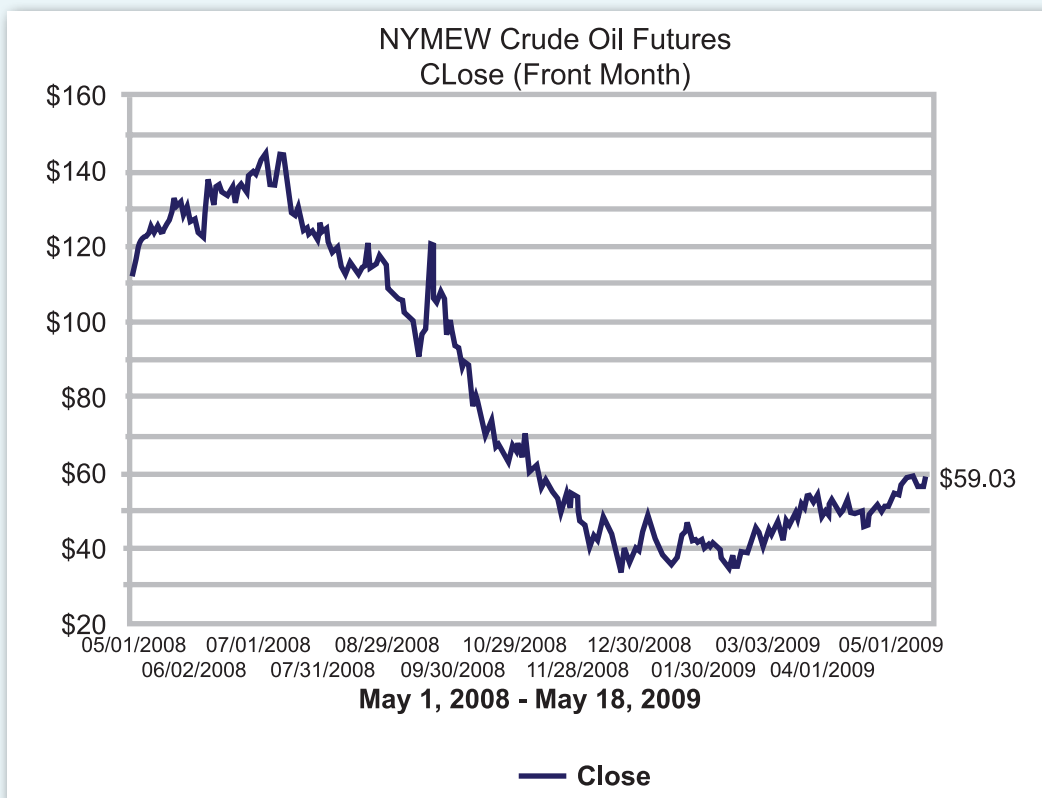
World oil consumption remains weak because of the global economic downturn and it is projected to fall by 1.8 million barrels per day (bbl/d) in 2009. World oil consumption is expected to grow by 0.7 million bbl/d in 2010, assuming rebounding global economic activity next year.

Energy prices have risen in Q2 2009 on indications that the U.S. economy may be starting to improve in some sectors. Crude oil prices are expected to range between \$50 and \$75 per barrel over the next few months. According to the Energy Information Administration (EIA), the price of West Texas Intermediate (WTI)



crude oil will remain relatively flat for the remainder of 2009, averaging about \$55 per barrel in the second half of 2009. Assuming modest economic improvement next year, WTI prices are expected to average about \$58 in 2010.

Declining oil prices have contributed to falling production costs for petroleum-based plastics. As expenses decline, the spread between conventional plastics new bioplastics widens and the premium on bioplastics is high right now at three to five times in some cases. Over the longer-term, however, it is likely that oil prices will rise and the price gap will narrow. The long-term outlook for bioplastics is positive because more consumers are interested in ecological products, and bioplastics will become competitive again if oil prices rise above \$80 a barrel, which is a possible scenario beginning with the second half of 2010.



Source: www.wtrg.com/daily/crudeoilprice.html

Environmental concerns

More than 200 million tons of plastic are manufactured annually around the world, according to the SPE. Of those 200 million tons, 26 million are manufactured in the United States. In 2003, only 5.8% of those 26 million tons of plastic waste were recycled, although this percentage is increasing rapidly. Traditional plastics do not biodegrade for hundreds of years. With billions and billions of pounds of plastics produced per year, the waste problem adds up.

Switching from conventional plastics to biodegradable bioplastics not only helps reduce demand for oil and cut the amount of waste sent to landfills, but also reduces carbon emissions. A new study from the Royal Melbourne Institute of Technology found that bioplastics use 60% less energy through their lifecycle than conventional polyethylene plastics and half the energy used by polylactic acid (PLA) bioplastics.

Legislation is a key determinant of plastics demand. China and Ireland have banned or taxed the use of plastic bags. Legislation has been introduced in the U.S. House of Representatives that would require all spring water be packaged in bioplastics and the city of Seattle will require all businesses serving carry-out food to use bioplastics by 2010.

A hot technology being discussed at this year's National Plastics Exposition (NPE) in Chicago (June 22-26) is plastics made from plants. Three raw material companies will report on bioplastics manufacturing ventures. Another 39 companies, agencies and industry consortia will make conference presentations on bioplastics technology and business strategy. On the NPE show floor, there will be 16 booths featuring bioplastics.

Financial Analysis

Income statement

In FY 2008 CERP reported net sales of \$4.5 million, compared with net sales of \$2.2 million in FY 2007, a 107% year-over-year increase. This sales growth is the result of volume growth in the Company's bioplastic resins from both existing and new customers launching commercial applications with its resins.

Income Statement, \$

	2007	2008	% chg
Net sales	2,179,998	4,512,156	107.0%
Cost of sales	2,090,730	4,431,976	112.0%
Gross profit	89,268	80,180	-10.2%
Total operating expenses, including	12,014,541	13,279,369	10.5%
Depreciation and amortization	373,687	545,832	46.1%
Financing costs	-	100,027	n/m
Financing discount costs	3,243,460	-	n/m
Marketing expense	252,275	1,547,547	513.4%
Professional fees	856,705	996,322	16.3%
Rent expense	367,276	1,064,765	189.9%
Research and development	321,450	1,071,814	233.4%
Salaries and wages	2,027,539	3,263,518	61.0%
Salaries, wages & stock-based compensation	3,142,477	2,859,680	-9.0%
Other operating expenses	1,429,672	1,829,864	28.0%
Operating profit	(11,925,273)	(13,199,189)	n/m
Other income	247,038	450,488	82.4%
Net income	(11,678,235)	(12,748,701)	n/m
Diluted EPS	(0.05)	(0.05)	n/m

Source: SEC Filings

Gross profit declined 10.2% from 2007, to \$80,180 in 2008. The decrease in gross profit was largely attributable to increases in raw material and associated freight costs experienced in the latter half of 2008, as well as the inclusion of a reserve for inventory obsolescence of \$132,000 charged to cost of sales in 2008 following a review of development grade resin stocks to reflect replacement by grades with improved performance characteristics and customer acceptance.

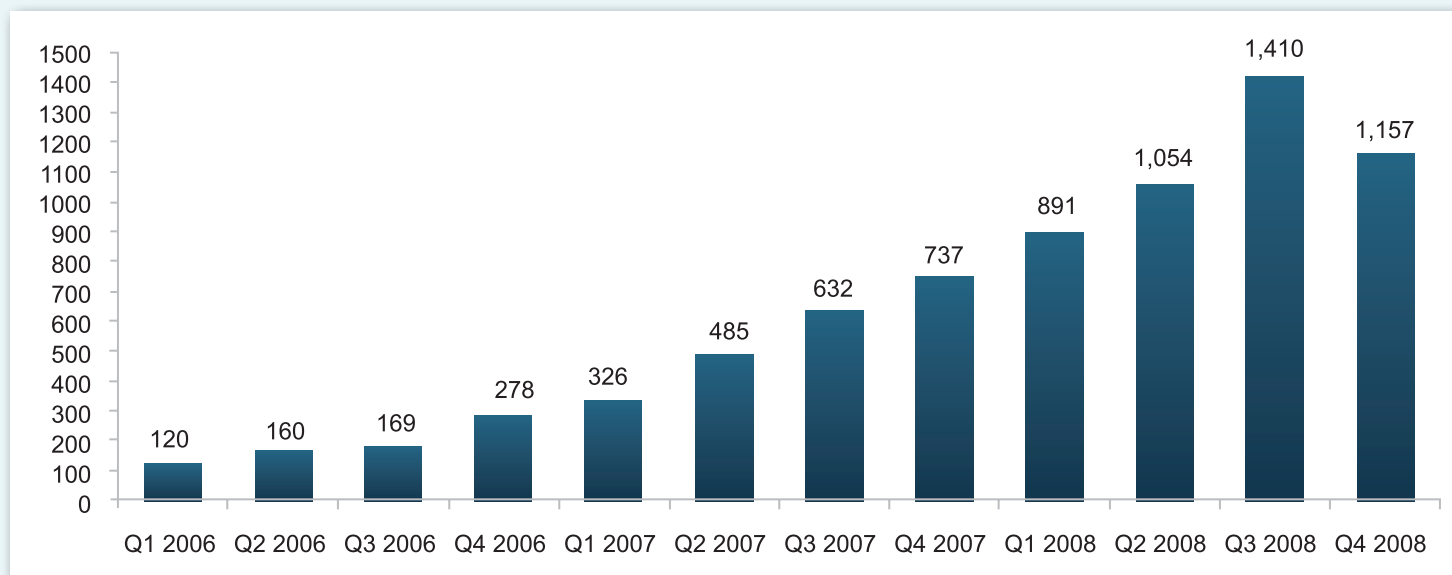
Operating expenses increased 10.5% to \$13.3 million in 2008 from \$12.0 million for 2007. The increase is attributable to higher spending to support technical development and commercial expansion of the Company's two resin families; upgrading business processes and strengthening functional management across all departments; expanding production, logistics and testing facilities; and support costs related to intellectual property, branding/communications and third-party testing/accreditation needs.

The Company reported a net loss of \$12.7 million, or \$0.05, per share, for 2008 compared with a net loss of \$11.7 million, or \$0.05 per share, in 2007. Higher net losses were a result of higher operating and development expenses associated with the growth of CERP's resin operations.

Quarterly results

Adverse business conditions contributed to a sequential decline in the Company's revenue in Q4 2008. However, we expect CERP to weather the negative impact of the consumer spending contraction with new customer contracts and the imminent launch of several new products into new markets.

Net revenues, \$ thousands



Source: SEC Filings

Liquidity

The Company had net unrestricted cash of \$501,699 at December 31, 2008, as compared to \$8,593,714 at December 31, 2007. Unrestricted cash fell because of funds used for operating activities and the purchase of equipment for CERP's Seymour facility.

During 2008, CERP used \$8,308,426 of cash for operating activities, \$2,891,918 for investing purposes and generated \$2,600,316 from equity sales. Members of the management team continue to take a significant component of their personal compensation in CERP stock in lieu of cash. In addition, all senior executives have agreed to defer an additional portion of their cash compensation in 2009 to help the Company conserve cash.

Balance sheet, \$ thousands

	12/31/07	12/31/08
Total Current Assets, including	10,919,991	2,781,439
Cash and Equivalents	8,593,714	501,699
Net Property and Equipment	2,251,595	4,596,714
Other Assets	122,591	266,856
Total Assets	13,294,177	7,645,009
Current Liabilities, including	836,333	2,242,107
Short term Debt	82,951	263,796
Long-Term Liabilities	91,314	40,045
Total Shareholders Equity, including	12,366,530	5,362,857
Accumulated Deficit	(16,623,319)	(29,372,020)

Source: SEC Filings

Based on the Company's operating plan, existing working capital is not sufficient to meet the Company's cash requirements through June 30, 2009, and CERP will need to raise additional cash. There is no assurance that CERP will be able to obtain additional financing on acceptable terms, or at all. If the Company cannot obtain additional financing, it may be forced to file for bankruptcy or cease operations.

During Q3 2008, CERP completed a \$2.6 million private placement of unregistered common stock with a group of existing investors. The Company also secured a \$20 million equity line of credit in December 2008 with an existing shareholder. During Q1 2009, the Company commenced a \$5.0 million unregistered private placement. The private placement has a rolling closing under which the Company has already received \$717,340 in gross proceeds. In addition, the Company is exploring other financing alternatives, including bank debt and convertible debt instruments.

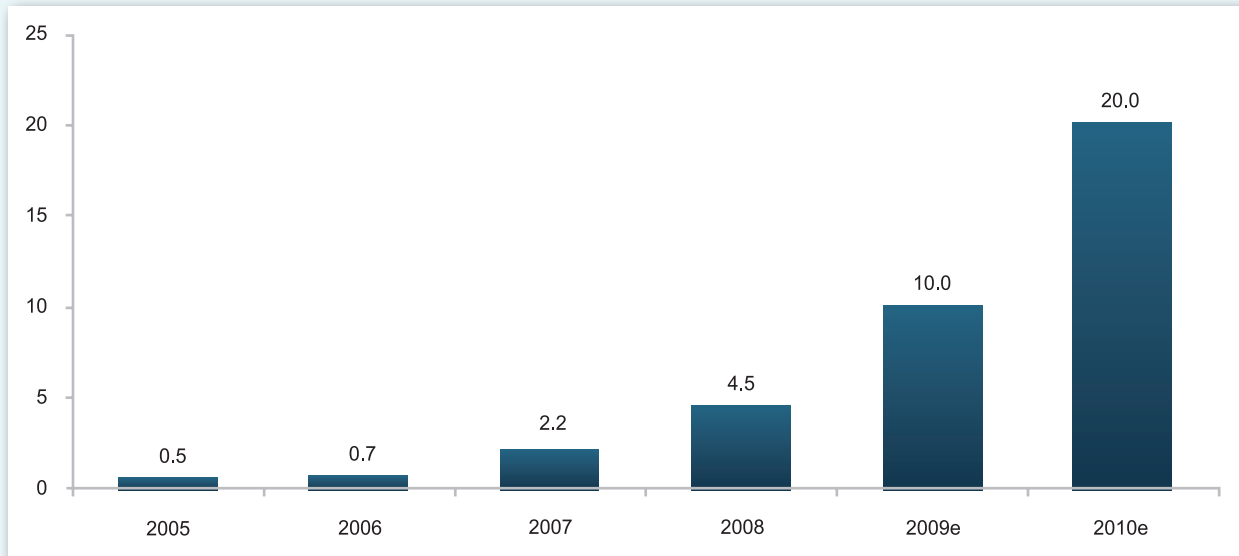
Analyst Summary

Since our initial report, CERP's share price has declined 80% from \$0.62 in December 2007 to \$0.125 in May 2009. The major reasons for the decline are lower-than-expected revenue growth, the general economic downturn and reduced consumer spending, poor liquidity and significant dilution to existing shareholders.

CERP's net sales declined sequentially in Q4 2008 and are expected to decline slightly in Q1 2009 compared to the same period in 2008 due to reduced demand from existing customers as a result of the general economic downturn.

However for full-year 2009, CERP's management anticipates new customer contracts, new product launches and applications for its resins in new markets will help fuel triple-digit, year-over-year revenue growth. Management forecasts 2009 revenues ranging around \$10 million and 2010 revenues rising to nearly \$20 million.

Revenue forecast, \$ Mn



Source: Management guidance

CERP faces liquidity challenges which may challenge its ability to grow the business. However, the Company is pursuing financing agreements in 2009 to support business growth and mitigate going concern risk.

Despite current challenges, the growth potential of CERP's bioplastics products is enormous. In addition, the Company has fine-tuned its business model to support rapid growth without significant cash outflows. Its proprietary technology, environmentally friendly resins and increasing visibility make CERP a potentially attractive takeover candidate for a larger chemicals and plastics company. We consider the revenue weakness in Q4 2008 and Q1 2009 to be temporary and expect growth to resume in the second half of 2009 as the Company signs new customers and launches new products.

We are also anticipating that bioplastics applications will continue to expand. CERP's resin products are ideal for nearly all brand owners and converters looking to enhance sustainability in their processes by substituting bioplastics for traditional petroleum-based plastics. Accordingly, we reiterate our Speculative Buy rating for Cereplast Inc. and \$1.12 long-term price target.

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Victor Sula, Ph.D. - Senior Analyst

Victor Sula, Ph.D. has held the position of Senior Analyst with several independent investment research firms since 2004. Prior to 2004, Mr. Sula held Senior Financial Consultant positions within the World Bank sponsored Agency for Restructuring and Enterprise Assistance and TACIS sponsored Center for Productivity and Competitiveness of Moldova, where he was involved in corporate reorganization and liquidation. He is also employed as Associate Professor at the Academy of Economic Studies of Moldova. Mr. Sula earned his Ph.D. degree in 2001 and bachelor's degree in Finance in 1997 from the Academy of Economic Studies of Moldova. Mr. Sula is currently a level III candidate in the CFA program.