

ASX RELEASE

10 January 2011

Folkestone Limited

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Recapitalisation of Folkestone Limited and acquisition of Equity Real Estate Partners

Folkestone Limited ("Folkestone") today announced that the company has approved a proposal to recapitalise Folkestone and to acquire Equity Real Estate Partners (EREP), both of which are subject to shareholder approval.

Folkestone will hold a general meeting of shareholders on 17 February 2011 at 10.00am at the offices of Deloitte, Level 10 550 Bourke Street Melbourne to vote on ten resolutions to approve the proposal. Attached to this announcement is a copy of the Chairman's Letter to Shareholders, Notice of Meeting and Explanatory Memorandum setting out further details of the proposal. A Notice of Meeting and Explanatory Memorandum will be forwarded to all shareholders.

If approved by shareholders, these initiatives are expected to provide existing Folkestone shareholders with access to an expanded management team with proven real estate and funds management experience and an enhanced capital base to take advantage of value-add, opportunistic, real estate investment development and funds management activities ("New Strategy").

Mr Alister Maitland, Folkestone's Non-executive Chairman said "I am delighted that we have been able to finalise agreement with the principals of EREP which if implemented will allow Folkestone, subject to shareholder approval, to be recapitalised to take advantage of the opportunities available in the Australian real estate market".

"The New Strategy is consistent with Folkestone's stated aim to pursue a transition into a larger listed real estate investment, development and funds management company" said Mr Maitland.

Key steps towards implementation of the New Strategy

In order to implement the New Strategy, it is proposed that Folkestone will:

- undertake a capital raising to raise gross proceeds of a minimum of \$20 million and up to a maximum of \$100 million at a minimum price of \$0.08 per share to recapitalise Folkestone to execute the New Strategy;
- acquire EREP from entities associated with Greg Paramor, Jonathan Sweeney and Adrian Harrington ("EREP Principals") for consideration of \$1 million;

- appoint the EREP Principals as senior executives of Folkestone;
- appoint a New Board with responsibility for implementing the New Strategy, including the appointment of Greg Paramor as Executive Chairman of Folkestone;
- provide for the retirement of Alister Maitland, Michael Parkinson and Kaye Dening from the Board immediately after the close of the meeting, should the Resolutions be approved; and
- implement an employee incentive plan to enhance alignment and grant certain incentives to the New Board members and senior executives.

The Folkestone Board recommends that, in the absence of a superior proposal, shareholders vote in favour of the Resolutions that will allow Folkestone to implement the New Strategy.

If the resolutions required to implement the New Strategy are not approved or the minimum \$20 million is not raised under the capital raising then Folkestone will continue an orderly sell down of projects in a manner and within a timeframe that will maximise shareholder returns with a view to winding-up the Company.

Further information in relation to the capital raising will be released following receipt of shareholder approval.

Key benefits of the New Strategy

The expected key benefits of the New Strategy include:

- a significant increase in Folkestone's capital base providing stability to the Company's existing development projects and enhancing its ability to proactively pursue additional real estate opportunities;
- retention and alignment of a senior management team, led by Greg Paramor, who have extensive experience in the real estate, funds management and financial services industries;
- an enhanced ability to capitalise on the unique investment opportunities presented in the Australian real estate sector;
- expansion of Folkestone's existing business to include a funds management platform which is expected to provide additional revenue streams and potential access to external sources of capital;
- increased flexibility in relation to unlocking the inherent value of Folkestone's existing development projects; and
- attraction of a highly qualified and experienced New Board.

Mr Greg Paramor, Executive Chairman of EREP said "We are pleased to be entering into this transaction with Folkestone. Following the recapitalisation, we believe it will be well placed to take advantage of a substantial number of attractive real estate opportunities that have arisen due to the recent dislocation in financial and real estate markets and that the New Strategy will position Folkestone to proactively pursue these opportunities and enhance shareholder returns."

Shareholders should read the Notice of Meeting and Explanatory Memorandum in full to assess the Resolutions being put forward for approval.

For further information regarding this announcement please contact:

Mr Scott Martin
Acting CEO
Chief Financial Officer & Company Secretary
Folkestone Limited
03-9543-2544

Mr Greg Paramor
Executive Chairman
Equity Real Estate Partners
02-9026-0466

Folkestone Limited

ABN 21 004 715 226

Notice of General Meeting

(incorporating an Explanatory Memorandum to Shareholders)

To be held at the offices of Deloitte, Level 10, 550 Bourke Street,
Melbourne VIC 3000 on Thursday 17 February 2011 at 10:00am
(Melbourne Time)

CHAIRMAN'S LETTER

10 January 2011

Folkestone

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Mount Waverley, Victoria 3170
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Telephone: 03) 9543 2544
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Dear Shareholder,

On 10 January 2011, the Folkestone Board announced a proposal to transform Folkestone with a significant capital raising initiative and the conditional acquisition of EREP, a real estate investment, development and funds management company.

If implemented, these initiatives are expected to provide existing Folkestone Shareholders with access to an expanded management team with proven real estate and funds management experience and an enhanced capital base to take advantage of value-add, opportunistic, real estate investment, development and funds management activities ("New Strategy"). The enclosed Explanatory Memorandum and Notice of Meeting set out in more detail these issues.

The Folkestone Board believes that there may be a substantial number of attractive real estate opportunities that have arisen due to the recent dislocation in financial and real estate markets and that the New Strategy will position Folkestone to proactively pursue these opportunities and enhance Shareholder returns.

The New Strategy is consistent with Folkestone's stated strategy to pursue a transition into a larger listed real estate investment, development and funds management company.

Key steps towards implementation of the New Strategy

In order to implement the New Strategy, it is proposed that Folkestone will:

- undertake a Capital Raising to raise gross proceeds of a minimum of \$20 million and up to a maximum of \$100 million at a minimum price of \$0.08 per Share to recapitalise Folkestone to execute the New Strategy. The VWAP of Folkestone Shares traded on the ASX for the 30 days to 5 January 2011 was 12.7 cents per Share;
- acquire EREP for \$1 million from entities associated with Greg Paramor, Jonathan Sweeney and Adrian Harrington ("EREP Principals");
- appoint the EREP Principals as senior executives of Folkestone;
- appoint a New Board with responsibility for implementing the New Strategy; and
- implement an employee incentive plan to enhance alignment and grant certain incentives to existing Folkestone Board members and senior executives.

The Capital Raising

In order to implement the New Strategy, Folkestone is seeking to undertake a Capital Raising to raise gross proceeds of a minimum of \$20 million and up to a maximum of \$100 million. The Capital Raising will recapitalise and reposition the Company to take advantage of investment opportunities in the Australian real estate sector.

If the Resolutions are approved, Alister Maitland, Michael Parkinson and Kaye Denning will resign at the end of the Meeting and the New Board will be appointed and will be responsible for undertaking the Capital Raising, which is contemplated to take place in early 2011. The Capital Raising is anticipated to include a placement to institutions and sophisticated investors and a public offer and a priority/entitlement offer to existing Shareholders under a prospectus. The precise structure of the capital raising will be determined by the New Board.

CHAIRMAN'S LETTER Continued

Vote on the New Strategy

In order to implement the New Strategy, ten Resolutions will be put to Shareholders for approval at the Meeting to be held on 17 February 2011. It is proposed that all Resolutions (with the exception of Resolution 10) will be interdependent and each Resolution other than Resolution 10 must be successfully passed before the New Strategy can be implemented.

All Resolutions (except the Resolution relating to the Capital Raising itself, Resolution 10 and the Resolutions for the New Board appointments) will only take effect once Folkestone has raised gross proceeds of a minimum of \$20 million as part of the Capital Raising. This is to assure Shareholders that the transactions relating to those Resolutions will only take effect where Folkestone has raised sufficient capital to commence executing the New Strategy in an effective manner.

If the minimum of \$20 million is not raised under the Capital Raising the other Resolutions will not come into effect and the New Strategy will not be implemented. The New Board will then continue with an orderly sell down of existing projects as detailed further in the Explanatory Memorandum.

Folkestone Board's recommendation

The Folkestone Board (other than the directors who have a conflict of interest – Greg Paramor and Hugh Gurner) assessed the merits of restructuring Folkestone to pursue the New Strategy against alternative strategies, including an orderly realisation of existing projects and a return of capital leading to a winding-up of Folkestone. The Folkestone Board engaged a major accounting firm to assist it in this assessment.

Taking into account the analysis of the alternatives, the Folkestone Board recommends that, in the absence of a superior proposal, you vote in favour of the Resolutions that will allow Folkestone to implement the New Strategy. Subject to any relevant voting exclusions, each of the members of the Folkestone Board intends to vote in favour of the Resolutions with respect to all Folkestone Shares in which they have a relevant interest. Notwithstanding this recommendation, also set out in sections 1.2 and 1.3 of the Explanatory Memorandum are reasons which you may consider in deciding whether to vote for or against the New Strategy respectively. In particular, you need to appreciate that whether or not the New Strategy is successfully implemented will be dependent on the ability of the New Board to successfully achieve the goals set out in it, and no assurance can be given that Shareholder returns will be enhanced under the New Strategy.

Key benefits of the New Strategy

In the opinion of the Folkestone Board, approval of the Resolutions that will allow Folkestone to implement the New Strategy represents the most attractive proposition for Shareholders in light of the other options available. The expected key benefits of the New Strategy include:

- a significant increase in Folkestone's capital base providing stability to the Company's existing development projects and enhancing its ability to proactively pursue additional real estate opportunities;
- retention and alignment of a senior management team, led by Greg Paramor, who have extensive experience in the real estate, funds management and financial services industries;
- an enhanced ability to capitalise on the unique investment opportunities presented in the Australian real estate sector;
- expansion of Folkestone's existing business to include a funds management platform which is expected to provide additional revenue streams and potential access to external sources of capital;
- increased flexibility in relation to unlocking the inherent value of Folkestone's existing development projects; and
- attraction of a highly qualified and experienced New Board.

CHAIRMAN'S LETTER Continued

Shareholder vote

There will be a Meeting of Shareholders held at 10:00am on 17 February 2011 at the offices of Deloitte, Level 10, 550 Bourke Street, Melbourne.

At this Meeting, Shareholders will be able to vote on the Resolutions set out in the Notice of Meeting to determine the future direction of Folkestone.

Shareholders are encouraged to attend the Meeting to cast their vote. You may also vote by returning the proxy form enclosed with the Notice of Meeting in accordance with the instructions on the form.

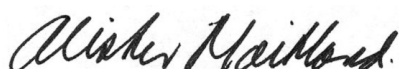
Further information

The Explanatory Memorandum contains important information in relation to the Resolutions and the New Strategy, including possible risks and disadvantages, and I encourage you to read the Explanatory Memorandum carefully before making your decision and voting at the Meeting.

A prospectus relating to the Capital Raising will be lodged by the New Board with ASIC at the appropriate time and will be distributed separately. You should review that document for important information in relation to the Capital Raising if you are interested in participating in it.

On behalf of the Folkestone Board, I recommend the New Strategy to you and encourage you to read the Explanatory Memorandum, attend the Meeting and, in the absence of a superior proposal, vote in favour of the Resolutions that will allow the implementation of the New Strategy.

Yours sincerely,



Alister T L Maitland
Chairman
Folkestone Limited

NOTICE OF GENERAL MEETING

FOLKESTONE LIMITED

A.B.N. 21 004 715 226

A General Meeting of **FOLKESTONE LIMITED** will be held at the offices of Deloitte at Level 10, 550 Bourke Street, Melbourne, Victoria 3000 on 17 February 2011 commencing at 10:00am.

Agenda

1. Change of Business

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed and subject to the Company raising gross proceeds of at least \$20 million pursuant to the capital raising proposed in Resolution 2, that for the purposes of ASX Listing Rule 11.1.2 and for all other purposes, the Company is authorised to acquire all of the issued share capital of Equity Real Estate Partners Pty Ltd (“EREP”) on the terms and conditions of the Share Sale Agreement described in the Explanatory Memorandum, and to effect a consequential change in the activities of the Company from real estate development to real estate investment, development and funds management as described in the Explanatory Memorandum.”

2. Capital Raising

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed, that for the purposes of ASX Listing Rule 7.1 and for all other purposes, the shareholders of the Company approve the proposed issue of up to 1,250,000,000 fully paid ordinary shares in the capital of the Company at a minimum issue price of 8 cents per share to raise gross proceeds of a minimum of \$20 million and up to \$100 million on the basis set out in the Explanatory Memorandum.”

3. Issue of Shares to the EREP Vendors

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed and subject to the Company raising gross proceeds of at least \$20 million pursuant to the capital raising proposed in Resolution 2, that for the purposes of ASX Listing Rule 10.11 and for all other purposes, the shareholders of the Company approve the following proposed issues of shares in the capital of the Company, each at a deemed issue price of 10 cents per share, as

may be adjusted on the basis set out in the Explanatory Memorandum as consideration for the acquisition of Equity Real Estate Partners Pty Ltd:

- The issue of 2,500,000 shares to an entity controlled by Adrian Harrington by the name of Adkar Investments Pty Ltd as trustee for the Harrington Family Trust;
- The issue of 2,500,000 shares to an entity controlled by Jonathan Sweeney by the name of Serrano Investments Pty Ltd as trustee for the ES and JS Family Trust; and
- The issue of 5,000,000 shares to an entity controlled by Greg Paramor by the name of ERE Holdings Pty Ltd as trustee for the Para EREP Trust.”

4. Executive Incentive Performance Rights Plan

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed and subject to the Company raising gross proceeds of at least \$20 million pursuant to the capital raising proposed in Resolution 2, that for the purposes of ASX Listing Rule 7.2 Exception 9(b) and for all other purposes, the directors of the Company are authorised to implement and maintain a plan to be called the “Folkestone Incentive Performance Rights Plan” and to issue Performance Rights under that plan from time to time to persons who are eligible to participate in the plan upon the terms and conditions specified in the Folkestone Incentive Performance Rights Plan Rules (the terms of which are summarised in the Explanatory Memorandum), and to issue shares in the capital of the Company upon vesting of those Performance Rights from time to time, as an exception to ASX Listing Rule 7.1”.

5. Issue of Performance Rights to Greg Paramor

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed and subject to the Company raising gross proceeds of at least \$20 million pursuant to the capital raising proposed in Resolution 2, that for the purpose of ASX Listing Rule 10.14 and for all other purposes, the shareholders of the Company authorise and approve the grant by the Company to Mr Greg Paramor of up to 15 million Performance Rights and the issue of shares upon vesting of those Performance Rights from time to time, in

NOTICE OF GENERAL MEETING Continued

accordance with the Folkestone Incentive Performance Rights Plan and otherwise on the terms and conditions set out in the Explanatory Memorandum.”

6. Issue of Performance Rights to Jonathan Sweeney

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed and subject to the Company raising gross proceeds of at least \$20 million pursuant to the capital raising proposed in Resolution 2, that for the purpose of ASX Listing Rule 10.14 and for all other purposes, the shareholders of the Company authorise and approve the grant by the Company to Mr Jonathan Sweeney of up to 7.5 million Performance Rights and the issue of shares upon vesting of those Performance Rights from time to time, in accordance with the Folkestone Incentive Performance Rights Plan and otherwise on the terms and conditions set out in the Explanatory Memorandum.”

7. Issue of Performance Rights to Adrian Harrington

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed and subject to the Company raising gross proceeds of at least \$20 million pursuant to the capital raising proposed in Resolution 2, that for the purpose of ASX Listing Rule 10.14 and for all other purposes, the shareholders of the Company authorise and approve the grant by the Company to Mr Adrian Harrington of up to 7.5 million Performance Rights and the issue of shares upon vesting of those Performance Rights from time to time, in accordance with the Folkestone Incentive Performance Rights Plan and otherwise on the terms and conditions set out in the Explanatory Memorandum.”

8. Appointment of Garry Sladden as a Director

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed, Garry Sladden, being eligible and having offered himself for election, be elected as a Director of the Company”.

9. Appointment of Ross Strang as a Director

To consider and, if thought fit, pass the following as an ordinary resolution:

“Subject to all other Resolutions (other than Resolution 10) being passed, Ross Strang, being eligible and having offered himself for election, be elected as a Director of the Company”.

10. Participation in placement by Greg Paramor

To consider and, if thought fit, pass the following as an ordinary resolution:

“That, for the purpose of ASX Listing Rule 10.11 and for all other purposes, the shareholders of the Company authorise and approve the issue of up to 40 million fully paid ordinary shares in the capital of the Company at a minimum issue price of 8 cents per share to Greg Paramor, or an entity associated with Greg Paramor, pursuant to, and on the same terms as, the capital raising proposed in Resolution 2 and on the basis set out in the Explanatory Memorandum”.

By Order of the Board



Scott Martin
Company Secretary

10 January 2011

NOTICE OF GENERAL MEETING Continued

Voting exclusion statements

- In relation to Resolution 1, the Company will disregard any votes cast on the resolution by the EREP shareholders and any person who might obtain a benefit, except a benefit solely in the capacity of a holder of ordinary securities, if the resolution is passed, and any associate of that person or those persons.
- In relation to Resolution 2, the Company will disregard any votes cast on the resolution by any person who is to participate in the non-public offer component of the capital raising. This means that if you vote you will not be able to participate in the non-public offer.
- In relation to Resolution 3, the Company will disregard any votes cast on the resolution by any person who is to receive securities in the Company pursuant to that resolution and any associate of that person or those persons.
- In relation to Resolution 4, the Company will disregard any votes cast on the resolution by a director of the Company and any associate of that person or those persons.
- In relation to Resolution 5, the Company will disregard any votes cast on the resolution by a director of the Company and any associate of that person or those persons.
- In relation to Resolution 6, the Company will disregard any votes cast on the resolution by Jonathan Sweeney, a director of the Company and any associate of that person or those persons.
- In relation to Resolution 7, the Company will disregard any votes cast on the resolution by Adrian Harrington, a director of the Company and any associate of that person or those persons.
- In relation to Resolution 10, the Company will disregard any votes cast on the resolution by Greg Paramor and any associate of that person.

These voting exclusions do not apply if:

- the vote is cast by a person as a proxy for a person who is entitled to vote in accordance with the directions on the proxy form; or
- it is cast by the Chairman as a proxy for a person who is entitled to vote in accordance with a direction on the proxy form to vote as the proxy decides.

Entitlement to attend and vote

In accordance with Reg 7.11.37 of the Corporations Regulations 2001, the Board has determined that persons who are registered holders of shares of the Company as

at 7:00pm on the day which is two days before the date of the meeting will be entitled to attend and vote at the Meeting as a shareholder.

If more than one joint holder of shares is present at the meeting (whether personally, by proxy or by attorney or by representative) and tenders a vote, only the vote of the joint holder whose name appears first on the register will be counted.

Proxies

If you are unable to attend and vote at the meeting and wish to appoint a person who is attending as your proxy, please complete the enclosed proxy form. This form must be received by the Company by 48 hours before the commencement of the meeting.

The completed proxy form may be:

- Mailed to Link Market Services Limited, Locked Bag A14, Sydney South, NSW 1235;
- Faxed to 61-2-9287-0309;
- Delivered by hand to Link Market Services Limited, Level 12, 680 George Street, Sydney, NSW 2000; or
- Completed online at www.linkmarketservices.com.au

A member entitled to attend and vote is entitled to appoint not more than two proxies. Where more than one proxy is appointed, each proxy must be appointed to represent a specific proportion of the members voting rights. A proxy need not be a member of the Company. The Chairman of the Meeting intends to vote all undirected proxies in favour of each Resolution.

Voting by Attorney

If the proxy form is signed under power of attorney, then the original power of attorney under which the proxy form is signed (or a certified copy of that power of attorney or other authority) must be provided to the Company before the meeting.

Corporate Representatives

A body corporate which is a shareholder, or which has been appointed as a proxy, is entitled to appoint any person to act as its representative at the meeting. The appointment of the representative must comply with the requirements under section 250D of the Corporations Act. The representative should bring to the meeting a properly executed letter or other document confirming its authority to act as the company's representative.

Folkestone Limited

Explanatory Memorandum

10 January 2011

The Folkestone Board **RECOMMENDS** that
you **VOTE IN FAVOUR** of the
Resolutions to approve the New Strategy,
in the absence of a superior proposal

This Explanatory Memorandum accompanies a Notice of Meeting and proxy form.

Your vote is important in determining whether the New Strategy proceeds.

This is an important document and requires your immediate attention.
You should read this document in its entirety before deciding how to vote.

If you have any questions about the Resolutions or other information contained in
this Explanatory Memorandum, please call Folkestone on 03 9543 2544,
Monday to Friday between 8.30am and 5.30pm (AEST).

If you are in doubt as to what you should do, you should consult your professional adviser.

Important notices

What is this document?

This document is the Explanatory Memorandum accompanying the Notice of Meeting. The document provides such information as is prescribed or otherwise material to the decision of Shareholders on how to vote on the Resolutions at the Meeting.

The primary purpose of this Explanatory Memorandum is to provide Shareholders with information about the Resolutions which, if approved, will result in the recapitalisation of Folkestone and will reposition Folkestone to take advantage of the unique investment opportunities in the Australian real estate sector that have arisen through the recent dislocation in financial and real estate markets. Folkestone will be in a position to pursue its strategy to become a larger listed real estate development, investment and funds management company.

Date

This Explanatory Memorandum is dated 10 January 2011.

General

Shareholders should read this Explanatory Memorandum in its entirety before making a decision as to how to vote on the Resolutions to be considered at the Meeting.

If you have any questions about the Resolutions, please contact Folkestone on 03 9543 2544, Monday to Friday between 8.30 am and 5.30 pm (AEST). For information about your individual circumstances, please consult your professional adviser.

Folkestone may update the Notice of Meeting and Explanatory Memorandum by posting the relevant amendments on its website. Folkestone will provide shareholders with a paper copy of such amendments on request.

No investment advice

This Explanatory Memorandum does not constitute financial product advice and has been prepared without reference to your particular investment objectives, financial situation, tax situation or needs.

Folkestone Board

References in this document to the beliefs, recommendations and considerations of

the Folkestone Board in respect of the New Strategy and the Resolutions are, where the context permits, references to those members of the Board who do not have a conflict of interest with respect to the matters being considered and voted on at the Meeting. All other references to the Folkestone Board in this Explanatory Memorandum refer to all members of the Board of Folkestone.

All references in this Explanatory Memorandum to the New Board are to Greg Paramor, proposed Executive Chairman; Hugh Gurner, Non-Executive Director; Garry Sladden, proposed Non-Executive Director; and Ross Strang, proposed Non-Executive Director. All references in this Explanatory Memorandum to the New Strategy means the strategy to be implemented by the New Board. Each member of the New Board has consented in writing to all references to them in this Explanatory Memorandum, in the form and context in which they appear.

Disclosure regarding forward-looking statements

This Explanatory Memorandum contains both historical and forward-looking statements in connection with Folkestone and EREP. Past performance is not indicative of future performance.

The forward-looking statements in this Explanatory Memorandum are not based on historical facts, but reflect the current expectations of Folkestone or EREP, as the case may be, concerning future results and events and generally may be identified by the use of forward-looking words or phrases such as “believe”, “aim”, “expect”, “anticipated”, “intending”, “foreseeing”, “likely”, “should”, “planned”, “may”, “estimated”, “potential”, or other similar words and phrases. Similarly, statements that describe Folkestone’s or EREP’s objectives, plans, goals or expectations are or may be forward-looking statements.

These forward-looking statements involve known and unknown risks, uncertainties, assumptions and other factors that may cause either Folkestone’s or EREP’s actual results, performance or achievements to

differ materially from the anticipated results, performance or achievements expressed, projected or implied by these forward-looking statements. Deviations as to future results, performance and achievements are both normal and to be expected. Shareholders should review carefully all of the information, including the financial information, included in this Explanatory Memorandum. The forward-looking statements included in this Explanatory Memorandum are made only as of the date of this Explanatory Memorandum. Neither Folkestone nor EREP gives any representation, assurance or guarantee to Shareholders that any forward-looking statements will actually occur or be achieved. Shareholders are cautioned not to place undue reliance on such forward-looking statements.

Subject to any continuing obligations under law or the ASX Listing Rules, neither Folkestone nor EREP give any undertaking to update or revise any forward-looking statements after the date of this Explanatory Memorandum to reflect any change in expectations in relation to those statements or any change in events, conditions or circumstances on which any such statement is based.

Disclosure regarding EREP

Section 4 of this Explanatory Memorandum has been prepared by EREP. Neither Folkestone nor any of its directors, officers and advisers assumes any responsibility for the accuracy or completeness of Section 4 of this Explanatory Memorandum. EREP has consented to all references to EREP in this Explanatory Memorandum, in the form and context in which they appear.

Defined terms

Capitalised terms used in this Explanatory Memorandum and proxy form are defined in the Glossary.

Voting

Your vote is important and is your opportunity to have your say on the Resolutions and the future direction of Folkestone. The decisions at the Meeting could have a significant impact on your investment and therefore the Folkestone Board encourages Shareholders to vote.

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Key dates

Date	Event
10:00am, 15 February 2011	Last date for receipt of proxies
7:00pm, 15 February 2011	Record date for voting eligibility at the Meeting
10:00am, 17 February 2011	Meeting

The timetable is indicative only. Folkestone reserves the right to vary any or all of these dates and times.

*All references to time in this Explanatory Memorandum are to AEST.

1. OVERVIEW OF THE NEW STRATEGY

1.1 BACKGROUND TO THE NEW STRATEGY

A detailed description of the various initiatives comprising the New Strategy as provided by EREP is set out in Section 4. By way of summary, the key features of the New Strategy include:

- undertaking promptly after the Meeting a Capital Raising to raise gross proceeds of a minimum of \$20 million and up to a maximum of \$100 million to recapitalise Folkestone. Upon the minimum amount of \$20 million being raised, the following aspects of the New Strategy will be implemented;
- acquisition of EREP pursuant to a Share Sale Agreement for total consideration of \$1 million intended to be payable by the issue of 10 million Folkestone Shares to the EREP shareholders;
- appointment of a team led by Greg Paramor, Jonathan Sweeney and Adrian Harrington as new senior management of Folkestone. These three individuals possess extensive experience in the Australian real estate, financial services and funds management industries and have an established track record of performance across these industries;
- implementation of a new investment strategy which will enable the Company to take advantage of investment opportunities presented by the recent dislocation in real estate and financial markets;
- implementation of a new Executive Incentive Performance Rights Plan as part of the Company's overall remuneration strategy which is designed to attract, retain and motivate qualified and experienced directors and senior executives.

The New Board, with a majority of Non-Executive Directors, will be appointed at the end of the Meeting if Resolutions 1 to 9 are passed, and Alister Maitland, Michael Parkinson and Kaye Dening will simultaneously resign. The New Board is charged with the responsibility of implementing the Capital Raising and the New Strategy.

Folkestone repositioned

Folkestone has stated its intention to transition into a larger listed real estate investment, development and funds management company that is attractive to both institutional and retail investors. Under the New Strategy, Folkestone will be repositioned to undertake value-add and opportunistic investments presented by the recent downturn in real estate and financial markets including:

- acquiring assets from distressed real estate owners and developers on attractive terms;

- partnering with balance sheet constrained developers to provide funding for quality real estate projects;
- acquiring development opportunities for Folkestone's balance sheet or managed funds; and
- investing in preferred equity or mezzanine loans backed by real estate assets.

Under the New Board it is intended to expand EREP's existing real estate funds management platform with funds being offered to private clients, high net worth individuals and select institutional investors across the risk-return spectrum.

Rationale for the New Strategy

Upon implementation of the matters set out in the Resolutions, Folkestone will be repositioned as a diversified real estate investment, development and funds management company.

The Folkestone Board believes that the New Strategy provides Folkestone with a tangible path to potentially generate enhanced Shareholder returns for the following reasons:

- the Capital Raising will generate a significant increase in Folkestone's capital base providing stability to the Company's existing developments and enhancing its ability to proactively pursue opportunistic real estate investments;
- the retention and alignment of a senior management team, led by Greg Paramor, who have extensive experience in the real estate, funds management and financial services industries with a strong track record of performance;
- an enhanced ability to capitalise on the unique investment opportunities that exist in the Australian real estate sector as a result of the recent dislocation in real estate and financial markets; and
- the expansion of Folkestone's existing business to include a funds management platform which is expected to provide additional revenue streams and access to external sources of capital.

Shareholder approvals required

In order to implement the New Strategy, ten Resolutions will be put to Shareholders for approval at the Meeting to be convened on 17 February 2011. It is proposed that all Resolutions (with the exception of Resolution 10) will be interdependent, and each Resolution other than Resolution 10 must be successfully passed before the New Strategy can be implemented. Resolutions 1-9 will proceed if approved, even if Resolution 10 is not approved.

1. OVERVIEW OF THE NEW STRATEGY Continued

In addition, all Resolutions (except the Resolution relating to the Capital Raising itself, Resolution 10 and the Resolutions for the New Board appointments) will only take effect once Folkestone has raised gross proceeds of a minimum of \$20 million as part of the Capital Raising. This is to assure Shareholders that the transactions relating to those Resolutions will only take effect where Folkestone has raised sufficient capital to commence executing the New Strategy in an effective manner.

If the minimum of \$20 million is not raised under the Capital Raising the other Resolutions (with the exception of Resolutions 8, 9 and 10) will not come into effect, EREP will not be acquired and the New Strategy will not be implemented. The New Board will then continue with an orderly sell down of existing projects.

1.2 REASONS TO VOTE FOR THE NEW STRATEGY

The Folkestone Board recommends that you VOTE IN FAVOUR of the Resolutions which will allow the implementation of the New Strategy, in the absence of a superior proposal. Reasons to approve the Resolutions and the New Strategy include the following:

Best option available to Shareholders

The Folkestone Board engaged a major accounting firm to assess the merits of approving the Resolutions against alternative strategies to enhance Shareholder returns, including an orderly realisation of existing projects and subsequent return of capital leading to a winding-up of Folkestone. Taking into account the analysis of the alternative strategies completed by the major accounting firm and having regard to potential reasons to vote against the Resolutions in Section 1.3, it is the opinion of the Folkestone Board that the approval of the Resolutions that should allow the implementation of the New Strategy will provide a superior outcome to Folkestone Shareholders as compared to the alternative strategies currently available to Folkestone.

Folkestone's New Strategy will be implemented by an experienced senior management team

Following the acquisition of EREP and employment of the EREP Principals, Folkestone's senior management team will include Greg Paramor, Jonathan Sweeney and Adrian Harrington. These three individuals possess extensive experience in, and long-standing relationships throughout, the Australian real estate, financial services and funds

management industries with an established successful track record of performance across real estate investment, development and funds management activities.

Experienced New Board

The New Board will comprise four members with a majority of Non-Executive Directors. This is one of the recommendations for best practice from a corporate governance perspective for an ASX listed company. Each of the members of the New Board possesses extensive experience in acting as senior executives and directors of both listed and unlisted entities and has an established track record of performance in the Australian market.

An enhanced ability to pursue a diverse range of Australian real estate opportunities

If the Resolutions are adopted, it is intended Folkestone will be transitioned into an integrated real estate group with the ability to pursue a diverse range of Australian real estate opportunities across:

- investment types: such as direct investment, joint venture investments and co-investing in Folkestone managed funds;
- capital structures: equity, preferred equity and mezzanine debt; and
- sectors: office, retail, industrial, residential and social infrastructure.

Folkestone's broad investment mandate will provide the Company with the flexibility to take advantage of investment opportunities as they arise including those that have resulted from the recent downturn in real estate and financial markets.

Improved financial position and enhanced flexibility

Folkestone will be recapitalised with proceeds from the Capital Raising and will be repositioned to proactively pursue opportunistic real estate investment opportunities. The additional capital will also present Folkestone with enhanced flexibility to unlock the inherent value in its existing three development projects in a manner and within a timeframe that enhances Shareholder returns.

Expansion of Folkestone's existing business to include a funds management platform

Following the acquisition of EREP, under the New Strategy Folkestone will look to grow EREP's existing real estate

1. OVERVIEW OF THE NEW STRATEGY Continued

funds management platform that actively manages funds on behalf of private clients, high net worth individuals and select institutional investors. This is intended to present Folkestone with new revenue streams and additional sources of third party capital, offering flexibility in assessing, funding, holding and managing real estate assets and generating enhanced Shareholder returns.

Potential exposure to higher returns

Under the New Strategy, Folkestone will target an after-tax return on equity of 15.0% per annum on a rolling three year basis once the proceeds from the Capital Raising are fully deployed. It is currently considered unlikely that Folkestone will pay any dividends for a period of at least three years with any excess capital generated to be re-invested into future investment opportunities and the funds management platform.

Prospects if the New Strategy is not implemented

In August 2009, Folkestone announced that it would pursue an orderly sell down of existing projects in a manner and within a timeframe that would maximise Shareholder returns, followed by a winding-up of the Company. The stated timeframe was for this process to be completed by December 2011. Details of the projects are set out in Section 3.

The Noone Street, residential project remains on track to be completed by this date, however the ability of the Company to achieve this timeframe for the Millers Road and Donnybrook Road projects in a manner that will maximise Shareholder returns continues to be impacted by the subdued state of the bulky goods and industrial property markets.

1.3 REASONS TO VOTE AGAINST THE NEW STRATEGY

The Folkestone Board recommends that you VOTE IN FAVOUR of the Resolutions which will allow the implementation of the New Strategy, in the absence of a superior proposal. However, factors that may lead you to vote against the New Strategy include the following:

Changing nature of your investment

If the New Strategy is implemented, Folkestone's operations will expand to include opportunistic real estate investment, development and funds management. Whilst these activities may provide Folkestone with the prospect of generating higher earnings and growth, this may also result in a higher risk profile for the Company. As the New Strategy is opportunistic and not definitive it is not possible to independently assess the projected cash flows or discount these cash flows back to present value.

Dilution of existing shareholding

The Capital Raising will result in a dilution to the interests of existing Folkestone Shareholders, particularly if Shareholders elect not to participate in that Capital Raising.

Transaction costs

Folkestone will incur fees and costs of approximately 5%-8% of the gross proceeds raised in relation to the implementation of the New Strategy if it is approved. These fees and costs primarily relate to underwriting and professional advisory fees which will be dependent on the size of the Capital Raising and will be paid from the proceeds of the Capital Raising.

Key person risk

It is intended that the New Strategy will be implemented by a senior management team including Greg Paramor, Jonathan Sweeney and Adrian Harrington, which will provide Folkestone with an extensive network of relationships within the real estate industry and capital markets. The loss of services of any of these key personnel could adversely affect Folkestone's ability to successfully implement the New Strategy.

Minimal history

Despite the New Board's extensive involvement in the Australian real estate investment, development and funds management industries, the New Board will not comprise any person with more than a one year history of Folkestone's business.

1. OVERVIEW OF THE NEW STRATEGY Continued

Executive Chairman

Under the New Strategy Greg Paramor will act as Executive Chairman with effect from the date of successfully raising \$20 million under the Capital Raising. This may not be considered best practice from a corporate governance perspective for an ASX listed company.

Business strategy risk

The New Strategy requires the ability to deploy the capital raised under the Capital Raising in new investment opportunities. If appropriate opportunities do not arise, Folkestone under the stewardship of the New Board will not be able to implement the New Strategy and the performance of Folkestone may be adversely impacted. There is no guarantee that the New Strategy will result in Folkestone delivering the target after-tax return on equity of 15.0% per annum.

Other risks

Other key risks associated with an investment in Folkestone and with the adoption of the New Strategy are set out in section 6.

Disagreement regarding the relative merits of the strategic options open to Folkestone

You may not agree with the view of the Folkestone Board that the New Strategy is superior to the other strategic options available to Folkestone, including a winding-up of the Company.

Expectation of a superior proposal

You may consider that there is the potential for a superior proposal to be made. As at the date of this Explanatory Memorandum, no superior proposal has emerged.

2. FREQUENTLY ASKED QUESTIONS

2.1 OVERVIEW

Question	Answer	Where can I find further information?
<p>Why have I received this Explanatory Memorandum?</p>	<p>This Explanatory Memorandum has been sent to you because you are a Folkestone Shareholder.</p> <p>This Explanatory Memorandum is intended to help you to decide how to vote on the Resolutions to be tabled at the Meeting on 17 February 2011 at 10:00am to approve the New Strategy.</p> <p>You should carefully read this Explanatory Memorandum and, if necessary, consult your legal, tax, financial or other independent professional adviser before voting on the Resolutions.</p>	
<p>What is the New Strategy?</p>	<p>Under the New Strategy it is proposed that Folkestone will be repositioned and will implement a new business strategy focusing on value-add, opportunistic, real estate investment, development and funds management.</p> <p>The New Strategy comprises the following key elements:</p> <ul style="list-style-type: none"> • acquire EREP for consideration of \$1.0 million intended to be payable through the issue of 10 million Folkestone Shares at \$0.10 per share; • appoint the EREP Principals as senior executives of Folkestone; • appoint a New Board with responsibility for implementing the New Strategy; • implement an incentive plan; and • undertake a Capital Raising to raise between \$20 million and \$100 million. 	Section 4
<p>What alternatives to the New Strategy have the Folkestone Board considered?</p>	<p>As part of a strategy review, the Folkestone Board analysed a number of alternatives for the future of Folkestone, with a focus on maximising Shareholder value.</p> <p>The alternatives considered by the Folkestone Board included the realisation of Folkestone's current assets and return of capital to Shareholders, and subsequent winding-up of the Company.</p> <p>Current market conditions, Folkestone's limited capital base, limited cash reserves and the fact that its investments include joint venture and minority interests continue to adversely impact the ability of Folkestone to complete the realisation of existing projects in a manner and within a timeframe that will maximise Shareholder returns. The New Strategy provides Folkestone with a stable platform from which to grow and should provide it with the ability to enhance Shareholder returns.</p>	Section 3.5

2. FREQUENTLY ASKED QUESTIONS Continued

Question	Answer	Where can I find further information?
Does the Folkestone Board recommend the New Strategy?	The Folkestone Board recommends that you vote in favour of the New Strategy, in the absence of a superior proposal.	Section 1.2
Why is there a Meeting?	<p>The New Strategy is subject to a number of conditions, including Folkestone Shareholder approval by the requisite majorities. Folkestone has convened the Meeting to allow Shareholders to consider the Resolutions.</p> <p>The Resolutions and the requisite majorities are set out in the Notice of Meeting accompanying this Explanatory Memorandum.</p>	Notice of Meeting
What is the effect of the Resolutions being approved?	<p>All Resolutions (with the exception of Resolution 10) are interdependent and each Resolution other than Resolution 10 must be successfully passed before the New Strategy can be implemented. All Resolutions (except the Resolution relating to the Capital Raising itself, Resolution 10 and the Resolutions for the New Board appointments) will only take effect once Folkestone has raised a minimum \$20 million as part of the Capital Raising. This will ensure that the Company has sufficient capital to enable it to commence implementing the New Strategy in an effective manner.</p> <p>Subject to the minimum Capital raising of \$20 million (other than in respect of the Resolutions for the New Board appointments), Resolutions 1-9 will proceed if approved, even if Resolution 10 is not approved.</p>	Notice of Meeting
What are my options?	<p>If you are a Folkestone Shareholder, your principal options are to:</p> <ul style="list-style-type: none"> • vote in favour of the New Strategy at the Meeting by voting in favour of all Resolutions tabled at the Meeting. This is the course of action unanimously recommended by the Folkestone Board in the absence of a superior offer; • vote against the New Strategy at the Meeting by voting against all or any of the Resolutions tabled at the Meeting; • sell your Folkestone Shares; or • do nothing. 	

2. FREQUENTLY ASKED QUESTIONS Continued

2.2 VOTING ON THE NEW STRATEGY

Question	Answer	Where can I find further information?
Why might I vote for the New Strategy?	<p>The Folkestone Board unanimously recommends that Shareholders vote in favour of the New Strategy, in the absence of a superior proposal.</p> <p>Possible reasons to vote for the New Strategy include the following:</p> <ul style="list-style-type: none">• in the opinion of the Folkestone Board the New Strategy is superior to alternative options currently available to Folkestone Shareholders;• the New Strategy will be implemented by an experienced senior management team with a strong track record in establishing real estate and funds management businesses and extensive and long-standing relationships in the Australian real estate, financial services and funds management industries;• the New Board, charged with the responsibility of implementing and overseeing the New Strategy is experienced and has an established track record of performance in the Australian market;• it enables Folkestone to pursue a diverse range of Australian real estate assets and take advantage of investment opportunities presented by the recent downturn in real estate and financial markets, providing potential exposure to higher returns;• gives Folkestone an improved financial position and enhanced flexibility in relation to unlocking the inherent value of the Company's existing development projects in a manner and within a timeframe that maximises Shareholder returns;• enables Folkestone to expand its existing business to include a funds management platform; and• Folkestone currently lacks the scale and liquidity to generate enhanced Shareholder returns – the New Strategy will transform the Company and reposition it to enhance Shareholder returns.	Section 1.2

2. FREQUENTLY ASKED QUESTIONS Continued

Question	Answer	Where can I find further information?
<p>Why might I vote against the New Strategy?</p>	<p>Although the Folkestone Board unanimously recommends that you vote in favour of the New Strategy, in the absence of a superior proposal, factors which may lead you to vote against the New Strategy include the following:</p> <ul style="list-style-type: none"> • the New Strategy may result in a higher risk profile for the Company; • the New Strategy is opportunistic and it is not possible to independently assess its projected cash flows; • the Capital Raising may result in a dilution to the interests of existing Folkestone Shareholders; • Greg Paramor intends to act as Executive Chairman which may not be considered best practice from a corporate governance perspective; • the New Board will not comprise any person with more than a one year history of Folkestone's business; • Folkestone will incur fees and costs of approximately 5%-8% of the gross proceeds raised if the Resolutions are approved and the Capital Raising proceeds; • the loss of services of any key personnel, or the inability to attract new qualified personnel, could adversely affect Folkestone's ability to successfully implement the New Strategy; • if appropriate investment opportunities do not arise, Folkestone will not be able to implement the New Strategy effectively; • no assurance can be given that Shareholder returns will be enhanced under the New Strategy; • you may not agree with the view of the Folkestone Board that the New Strategy is superior to the other strategic options available to Folkestone; and • you may consider that there is the potential for a superior proposal to be made. As at the date of this Explanatory Memorandum, no superior proposal has emerged. 	<p>Section 1.3</p>
<p>When and where will the Meeting be held?</p>	<p>The Meeting will be held on 17 February 2011 in the offices of Deloitte, Level 10, 550 Bourke Street, Melbourne VIC 3000 commencing at 10:00am.</p>	<p>Notice of Meeting</p>
<p>Who is entitled to attend and vote at the Meeting?</p>	<p>If you are registered as a Shareholder at close of business on 15 February 2011, you will be entitled to attend the Meeting and to vote on the Resolutions (in person, by proxy, by attorney or, in the case of a body corporate, by a corporate representative), unless otherwise noted in the voting exclusion statement contained in the Notice of Meeting.</p>	<p>Notice of Meeting</p>

2. FREQUENTLY ASKED QUESTIONS Continued

Question	Answer	Where can I find further information?
What are the voting majorities required at the Meeting?	All Resolutions to be tabled at the Meeting will be ordinary resolutions, which may be passed by Shareholders present at the Meeting and entitled to vote, in person or by proxy or attorney, holding 50% or more of the voting rights.	Section 7
Is voting compulsory at the Meeting?	<p>Voting is not compulsory. However, if you do not vote, either in person or by proxy, and the New Strategy is approved and implemented, it will become binding on you even if you did not participate in the Meeting.</p> <p>The Folkestone Board encourages you to read this Explanatory Memorandum and exercise your right to vote. Your vote is important and represents your opportunity to have your say on the New Strategy.</p>	
How do I vote?	<p>You may attend the Meeting and vote in person at the Meeting.</p> <p>If you cannot or do not wish to attend the Meeting, you may appoint a proxy, attorney or representative to vote at the meeting on your behalf.</p> <p>Full details of how these appointments may be made are contained in the notes to the Notice of Meeting. A proxy form for the Meeting is included with the Notice of Meeting.</p> <p>If the New Strategy is approved and implemented, it will become binding on Folkestone even if you did not participate in the Meeting.</p>	Notice of Meeting

2.3 OTHER INFORMATION AND DETAILS OF THE NEW STRATEGY

Are there any conditions that must be satisfied before the New Strategy can be implemented?	<p>The New Strategy is subject to a number of conditions, including Folkestone Shareholder approval. All Resolutions are interdependent (with the exception of Resolution 10), so for the New Strategy to be implemented, all Resolutions other than Resolution 10 must be approved at the Meeting.</p> <p>Further, even if all relevant approvals are obtained at the Meeting, all Resolutions (except the Resolution relating to the Capital Raising itself, Resolution 10 and the Resolutions for the New Board appointments) will only take effect once Folkestone has raised gross proceeds of a minimum of \$20 million capital as part of the Capital Raising.</p> <p>This is to assure Shareholders that those transactions will only take effect if the EREP acquisition occurs and where Folkestone has raised sufficient capital to commence executing the New Strategy in an effective manner.</p>	Section 4
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2. FREQUENTLY ASKED QUESTIONS Continued

Question	Answer	Where can I find further information?
<p>What happens if the New Strategy is not approved?</p>	<p>If the New Strategy is not approved:</p> <ul style="list-style-type: none"> • you will retain your current investment in Folkestone Shares and continue to be exposed to the benefits and risks presently associated with this investment. These risks include general risks of holding shares and risks that are specific to Folkestone’s existing business; and • Folkestone will continue to complete an orderly sell down of existing projects in a manner and within a time frame that will maximise Shareholder returns with a view to winding-up the Company. As outlined in other sections of the Explanatory Memorandum Folkestone’s limited capital base, limited cash reserves and the fact that its investments include joint venture and minority interests will continue to impact this strategy. 	
<p>What happens if Folkestone receives a superior proposal?</p>	<p>The Folkestone Board will carefully consider, and inform you, of any superior proposal that may emerge.</p>	
<p>What is the cost of the New Strategy if it is approved?</p>	<p>If it is approved and implemented, the total cost of implementing the New Strategy will be approximately 5%-8% of the gross proceeds raised, depending on the size of the Capital Raising. These costs are for underwriting, legal, other advisory and miscellaneous expenses.</p>	<p>Section 1.3</p>
<p>How do I obtain further information?</p>	<p>The information in this table is a summary only. Full details of the New Strategy are set out in the remainder of this Explanatory Memorandum. Please read it carefully.</p> <p>If you have any questions about the New Strategy, please contact Folkestone on 03 9543 2544, Monday to Friday between 8.30 am and 5.30 pm (AEST).</p> <p>The Folkestone Board recommends that you consult your professional adviser concerning the impact your decision may have on your own circumstances.</p>	

3. INFORMATION ABOUT FOLKESTONE

3.1 FOLKESTONE OVERVIEW

Folkestone is a Melbourne-based property company which listed on the Australian Stock Exchange as an independent company in 2000. Folkestone has primarily focussed on the industrial, commercial and residential property sectors and has an operating history of more than 40 years.

Folkestone's last stated net assets was \$27.0 million as per the Company's audited financial statements as at 30 June 2010 and the Company's market capitalisation was \$12.0 million on 5 January 2011. As at the date of this Explanatory Memorandum, there are 99,699,228 million shares on issue.

Folkestone retains a current development book of three projects situated in Victoria with a gross book value of \$42.2 million as at 30 June 2010 (Folkestone's share). All three projects are being undertaken in joint venture with the AMP Capital Investors' managed Select Property Portfolio Number 2 Fund.

3.2 FOLKESTONE'S FINANCIAL POSITION AND STATUS OF DEVELOPMENT PROJECTS

Folkestone's financial position as per the 30 June 2010 audited financial statements is outlined in the table below.

Project	Location	Sector	Ownership	Book value (\$m)	Debt (\$m)	Net book value (\$m)
Noone Street	Clifton Hill, VIC	Residential	50%	12.9	(5.3)	7.6
Millers Road	Altona, VIC	Bulky goods	50%	8.2	(4.5)	3.7
Donnybrook Road	Mickleham, VIC	Industrial	20%	21.1	(17.9)	3.2
Cash/net Working Capital				12.5	-	12.5
Total				54.7	(27.7)	27.0

^ Values in table represent Folkestone's ownership interests and are as at 30 June 2010.

Since 30 June 2010, the following material subsequent events have occurred which have an impact on Folkestone's financial position:

- Settlement of the Donnybrook Road Mickleham project took place on 21 December 2010. Folkestone's equity contribution towards settlement was approximately \$9.1m which was paid out of Folkestone's cash reserves. Settlement has also had the effect of reducing Folkestone's share of debt for this project from \$17.9m to \$8.7m.
- Folkestone's share of the senior debt facility in respect of the Millers Road Altona project has been reduced from \$4.5m to \$4.1m. This reduction was funded via an equity contribution by Folkestone which was paid out of Folkestone's cash reserves.

It is currently intended that the Half Year Report will be released to the ASX prior to date of the Meeting. As part of the preparation of the Half Year Report and consistent with usual practice, Folkestone will be undertaking a review of the carrying value of its interests in the three current development projects and external valuations will be sought where appropriate.

When the Half Year Report is released, Shareholders are encouraged to read it to assist in their decision whether to vote in favour of the Resolutions.

Noone Street, Clifton Hill

Noone Street is a 103 residential dwelling project comprising 58 townhouses and 45 apartments located 3.1 kilometres northeast of the Melbourne CBD. Pre-sales totalling \$53.4m have been signed to date representing over 95% of the total project revenue. The development is being completed on a staged basis with two of the seven stages, together with the sale of a super-lot, having been completed and settled. Construction activity on the remaining five stages is underway and is on schedule to be completed in the second half of the 2011 calendar year. The debt facility associated with this project was refinanced during the 2010 financial year and now matures in December 2011.

3. INFORMATION ABOUT FOLKESTONE Continued

Millers Road, Altona

Millers Road is a 13 hectare parcel of land with an industrial 3 zoning and a permit to develop a 36,693sqm bulky goods retail complex. The site is located approximately 11 kilometres from the Melbourne CBD and 2.5 kilometres from the Westgate Freeway and Western Ring Road.

Following the global financial crisis, the site was put to the market in November 2009 via an expression of interest campaign however no buyer was secured. Since this time, the joint venture has continued to field enquiries for the property, however no sale has been concluded.

The proposed tenants for the bulky goods complex remain interested in the site and market conditions are slowly improving.

The debt facility was recently extended to 30 November 2011.

Donnybrook Road, Mickleham

Donnybrook Road is a 320 hectare site, zoned for business use and located within the Urban Growth Boundary of Victoria. The site enjoys excellent links to Melbourne's road transport infrastructure in particular the Hume Highway and Craigieburn bypass.

The final land payment to the vendor was made on 21 December 2010. The joint venture is currently undertaking works to bring infrastructure services to the site to ensure the site is able to capitalise on any demand for employment land in the northern growth corridor.

The debt facility expires in December 2011.

3.3 CHALLENGES FACING FOLKESTONE

In August 2009, Folkestone announced that it would pursue an orderly sell down of existing projects in a manner and within a timeframe that would maximise Shareholder returns. The stated timeframe for completing the orderly sell down of existing projects was December 2011.

The Noone Street residential project remains on track to be completed by this date, however the ability of Folkestone to achieve this timeframe for the Millers Road and Donnybrook Road projects in a manner that will maximise Shareholders returns continues to be impacted by the subdued state of the bulky goods and industrial property markets.

The current market conditions together with Folkestone's limited capital base, limited cash reserves, the fact that its investments include joint venture and minority interests, and lack of scale and liquidity, will continue to impact Folkestone's ability to deliver earnings growth and Share price performance in the future.

3.4 THE NEW STRATEGY

As a result of the difficulties outlined above, Folkestone has considered several alternative strategies to enhance Shareholder returns.

The Folkestone Board is currently focused on transforming Folkestone into a larger listed real estate company, as it believes that demand exists within the listed investment market for a mid-scale, lowly geared, diversified real estate company that is attractive to institutional and retail investors and provides Shareholders with attractive risk-adjusted returns.

3.5 ALTERNATIVE STRATEGIES CONSIDERED

In order to pursue the transformation of Folkestone into a larger, more diversified listed real estate company, Folkestone has been active in identifying and assessing a range of market opportunities which have the ability to enhance Shareholder value in the context of current market conditions, whilst continuing to manage Folkestone's existing projects with a view to undertaking an orderly sell down of these projects.

The New Strategy was superior to any other opportunity assessed by the Folkestone Board.

In coming to this determination, the Folkestone Board has assessed the New Strategy against the alternative of completing an orderly sell down of existing projects leading to a winding-up of Folkestone.

Current property market conditions together with Folkestone's limited capital base, limited cash reserves and the fact that its investments include joint venture and minority interests continue to adversely impact the ability of Folkestone to complete the realisation of existing projects in a manner and within a timeframe that will maximise Shareholder returns.

4. THE NEW STRATEGY

This section 4 has been prepared by EREP.

4.1 INTRODUCTION TO THE NEW STRATEGY

If the Resolutions are approved by Shareholders at the Meeting the New Board will be appointed immediately from the end of the Meeting to carry out the Capital Raising and implement the New Strategy. Under the New Strategy it is proposed that Folkestone will focus on value-add, opportunistic, real estate investment, development and funds management.

4.2 RATIONALE FOR THE NEW STRATEGY

Upon successful implementation of the New Strategy, it is intended Folkestone will be repositioned as a mid-scale, lowly geared diversified real estate company. The New Strategy is aimed at providing Folkestone with a tangible path to generate enhanced Shareholder returns for the following reasons:

- the Capital Raising will generate a significant increase in Folkestone's capital base providing stability to the Company's existing developments and enhancing its ability to proactively pursue opportunistic real estate investments;
- retention and alignment of a senior management team, led by Greg Paramor, who have extensive experience in the real estate, funds management and financial services industries with a strong track record of performance;
- an enhanced ability to capitalise on the unique investment opportunities that exist in the Australian real estate sector as a result of the recent dislocation in real estate and financial markets; and
- the expansion of Folkestone's existing business to include a funds management platform which is expected to provide additional revenue streams and access to external sources of capital.

Under the New Strategy it is proposed that Folkestone will target an after-tax return on equity of 15.0% per annum on a rolling three year basis once the proceeds from the Capital Raising are fully deployed. It is currently considered unlikely that Folkestone will pay any dividends for a period of at least three years with any excess capital generated to be re-invested into future investment opportunities and the funds management platform.

4.3 ACQUISITION OF EREP

As part of the New Strategy, Folkestone will acquire EREP pursuant to a Share Sale Agreement between Folkestone

and the EREP shareholders entered into on 10 January 2011. The Share Sale Agreement is subject to a number of conditions to completion, including Shareholder approval at the Meeting and raising gross proceeds of at least \$20 million of new capital under the Capital Raising.

Pursuant to the Share Sale Agreement, as consideration for the acquisition of the entire share capital of EREP, it is intended that Folkestone will pay an aggregate consideration of \$1.0 million through the issue of 10 million Folkestone Shares.

A summary of the Share Sale Agreement is set out in section 8.3 of this Explanatory Memorandum.

EREP is a specialist real estate funds manager and adviser, founded in 2009 by Greg Paramor, Jonathan Sweeney and Adrian Harrington. EREP was established to manage funds, partnership investments and mandates on behalf of private clients, high net worth individuals and select institutional investors. EREP provides its clients with the accumulated knowledge and expertise of more than 60 years investing and overseeing more than \$20 billion of assets.

Equity Real Estate Funds Management, a subsidiary of EREP, received an Australian Financial Services Licence No. 340990 on 2 December 2009. The license permits it to carry on a financial services business to provide certain general financial product advice, deal in certain financial products and provide certain custodial and depository services to wholesale and retail clients.

To date EREP has established two development funds – the EREP Tivoli Development Fund (“Tivoli Fund”) and the EREP Quakers Hill Development Fund (“Quakers Hill Fund”) with its subsidiary Equity Real Estate Funds Management as the trustee of those funds on terms where it receives certain fees. The Tivoli Fund is developing a 62 apartment development in West Melbourne in joint venture with a leading Melbourne residential developer. The Quakers Hill Fund acquired an interest in a residential development site in Quakers Hill, north-west Sydney, in joint venture with a leading Sydney residential developer. The interest in the development has been sold resulting in an equity IRR of 25%.

EREP has accumulated losses of approximately \$1 million as of 13 December 2010 (unaudited) which primarily represents its net operating costs since founding in 2009 and for Australian taxation purposes these accumulated losses may be able to be offset against any profits the Folkestone group may make in the future.

4. THE NEW STRATEGY Continued

4.4 APPOINTMENT OF EREP PRINCIPALS AS SENIOR EXECUTIVES OF FOLKESTONE

It is proposed that Greg Paramor, Jonathan Sweeney and Adrian Harrington will be appointed as senior executives of Folkestone in the following roles:

- Greg Paramor: Executive Chairman*
- Jonathan Sweeney: Chief Operating Officer; and
- Adrian Harrington: Head of Funds Management.

*Greg's appointment as Executive Chairman will take effect from the date of successfully raising gross proceeds of \$20 million under the Capital Raising. In the interim it is proposed that he be Non-Executive Chairman.

These three individuals possess extensive experience in, and long-standing relationships throughout, the Australian real estate, financial services and funds management industries with an established track record of performance across real estate investment, development and funds management activities.

Further details on Folkestone's new senior management team including individual biographies are provided in section 5 of this Explanatory Memorandum.

4.5 APPOINTMENT OF A NEW BOARD

It is proposed that immediately after the Meeting if the Resolutions are approved that a new board of Folkestone will be established comprising three Non-Executive Directors and an Executive Director as follows:

- Greg Paramor: Executive Chairman* (existing Non-Executive Director);
- Hugh Gurner: Non-Executive Director (existing Non-Executive Director);
- Garry Sladden: Non-Executive Director; and
- Ross Strang: Non-Executive Director.

*Greg's appointment as Executive Chairman will take effect from the date of successfully raising gross proceeds of \$20 million under the Capital Raising. In the interim it is proposed that he be Non-Executive Chairman.

The New Board will be responsible for the implementation and execution of the New Strategy.

Further details on Folkestone's New Board including individual biographies are provided in section 5.1.2 of this Explanatory Memorandum.

All other existing Board members will resign immediately after the Meeting if the Resolutions are approved.

4.6 IMPLEMENT AN EXECUTIVE INCENTIVE PERFORMANCE RIGHTS PLAN

Folkestone is committed to developing a remuneration strategy which is designed to attract, retain and motivate appropriately qualified and experienced directors and senior executives. Key principles in developing the remuneration structure and levels include the creation of longer term Shareholder value, alignment with Shareholder interests, market competitiveness, recognition of individual performance and experience and divisional and group performance.

Folkestone proposes to implement an employee incentive plan and grant certain incentives to certain Board members and senior executives as outlined below.

Greg Paramor, Jonathan Sweeney and Adrian Harrington will be entitled to a total of up to 30 million Performance Rights exercisable for nil consideration with a deemed value (based on a Share price of \$0.10) representing \$3 million in total split \$1.5 million to Greg Paramor and \$750,000 to each of Jonathan Sweeney and Adrian Harrington. The Performance Rights will vest on the third anniversary of the grant date, subject to the following performance hurdles:

- 50% will vest based on the achievement of a compound annual growth in Total Shareholder Return over the performance period ranging from 10% to 15% per annum on a sliding scale with:
 - the full 50% vesting where Total Shareholder Return is 15% per annum or above;
 - 25% vesting where Total Shareholder Return is 10% per annum; and
 - where Total Shareholder Return is between 10% and 15% per annum, the number of Performance Rights will be calculated on a straight line basis; and
- 50% will vest based on the achievement of a compound annual growth in Folkestone's Net Total Assets per Share over the performance period ranging from 10% to 15% per annum on a sliding scale with:
 - the full 50% vesting where the growth in Net Total Assets per share is 15% per annum or above;
 - 25% vesting where the growth in Net Total Assets per share is 10% per annum; and
 - where the growth in Net Total Assets per share is between 10% and 15% per annum, the number of Performance Rights will be calculated on a straight line basis.

4. THE NEW STRATEGY Continued

The Performance Rights will only be granted following the raising of gross proceeds of a minimum of \$20 million as part of the Capital Raising. To the extent less than \$50 million is raised through the Capital Raising, the Performance Rights will be reduced proportionately (ie. if \$30 million is raised through the Capital Raising, the number of Performance Rights issued to each proposed recipient will be calculated as follows:

Number to be issued = Number proposed to be issued x (30 million / 50 million).

Please refer to sections 8.4 and 8.5 of this Explanatory Memorandum for additional detail on the Performance Rights and their impact on the share capital of Folkestone.

4.7 CAPITAL RAISING

The New Board proposes to undertake a Capital Raising promptly after the Meeting to raise gross proceeds of a minimum of \$20 million and up to a maximum of \$100 million to appropriately recapitalise Folkestone to execute the New Strategy. Pending market conditions at the time of the Capital Raising, it is proposed that the issue price will be at least \$0.08 per Share. The VWAP of Folkestone Shares traded on the ASX for the 30 days to 5 January 2011 was 12.7 cents per Share. A maximum of 1.25 billion Folkestone Shares will be issued pursuant to the Capital Raising.

It is contemplated that the Capital Raising will take place in early 2011. The Capital Raising is anticipated to include a placement to institutions and sophisticated investors and a public offer and a priority/entitlement offer to existing Shareholders under a prospectus. The precise structure of the Capital Raising will be determined by the New Board.

Institutions and sophisticated investors with more than a 5% Shareholding will be given the opportunity to participate in any placement.

Existing Shareholders are to receive a priority entitlement of at least 10% of funds sought to be raised under any public offer (which requires shareholder approval) or in another way that in ASX's opinion is fair in all the circumstances. Folkestone will limit the number of shares it issues to an existing Shareholder under a public offer (which requires shareholder approval) to the higher of 5% of all the shares being offered under the priority entitlement and the number the existing Shareholder would be entitled to under a pro rata issue.

The acquisition of EREP described in section 4.3 above, the employment of the EREP Principals described in

section 4.4 above, the appointment of Greg Paramor as Executive Chairman described in section 4.5 above and the allocation of the employment incentives to the EREP Principals described in section 4.6 above are conditional on raising gross proceeds of at least \$20 million through the Capital Raising. This will ensure that those transactions will only take effect when Folkestone has raised sufficient capital to commence executing the New Strategy. If less than \$50 million of gross proceeds is raised, then any Performance Rights will be reduced proportionately.

Please refer to section 8.2 of this Explanatory Memorandum for additional detail on the Capital Raising.

4.8 NEW INVESTMENT STRATEGY

Under the New Strategy, Folkestone will possess a broad investment mandate that will enable the Company to take advantage of investment opportunities presented by the recent dislocation in real estate and financial markets including:

- acquiring assets from distressed real estate owners and developers on attractive terms;
- partnering with balance sheet constrained developers to provide funding for quality real estate projects;
- acquiring development opportunities for Folkestone's balance sheet or managed funds; and
- investing in preferred equity or mezzanine loans backed by real estate assets.

Folkestone will look to expand EREP's existing real estate funds management platform with funds being offered to private clients, high net worth individuals and select institutional investors across the risk-return spectrum (core, value-add and opportunistic).

Initially, Folkestone's target capital investment allocation will be:

- 70% in balance sheet investments ("Direct Investments"); and
- 30% in indirect investment in Folkestone managed funds.

The mix of capital allocated to Folkestone's investments may vary from time to time in order to take advantage of select investment opportunities that meet strategic and financial return hurdles.

Under the New Strategy, it is proposed that Folkestone will target an after-tax return on equity raised under the Capital Raising of 15.0% per annum over a rolling three year basis once the proceeds from the Capital Raising are fully deployed.

4. THE NEW STRATEGY Continued

Folkestone's new senior management team are highly experienced and expect to use their extensive and long-standing relationships in the Australian real estate industry to source attractive investment opportunities, including off-market opportunities.

4.8.1 Direct Investments

As part of the New Strategy, Folkestone's strategy for Direct Investments will be revised to focus on assets and projects which have the potential for capital growth over a two to three year investment horizon in the value-add and opportunistic space.

As part of the New Strategy, Folkestone will aim to achieve attractive risk-adjusted returns through a disciplined and selective investment screening process that seeks to identify opportunities, conducting thorough due diligence, determine a clear strategy for each asset with a view to adding value during the holding period and exiting the investment at an appropriate time.

Under the New Strategy, Folkestone will possess a broad investment mandate to take advantage of investment opportunities across sectors and investment type including asset repositioning, development, distressed situations and real estate debt.

While Folkestone will retain the flexibility to take advantage of any investment opportunities as they emerge, in the short term Folkestone will target the following areas for investment, which the New Board believes present attractive risk-adjusted returns in the current market:

- identifying medium size investment opportunities in the range of \$5 million to \$50 million that do not meet the minimum investment size for most large institutional investors and yet are considered generally beyond the funding capacity of small local investors;
- developing strategic alliances with successful, competent real estate developers and partnering with management teams with demonstrable track records positioned to take advantage of local market pricing anomalies; and
- providing finance to real estate developers in the form of preferred equity and / or mezzanine debt that capitalises on the significant volume of real estate loans that are to be refinanced over the next few years.

4.8.2 Funds management

Under the New Strategy, it is intended to expand EREP's real estate funds management platform by offering funds to private clients, high net worth individuals and select

institutional investors across the risk-return spectrum (core, value-added and opportunistic).

Once the New Strategy is adopted and the EREP acquisition is completed, Folkestone's business will include a new funds management business, which will aim to:

- generate new investment opportunities for Folkestone and underlying fund investors;
- provide Folkestone with an additional capital source for select developments allowing Folkestone to diversify the use of its own balance sheet capital across a broader range of investments; and
- diversify Folkestone's revenue streams through funds management and other associated fees including asset and development management fees.

Under the New Strategy Folkestone's funds management business will seek to grow by:

- accessing senior management's strong industry contacts to source opportunities to acquire assets for the funds;
- leveraging senior management's extensive distribution network of private clients, high net worth individuals and select institutional investors;
- diversifying fund offerings across the risk-return spectrum to include core, value-add and opportunistic; and
- ensuring Folkestone has a strong alignment of interest with underlying fund investors through predominantly performance-based fee structures and co-investment stakes in opportunistic funds.

Under the New Strategy Folkestone may also look, on a selective basis, to acquire the management rights of other existing funds. Any acquisition will need to meet strategic risk and financial return hurdles and be driven by Folkestone's ability to generate enhanced returns to Shareholders and underlying fund investors.

4.8.3 Borrowing guidelines

Under the New Strategy, it is currently intended that Folkestone will be conservatively geared with a target balance sheet gearing range of 0% to 30% and a target look-through gearing range of 20% to 60%. It is anticipated that gearing will be undertaken in specific special purpose vehicles at the asset / project level with limited or no recourse to Folkestone. Gearing of up to 80% of an individual development may be utilised for the purpose of development financing for approved projects on a non-recourse basis.

5. CHANGES TO FOLKESTONE BOARD AND SENIOR MANAGEMENT

5.1 FOLKESTONE BOARD

The Folkestone Board is currently comprised of five Non-Executive Directors, details of whom are set out in section 5.1.1 below. If the New Strategy is approved, immediately after the Meeting three Non-Executive Directors, Alister Maitland, Michael Parkinson and Kaye Denning, will retire and two new Non-Executive Directors, Garry Sladden and Ross Strang will be appointed to the Folkestone Board, and Greg Paramor will become the Non-Executive Chairman.

With effect from the date of successfully raising gross proceeds of \$20 million under the Capital Raising, Greg Paramor will be appointed Executive Chairman of Folkestone and the Folkestone Board will comprise three Non-Executive Directors and an Executive Chairman. The New Board will be responsible for undertaking the Capital Raising and the implementation and execution of the New Strategy. Details of the New Board are set out in section 5.1.2 below.

5.1.1 Current Board

Alister TL Maitland (BCom, FAICD, FAIM, SF Fin) **Chairman**

Alister was appointed as a Non-Executive Director of Folkestone in 1998 and has held the position of Chairman since January 1999. He is also Chairman of the Remuneration Committee and a member of the Audit and Risk Management Committee. He is a former Executive Director of the ANZ Banking Group Ltd. He is also a Non-Executive Director of Malayan Banking Berhad Malaysia (Maybank).

Michael W Parkinson (CBE, MA, MBA (Stanford), FAICD) **Non-Executive Director**

Michael was appointed as a Non-Executive Director in December 2005 and is the Chairman of the Audit and Risk Management Committee and a member of the Remuneration Committee. Michael is a former non-executive director of IOOF Holdings Ltd and its predecessor, IOOF Ltd, from 1996 to 2005. For the past 20 years, Michael has operated his own corporate advisory business specialising in investment opportunities. Michael is also a director of Singhi Advisors Limited.

Kaye H Denning (AM, BEc, AAPI (Val), AAIB, JP) **Non-Executive Director**

Kaye was appointed as a Non-Executive Director in June 2007 and is a member of the Audit and Risk Management and Remuneration Committees. Kaye has a long history of involvement in the construction and property development industries as CEO of Denning Group and has worked with Stockland Limited and NSW Government Landcom.

Greg J Paramor (FAPI, FAICD, FRICS) **Non-Executive Director**

Greg was appointed as a Non-Executive Director in May 2010. Greg is a founding partner of Equity Real Estate Partners. Greg has been involved in the real estate and funds management industry for more than 35 years, and was the cofounder of Growth Equities Mutual, Paladin Australia and the James Fielding Group. Greg was the CEO of Mirvac between 2004 and 2008. Greg is a past president of the Property Council of Australia and past president of Investment Funds Association, a Fellow of the Australian Property Institute and The Royal Institute of Chartered Surveyors. Greg is a director of a number of not-for-profit organisations, including the Garvan Institute of Medical Research and the National Breast Cancer Foundation. Greg is also a board member of the Sydney Swans and a director of LJ Hooker and Firstfolio Ltd.

Hugh Gurner (BA, FAICD) **Non-Executive Director**

Hugh was appointed as a Non-Executive Director in May 2010. Hugh has extensive experience in the property sector as an analyst and corporate adviser and has held board positions in a number of ASX listed and unlisted companies including executive and non-executive roles as a founding director of listed property funds management and venture capital companies. He is a Fellow of the Australian Institute of Company Directors and holds a Bachelor of Arts degree.

5.1.2 New Board

Greg J Paramor (FAPI, FAICD, FRICS) **Executive Chairman**

Please refer to section 5.1.1 above for Greg's profile.

Hugh Gurner (BA, FAICD) **Non-Executive Director**

Please refer to section 5.1.1 above for Hugh's profile.

5. CHANGES TO FOLKESTONE BOARD AND SENIOR MANAGEMENT Continued

Garry Sladden (B.Bus, FFINSA) **Non-Executive Director**

Garry is a business and strategic adviser who has a diversified business background in the areas of property, private equity, business operations, banking and finance, having held the position of General Manager Operations at Consolidated Press Holdings for six years and more recently (2007) the role of Group Operations Executive for a property investment, development and funds management group. Garry is Chairman of Trafalgar Corporate Group and Ashton Manufacturing Pty Limited, and a non-executive director of Endeavour Healthcare Limited.

Ross Strang (LLB (HONS), MAICD) **Non-Executive Director**

Ross is a consultant to Kemp Strang, a Sydney commercial law firm. Ross is one of Kemp Strang's founders and was a partner in the practice for over 30 years. Ross has extensive experience in commercial property, construction and securities matters on a broad front and is well known in legal, commercial and community circles. He is a non-executive Director of Mirvac Funds Management Limited and Mirvac Wholesale Funds Management Limited, and a member of the Australian Institute of Company Directors. Ross is also a director of the Millers Point Youth and Employment Partnership, which is a not for profit initiative aimed at providing employment and educational opportunities for inner city youth.

5.2 SENIOR MANAGEMENT TEAM

Details of the current Folkestone senior management team are set out in section 5.2.1 below. As part of the New Strategy, it is proposed that Greg Paramor, Jonathan Sweeney and Adrian Harrington will be employed as senior executives of Folkestone and be appointed to support the New Board implement the New Strategy. Details of the new senior management team are set out in section 5.2.2 below.

5.2.1 Current Senior Management Team

Scott Martin (B.Com, CA) **Acting CEO** **Chief Financial Officer & Company Secretary**

Scott joined the company in December 2005. He has had extensive experiences as a chartered accountant in a broad range of accounting and taxation fields, the last eight years of which have been in the property and construction industry.

5.2.2 New Senior Management Team

Greg J Paramor (FAPI, FAICD, FRICS) **Executive Chairman**

Please refer to section 5.1.1 above for Greg's profile.

Jonathan Sweeney (B.Comm, LLB, CFA, MAICD) **Chief Operating Officer**

Jonathan is a founding partner of Equity Real Estate Partners. Jonathan has over 23 years experience in the financial services industry. Firstly in London as a funds manager with Gartmore for 5 years and then in Australia with Armstrong Jones before joining Trust in 1991. He occupied a variety of senior positions at Trust and was Managing Director from May 2000 to December 2008. Jonathan holds a Bachelor of Law and a Bachelor of Commerce from the University of New South Wales, is a Certified Financial Analyst and a member of the Institute of Company Directors. He is a past president of the Trustee Corporation's Association and is a director of the Australian Davis Cup Tennis Foundation, Equities & Freeholds Ltd and BNY Trust Australia. He is also a member of the University of New South Wales School of Business Advisory Council.

Adrian Harrington (B.Sc (Hons), FFINSA) **Head of Funds Management**

Adrian is a founding partner of Equity Real Estate Partners. Adrian has 18 years of experience in the funds management and real estate industries. He was formerly CEO Funds Management, UK & USA for Mirvac. He previously held senior positions at James Fielding Group, Deutsche Asset Management, Paladin Australia and the Property Council of Australia. Adrian is the Non-Executive Chairman of IPD Australia. Adrian is Fellow of the Financial Services Institute of Australasia. Adrian has a Bachelor of Science (Hons) from the University of New South Wales and a Graduate Diploma in Applied Finance and Investment from the Financial Services Institute of Australasia.

Scott Martin (B.Com, CA) **Chief Financial Officer, Company Secretary**

Please refer to section 5.2.1 for Scott's profile.

6. KEY RISKS

A number of risks and uncertainties which are both specific to Folkestone and of a more general nature may affect the future operating and financial performance of the Company and the value of its Shares. If any of the following risks materialise, the Company's business, financial condition and operational results are likely to suffer, the trading price of Folkestone Shares may fall and you may lose all or part of the value of your investment.

6.1 EXISTING RISKS OF FOLKESTONE

The following key risk factors, which are not exhaustive, relate to an investment in Folkestone in its existing form. Neither the Folkestone Board nor the Company make any representation or give any guarantee that Folkestone will achieve its stated objectives, that the forecasts will be met or that other forward looking statements will be realised, in whole or in part. Each of the risks set out below could, if they eventuate, have a material adverse impact on Folkestone's operating performance and profits:

6.1.1 Property risk

The Company's asset values and earnings are subject to property market conditions. Increases in supply or falls in demand in any of the sectors of the property market in which the Company operates can influence the acquisition of sites, the timing and value of the Company's sales and the carrying value of projects and any income producing assets as well as earnings. A downturn in the property markets due to deterioration in the economic climate could result in reduced asset values and earnings, as could a decline in sales. Changes in market conditions for properties, including vacancy rates, incentive levels and rental rates may impact on any proceeds received from the Company's assets.

Property assets are by their nature illiquid investments, therefore it may not be possible for the Company to dispose of its properties in a timely manner. To the extent that the Company has properties for which there may be only a limited number of potential investors, the realisable value of those assets may be less than the full value indicated by the Company's expectation of proceeds in relation to them. The Company expects future growth will be derived from both organic and acquisition sources. The success of any future property acquisitions will depend on a number of factors including the availability of properties, the terms of the acquisition and the financial position of the Company. No assurance can be given that the Company will be able to successfully undertake further property acquisitions.

Market sentiment may be influenced by media commentary and observations by industry analysts which has a significant influence on the confidence of and the propensity of purchasers to buy properties. Perception may have a larger short term influence on project enquiry levels and rates of sale than medium term factors such as the likelihood of oversupply or undersupply in some market segments. Although rates of sale may not have a significant influence on the profitability of individual projects in the medium / long term, a decline in market sentiment which reduces rates of sales could adversely influence the amount of profit that can be brought to account in a particular financial period and can impact on the Company's liquidity.

Property specific factors which might impact on asset values and future earnings include the following:

- Environmental issues, changes to government regulations relating to property, land resumptions and major infrastructure developments;
- Any failure to deliver on or to effectively execute the Company's stated strategy or a failure to redefine the strategy to meet changing market conditions;
- An increase in capitalisation rates considered appropriate by professional valuers in response to changed market conditions;
- Changes in the conditions of town planning consents applicable to Company projects as a consequence of the unpredictable nature of council policies;
- Variances in the cost of development as a consequence of the imposition of levies by state and local government agencies;
- A failure of a significant portion of purchasers to settle on development projects;
- The activities of resident action groups; and
- Land resumptions for roads and major infrastructure, which cannot be adequately offset by the amount of compensation eventually paid.

6.1.2 Development risk

Part of the Company's business is to identify, analyse and invest in development projects which have a number of inherent risks in addition to those associated with property generally including:

- A risk that appropriate planning consents are not obtained or, if obtained, are not properly adhered to;
- A risk that development costs escalate beyond those originally anticipated;

6. KEY RISKS Continued

- A risk of project delays due to factors beyond the control of the Company;
- A risk that any property development manager and / or subcontractor appointed to implement a development project does not perform their role to a satisfactory standard or acts or fails to act in breach of contract;
- A risk that competing property development projects adversely affect the overall return achieved by a property development project undertaken by the Company because they provide competitive alternatives for potential purchasers and potential lessees;
- A risk that the property does not sell;
- A risk that market conditions change during any development; and
- Although some of these risks can be mitigated, it is not possible to remove entirely the risks inherent in development projects.

6.1.3 Funding risk

The property industry is highly capital intensive and the ability of the Company to raise funds on favourable terms for future refinancing, development and acquisitions depends on a number of factors including general economic, political, capital and credit market conditions. Any inability of the Company to raise funds on favourable terms could adversely affect its ability to acquire or develop new properties or refinance its debt.

The Company is exposed to risks relating to the refinancing of existing debt facilities, and the Company may experience some difficulty in refinancing some or all of its debt facilities maturing over the coming years. The terms on which they are refinanced may also be less favourable than at present. The Company has various covenants in relation to its debt facilities. Factors such as falls in asset values and the inability to achieve timely asset sales at prices acceptable to the Company could lead to a breach in debt covenants and in such an event the Company's lenders may require their loans to be repaid immediately. Unfavourable movements in interest rates could lead to increased costs.

6.1.4 Economic, market and general business risk

The Company's operating and financial performance is influenced by a variety of general economic and business conditions, including the level of inflation, interest rates, commodity prices, ability to access funding, oversupply and demand conditions and government fiscal, monetary and regulatory policies. Prolonged deterioration in these

conditions, including an increase in interest rates, an increase in the cost of capital or a decrease in consumer demand, could have a materially adverse impact on the Company's operating and financial performance. This risk is heightened in the current relatively difficult economic environment.

The market price of the Company's Shares is influenced by a number of factors that are common to most listed companies including the Australian and international economic outlook, movements in the general level of prices on stock markets, changes in economic conditions including inflation, changes in government fiscal, monetary and regulatory policies and the demand for listed shares. Higher than expected inflation rates could be expected to increase operating costs and development costs although they may be able to be offset by increased selling prices or rents. Increases in interest rates could have the effect of reducing the availability or increasing the cost of finance for potential purchasers and will also impact on the Company's cost of funds. The Company's Shares may trade at prices that may not fully reflect the Company's underlying net asset value. Shareholders who wish to sell their Shares may be unable to do so at an acceptable price.

The Company is exposed to the same form of general business risk that applies to any entity. This includes, but is not limited to, counterparty performance risk, staff retention risk, occupational health and safety risk, taxation change risk, other regulatory change risk, dispute risk, environmental and contamination risk and insurance coverage risk.

6.1.5 Liquidity risk in relation to Folkestone investments

Folkestone will invest in assets that are not listed on a stock exchange or for which there are only a limited number of potential investors. As a consequence, the realisable value of an asset may be less than its expected value.

6.1.6 Credit and insurance risk

The Company maintains insurance which it believes to be consistent with industry practice and adequate in the circumstances. However, no assurance can be given that the Company will be able to obtain such insurance coverage in the future at reasonable rates or that any coverage it arranges will be adequate. Insurance in relation to the Company's assets may not cover all events or all claims made. Further, appropriate cover for terrorism and other uninsurable risks may not be available, or the cover that is available may not be adequate or commercially viable.

6. KEY RISKS Continued

6.2 ADDITIONAL RISKS UNDER THE NEW STRATEGY

In addition to the risks that Shareholders are currently exposed to by virtue of their investment in Folkestone in its existing form, the following risk factors, which are not exhaustive, relate to an investment in Folkestone if the New Strategy is approved at the Meeting and implemented:

6.2.1 Changing investor demand for real estate investments

The demand for real estate as an asset class changes over time and can be influenced by general economic factors such as interest rates and stock market cycles. The demand for real estate and unlisted property funds to which Folkestone may launch or manage may change as investor preferences for particular sectors and asset classes change and this could adversely impact Folkestone's future earnings potential.

6.2.2 Funds management business

Folkestone will look to expand EREP's existing real estate funds management business. The ability to establish new funds will depend on the availability of suitable assets, capital and other market conditions at the time. The expansion of this business is not guaranteed.

6.2.3 Property finance

Folkestone may provide financing by way of preferred equity or mezzanine loan style investments backed by real estate assets or development projects. To the extent that asset values fall or the development projects do not complete or provide the required returns this may have an adverse impact on the carrying value of these investments along with reduced coupon interest income.

6.2.4 Key personnel risk

The New Strategy will be implemented by the New Board and New Senior Management team, led by a senior management team including Greg Paramor, Jonathan Sweeney and Adrian Harrington. It is anticipated that this will provide Folkestone with an exposure to an extensive network of relationships within the real estate industry and capital markets. The loss of services of any of these key personnel could adversely affect Folkestone's ability to successfully implement the New Strategy.

6.2.5 Executive Chairman

Under the New Strategy Greg Paramor intends to act as Executive Chairman with effect from the date of successfully raising gross proceeds of \$20 million under the Capital Raising. This may not be considered best practice from a corporate governance perspective for an ASX listed company.

6.2.6 Minimal history

The New Board will not comprise any person with more than a one year history of Folkestone's business.

6.2.7 Business strategy risk

The New Strategy depends on the Company's ability to raise sufficient funds through the Capital Raising and requires the ability to deploy the capital raised under the Capital Raising in new investment opportunities. If sufficient funds are not raised, or appropriate opportunities do not arise, Folkestone will not be able to implement the New Strategy and the performance of Folkestone may be materially adversely impacted. As the New Strategy is opportunistic and not definitive it is not possible to independently assess the projected cash flows or discount these cash flows back to present value. There is no guarantee that Shareholder returns will be improved by adoption of the New Strategy.

6.2.8 Integration risk

The New Strategy involves the integration of businesses that have previously operated independently. There is an inherent risk that the integration of a recently acquired business may encounter unexpected challenges or issues. The process of integrating operations could, among other things, divert management's attention, interrupt or lose momentum in the activities of one or more of the businesses and could result in the loss of key personnel. Any of these outcomes could have an adverse effect on Folkestone's business, results of operations or financial condition and performance.

7. APPROVALS REQUIRED

In order to reposition Folkestone and implement the New Strategy, a number of Resolutions must be passed by Shareholders. All Resolutions will be ordinary resolutions, which may be passed by Shareholders present at the Meeting and entitled to vote, in person or by proxy or attorney, holding 50% or more of the voting rights that are cast in favour of the Resolution. These are set out in the Notice of Meeting and are summarised below.

All Resolutions are interdependent (with the exception of Resolution 10). This means that a Resolution (other than Resolution 10) will only be passed if all other Resolutions are also passed. In addition, all Resolutions (other than Resolutions 2, 8, 9 and 10) will only take effect when Folkestone has raised gross proceeds of a minimum of \$20 million in new equity through the Capital Raising. Subject to the minimum Capital Raising of \$20 million (other than in respect of the Resolutions for the New Board appointments), Resolutions 1-9 will proceed if approved, even if Resolution 10 is not approved.

7.1 RESOLUTION 1 – CHANGE OF BUSINESS

Shareholder approval is sought for all purposes under the Corporations Act and the ASX Listing Rules, including for the purposes of ASX Listing Rule 11.1. This is because the acquisition of EREP and the implementation of the New Strategy will result in a significant change to the nature and scale of Folkestone's activities. Refer to section 8.1 for further details.

7.2 RESOLUTION 2 – CAPITAL RAISING

Shareholder approval of the proposed capital raising of up to \$100 million is sought for all purposes under the Corporations Act and the ASX Listing Rules, including for the purposes of ASX Listing Rule 7.1. Refer to section 8.2 for further details.

7.3 RESOLUTION 3 – ISSUE OF FOLKESTONE SHARES TO EREP PRINCIPALS

Shareholder approval of the issue of 10 million Folkestone Shares to trusts associated with the EREP Principals as consideration for the acquisition by Folkestone of EREP is sought for all purposes under the Corporations Act and the ASX Listing Rules, including for the purposes of ASX Listing Rule 10.11. The agreed issue price of the Folkestone Shares under the Share Sale Agreement is \$0.10 per Share.

The ASX has confirmed that Listing Rule 10.1 does not apply to the acquisition on the basis that the aggregate consideration is less than 5% of the equity interest of the Company as at 30 June 2010. Refer to section 8.3 for further details.

7.4 RESOLUTION 4 – EXECUTIVE INCENTIVE PERFORMANCE RIGHTS PLAN

Shareholder approval of the Executive Incentive Performance Rights Plan is sought for all purposes under the Corporations Act and the ASX Listing Rules, including for the purposes of ASX Listing Rules 7.2, Exception 9, so that any Performance Rights granted, and Shares issued upon vesting of such Performance Rights, under the Executive Incentive Performance Rights Plan will be excluded from the calculation of the maximum number of new Shares that can be issued by the Company in any 12 month period (currently 15% of shares previously on issue) for a period of three years from the date of approval.

Refer to section 8.4 for further details.

7.5 RESOLUTION 5 – ISSUE OF PERFORMANCE RIGHTS TO GREG PARAMOR

Shareholder approval for the grant to Mr Greg Paramor of 15 million Performance Rights pursuant to the Executive Incentive Performance Rights Plan, and the subsequent issue of Shares upon vesting of such Performance Rights, is sought for all purposes, including under ASX Listing Rule 10.14, which provides that the acquisition of securities by a Director under an employee incentive scheme requires Shareholder approval and Chapter 2E of the Corporations Act, which provides that the giving of a financial benefit to a related party (which includes a director or an associate of a director) requires Shareholder approval.

Refer to section 8.5 for further details.

7.6 RESOLUTION 6 – ISSUE OF PERFORMANCE RIGHTS TO JONATHAN SWEENEY

Shareholder approval for the grant to Mr Jonathan Sweeney of 7.5 million Performance Rights pursuant to the Executive Incentive Performance Rights Plan, and the subsequent issue of Shares upon vesting of such Performance Rights, is sought for all purposes, including under ASX Listing Rule 10.14, which provides that the

7. APPROVALS REQUIRED Continued

acquisition of securities by an associate of a director under an employee incentive scheme requires Shareholder approval and Chapter 2E of the Corporations Act, which provides that the giving of a financial benefit to a related party (which includes a director or an associate of a director) requires Shareholder approval.

Refer to section 8.5 for further details.

7.7 RESOLUTION 7 – ISSUE OF PERFORMANCE RIGHTS TO ADRIAN HARRINGTON

Shareholder approval for the grant to Mr Adrian Harrington of 7.5 million Performance Rights pursuant to the Executive Incentive Performance Rights Plan, and the subsequent issue of Shares upon vesting of such Performance Rights, is sought for all purposes, including under ASX Listing Rule 10.14, which provides that the acquisition of securities by an associate of a director under an employee incentive scheme requires Shareholder approval and Chapter 2E of the Corporations Act, which provides that the giving of a financial benefit to a related party (which includes a director or an associate of a director) requires Shareholder approval.

Refer to section 8.5 for further details.

7.8 RESOLUTION 8 – APPOINTMENT OF GARRY SLADDEN

Resolution 8 relates to the appointment of Mr Garry Sladden as a new Non-Executive Board member.

The experience, qualification and other information regarding Mr Sladden is set out in section 5.1.2.

Refer to section 8.6 for further details.

7.9 RESOLUTION 9 – APPOINTMENT OF ROSS STRANG

Resolution 9 relates to the appointment of Mr Ross Strang as a new Non-Executive Board member.

The experience, qualification and other information regarding Mr Strang is set out in section 5.1.2.

Refer to section 8.7 for further details.

7.10 RESOLUTION 10 – PARTICIPATION IN PLACEMENT BY GREG PARAMOR

Shareholder approval of the issue of up to 40 million Folkestone Shares to Greg Paramor, or an entity associated with Greg Paramor, pursuant to, and on the same terms as, any placement component of the Capital Raising is sought for all purposes under the Corporations Act and the ASX Listing Rules, including for the purposes of ASX Listing Rule 10.11.

Refer to section 8.8 for further details.

8. ADDITIONAL INFORMATION IN RELATION TO THE RESOLUTIONS

8.1 RESOLUTION 1 – CHANGE OF BUSINESS

The implementation of the New Strategy will effectively transform Folkestone into a mid-size listed real estate investment, development and funds management company with enhanced balance sheet capability as a result of the Company's significant capital raising initiative. Due to the significance of the change in the business of the Company, Shareholders will be asked to approve the acquisition of EREP and the change in the nature and scale of the business of Folkestone.

8.2 RESOLUTION 2 – CAPITAL RAISING

As set out in section 4.7 of this Explanatory Memorandum, Folkestone proposes to undertake a Capital Raising to raise gross proceeds of a minimum of \$20 million and up to a maximum of \$100 million to recapitalise Folkestone to execute the New Strategy. The terms and conditions of the Capital Raising will be as determined by the Board at the time of the Capital Raising. It is contemplated that the Capital Raising will take place in early 2011. The Capital Raising is anticipated to include a placement to institutions and sophisticated investors and a public offer and a priority/entitlement offer to existing Shareholders under a prospectus. The precise structure of the Capital Raising will be determined by the New Board.

Folkestone will allot and issue shares under Resolution 2 no later than three months after the date of the meeting. All Shares issued will be on the same terms and conditions as existing Folkestone Shares.

Institutions and sophisticated investors with more than a 5% Shareholding will be given the opportunity to participate in any placement.

Existing Shareholders are to receive a priority entitlement of at least 10% of funds sought to be raised under a public offer (which requires shareholder approval) or in another way that in ASX's opinion is fair in all the circumstances. Folkestone will limit the number of shares it issues to an existing Shareholder under any public offer (which requires shareholder approval) to the higher of 5% of all the shares being offered under the priority entitlement and the number the existing Shareholder would be entitled to under a pro rata issue.

Any person who votes on this Resolution will not be able to participate in the non-public offer.

8.3 RESOLUTION 3 – ISSUE OF FOLKESTONE SHARES TO EREP PRINCIPALS

8.3.1 EREP acquisition terms

A Share Sale Agreement has been entered into between Folkestone and entities associated with the EREP Principals for the acquisition by Folkestone of EREP, subject to receiving Shareholder approval and Folkestone raising gross proceeds of at least \$20 million under the Capital Raising.

The following is a summary of the material terms of the EREP acquisition.

Share sale

Folkestone will acquire all of the issued share capital in EREP. Through this acquisition, Folkestone will also acquire EREP's wholly owned subsidiaries, namely: Equity Real Estate Funds Management Pty Limited and Equity Real Estate Services Pty Limited.

Consideration

Folkestone will pay to entities associated with the EREP Principals (EREP shareholders) total consideration of \$1 million for EREP. Estimated net liabilities of the EREP group as at the date of completion are anticipated to be approximately \$400,000. The consideration is intended to comprise the issue of 10 million Folkestone Shares to the EREP shareholders at an agreed issue price of \$0.10 per Share. The Shares will be issued to the relevant entity on the date of completion under the Share Sale Agreement, and in any event not more than one month after the date of the Meeting. If completion does not occur within one month of the date of the Meeting, the consideration for the acquisition of EREP will be paid in cash, provided that the EREP shareholders enter into appropriate documentation with Folkestone whereby they agree to use the \$1 million to subscribe for Folkestone Shares at \$0.10 per share, unless the board considers on balance that it would be not be in the best interests of the Company and Shareholders to do so, subject to any requisite subsequent Shareholder approval which may be necessary.

The Shares issued to the EREP shareholders will be on the same terms as all other Folkestone Shares.

8. ADDITIONAL INFORMATION IN RELATION TO THE RESOLUTIONS Continued

Vendors and guarantors

The EREP shareholders are entities which are controlled by the EREP Principals. Each EREP Principal has guaranteed the obligations of its respective shareholder entity.

Conditions precedent

There are a number of conditions precedent which must be satisfied prior to completion of the EREP acquisition, including:

- (a) Shareholder approval being obtained;
- (b) the Capital Raising successfully raising \$20 million; and
- (c) entry by the EREP Principals into the Employment Agreements.

Period prior to completion of the EREP acquisition

During the period prior to completion of the EREP acquisition, the business of EREP must be conducted in the ordinary and usual course consistent with usual business practices.

Warranties

Warranties of a standard nature have been provided to Folkestone in respect of the following matters concerning EREP:

- (a) capacity of the EREP shareholders to sell and their solvency;
- (b) ownership and no encumbrance of the EREP shares;
- (c) incorporation status of EREP and its historical compliance with law;
- (d) completeness of EREP records and disclosure materials;
- (e) EREP personnel; and
- (f) liabilities (including as to taxation and litigation) of EREP.

A warranty claim must be made within nine months of completion of the EREP acquisition and the maximum amount recoverable under the warranty claim by Folkestone is the consideration paid.

Termination

Folkestone may terminate the Share Sale Agreement prior to completion for agreed matters, including if it becomes aware of a warranty claim of an amount not less than \$250,000 which has not been remedied by the vendors within 20 business days of receipt of notice of the matter.

The vendors may terminate prior to completion for agreed matters, including if Folkestone becomes insolvent, if a change of control event occurs in respect of Folkestone, if a material adverse event occurs, or if the directors of Folkestone do not recommend the EREP acquisition to Shareholders for approval.

Either party may terminate if any condition precedent remains unsatisfied as at the earlier of 30 June 2011 and the date that is three months after the date of the Meeting or has become incapable of being satisfied (and is not waived) or if the other party fails to complete the EREP acquisition within five business days of receiving a notice to complete.

At completion, as consideration for the acquisition of EREP, Folkestone has agreed to issue the following shares to the following entities:

- 2.5 million shares will be issued to Adkar Investments Pty Ltd as trustee for the Harrington Family Trust. Approval is required in relation to the issue of these shares as Adrian Harrington is a beneficiary of the trust and is also a director of EREP and a proposed new member of the senior management team of Folkestone;
- 2.5 million shares will be issued to Serrano Investments Pty Ltd as trustee for the ES and JS Family Trust. Approval is required in relation to the issue of these shares as Jonathan Sweeney is a beneficiary of the trust and is also a director of EREP and a proposed new member of the senior management team of Folkestone; and
- 5 million shares will be issued to Para-ERE Holdings Pty Ltd as trustee for the Para EREP Trust. Approval is required in relation to the issue of these shares as Greg Paramor is a beneficiary of the trust and is also a director of EREP and a director of Folkestone.

The agreed issue price of the shares is \$0.10.

If Shareholder approval is given, approval is not separately required under Listing Rule 7.1.

8. ADDITIONAL INFORMATION IN RELATION TO THE RESOLUTIONS Continued

8.4 RESOLUTION 4 – EXECUTIVE INCENTIVE PERFORMANCE RIGHTS PLAN

Folkestone is committed to developing a remuneration strategy which is designed to attract, retain and motivate appropriately qualified and experienced directors and senior executives. Key principles in developing the remuneration structure and levels include the creation of longer term Shareholder value, alignment with Shareholder interests, market competitiveness, recognition of individual performance and experience and divisional and group performance.

Subject to Shareholder approval, Folkestone proposes to establish a new long term incentive plan to be known as the Executive Incentive Performance Rights Plan (“Plan”). The Plan is designed to:

- assist with the attraction and retention of directors, executives, senior managers and employees;
- continue to motivate and drive performance at both the individual and corporate level; and
- strengthen the alignment between employee and Shareholder interests.

A summary of the Plan Rules is set out below.

In the future, it is proposed that grants of Performance Rights will be made annually, following announcement of Folkestone’s full-year audited results. Subject to any requisite Shareholder approval, the Board will have discretion to make grants at other times including on the commencement of employment by a person deemed by the Board to be eligible to participate in the Plan. Whilst the Plan Rules provide the Board with flexibility in the design of the annual offer, the Board currently intends to make future offers on terms substantially consistent with the terms of the offer proposed for the current financial year. As this is a new Plan, no Performance Rights have been issued under it.

Summary of the Plan Rules

Eligibility

Eligibility is restricted to those employees who the Board determines in its discretion are eligible and should be invited to participate in the Plan. Employees are defined in the Plan as a person who is in the full or part time employment of Folkestone or its subsidiaries (including directors).

Securities offered under the Plan

Employees selected for participation in the Plan will be offered Performance Rights.

A Performance Right is the right to receive a Share. On the vesting date, if the performance hurdles and tenure conditions are satisfied in respect of a Performance Right, the Performance Right immediately vests and Folkestone must procure the issue or transfer of a Share either directly to the participant or their nominee. In either case, the Share will be subject to disposal conditions if in the relevant terms of any offer it is specified that such conditions will apply.

No monetary consideration will be payable by an employee for an award of Performance Rights, nor will any amount be payable by the holder in connection with the vesting of a Performance Right.

Performance Rights will not be quoted on the ASX or another financial market and will be subject to restrictions on transfer and hedging. Shares delivered on the vesting of Performance Rights will rank equally with those traded on the ASX at the time of issue.

Performance Rights will not entitle the holder to receive any dividends from Folkestone or exercise any voting rights in respect of Folkestone.

Offers of Performance Rights

From time to time Folkestone may invite eligible employees to apply for Performance Rights. Each invitation may set out, among other things:

- the number of Performance Rights the employee may apply for;
- the amount payable (if any) for the grant of the Performance Right or how it is calculated;
- any performance hurdles (see below) attaching to the Performance Rights and the applicable vesting date or vesting dates (“Vesting Date”);
- the circumstances in which accelerated vesting or lapsing of Performance Rights will occur;
- the date on which the Performance Rights will lapse which is 3 years from issue (“Expiry Date”); and
- the restriction period (if any) in which the participant may not transfer or dispose of a Share received on the vesting of a Performance Right.

8. ADDITIONAL INFORMATION IN RELATION TO THE RESOLUTIONS Continued

Performance hurdles

Performance Rights will not vest and the holders of Performance Rights will not be entitled to Shares, unless the performance hurdles associated with those Performance Rights are satisfied or waived. The Board will determine the applicable performance hurdles prior to Performance Rights being granted. The hurdles may reflect Folkestone's business plans, targets, budgets and performance objectives.

Early vesting of Performance Rights

Performance Rights may vest or lapse earlier than the Vesting Date in certain circumstances. Where a participant ceases employment with Folkestone prior to the Expiry Date, the Performance Rights will normally lapse. However, the Board has the discretion to vest part or all of a participant's Performance Rights, including where:

- the participant's employment ceases due to death, retirement, total and permanent disablement or redundancy; or
- an event occurs in respect of Folkestone such as a change of control, receipt of a takeover bid, a court ordering the holding of a meeting in relation to a compromise or arrangement, a voluntary or compulsory winding up or Shares ceasing to be quoted on any exchange.

The Board also has the discretion to determine that a participant who dies or becomes totally and permanently disabled may retain their Performance Rights as though they remained an employee.

Early lapse of Performance Rights

Performance Rights, that have not vested, lapse on the earlier of:

- the Expiry Date specified in the invitation for the Performance Rights;
- the Board determining that a participant's Performance Rights should lapse where it is of the opinion the participant has committed an act of fraud, dishonesty or wilful misconduct or is convicted of a criminal offence which may injure Folkestone's reputation or the participant leaves Folkestone and is not a good leaver (or is otherwise a bad leaver);
- the participant becoming bankrupt; or
- the participant ceasing to be an employee and the Board not making a determination that the Performance Rights vest or that the employee is to

be treated as remaining employed for the purposes of assessing the vesting of the Performance Rights.

Dealing with Performance Rights and Shares

Participants may not sell, assign, transfer or otherwise deal with, or grant a security interest over, their Performance Rights. Performance Rights lapse immediately on any purported sale, assignment, transfer, dealing or grant of security interest unless the Board in its absolute discretion approves the dealing or transfer or transmission is effected by force of law on death or legal incapacity to the participant's legal representative. Participants are prohibited from entering into any arrangement to hedge or otherwise affect their economic exposure to their performance rights.

In addition, the Board may determine that participants will not be able to dispose or otherwise deal with the Shares they or their nominees receive on the vesting of Performance Rights until a set disposal restriction ends. The terms of any disposal restrictions are to be set by the Board and specified in a participant's invitation.

New issues and reorganisations of capital

In the event of any capital reorganisation by Folkestone (including bonus issues), the participant's Performance Rights, and the Shares allocated to the participant on vesting of the Performance Rights will be treated or adjusted, as set out in the Plan Rules. In general, it is intended that the participant will not receive any advantage or disadvantage from such an adjustment not received by holders of Shares.

Change of Plan Rules

The Board has reserved rights to change the rules of the Plan. Amendments may have retrospective effect, and may be made to conform the Plan to taxation or accounting requirements. In certain cases the consent of participants in the Plan may be required before an amendment can be made.

Vesting of Performance Rights

On the vesting of Performance Rights, Folkestone will arrange for Shares to be either issued or transferred directly to the participants (or their nominee). Each Performance Right will convey a right to one Share subject to adjustment in accordance with the Plan Rules (e.g. following a bonus issue). As this is a new Plan, no Performance Rights have been issued under it.

8. ADDITIONAL INFORMATION IN RELATION TO THE RESOLUTIONS Continued

8.5 RESOLUTIONS 5 TO 7 – ISSUE OF PERFORMANCE RIGHTS TO DIRECTORS AND EXECUTIVE MANAGEMENT

The key employment terms of the EREP Principals are as follows.

	Greg Paramor	Adrian Harrington	Jonathan Sweeney
Position	*Executive Chairman	Head of Funds Management	Chief Operating Officer
Location	Sydney	Sydney	Sydney
Remuneration	\$300,000	\$300,000	\$300,000
Performance Rights	**15 million Performance Rights allowing the holder to acquire 15 million Folkestone Shares	**7.5 million Performance Rights allowing the holder to acquire 7.5 million Folkestone Shares	**7.5 million Performance Rights allowing the holder to acquire 7.5 million Folkestone Shares
Hurdles for vesting of Performance Rights	<p>The Performance Rights will vest on the third anniversary of the grant date and vesting will be subject to the following performance hurdles:</p> <p>50% will vest based on the achievement of compound annual growth in Total Shareholder Return over the performance period ranging from 10% - 15% per annum on a sliding scale with:</p> <ul style="list-style-type: none"> the full 50% vesting where Total Shareholder Return is 15% per annum or above; 25% vesting where Total Shareholder Return is 10% per annum; and where Total Shareholder Return is between 10% and 15% per annum, the number of Performance Rights will be calculated on a straight line basis ; and <p>50% will vest based on the achievement of compound annual growth in Folkestone's Net Total Assets per share over the performance period ranging from 10% - 15% per annum on a sliding scale with:</p> <ul style="list-style-type: none"> the full 50% vesting where the growth in Net Total Assets per share is 15% per annum or above; 25% vesting where the growth in Net Total Assets per share is 10% per annum; and where the growth in Net Total Assets per share is between 10% and 15% per annum, the number of Performance Rights will be calculated on a straight line basis. 		

* With effect from the date of successfully raising gross proceeds of \$20 million under the Capital Raising, Greg Paramor will hold the position of Executive Chairman. From the date of the Meeting, if the Resolutions are approved, Greg Paramor will become Non-Executive Chairman.

** The Performance Rights are exercisable for nil consideration with a deemed value (based on a Share price of \$0.10) representing \$3 million in total, split \$1.5 million to Greg Paramor and \$750,000 to each of Jonathan Sweeney and Adrian Harrington

An independent remuneration consultant was engaged by the board to review the proposed remuneration structure. Taking into consideration the consultant's analysis, the Folkestone Board believes that the overall package proposed for the executives is one that is necessary in order to engage the team to implement the New Strategy.

As this is a new Plan, no Performance Rights have been issued under it. No Performance Rights will be issued as a consequence of Shareholder approval later than 12 months after the date of the Meeting.

8. ADDITIONAL INFORMATION IN RELATION TO THE RESOLUTIONS Continued

Each Employment Agreement provides that:

- the EREP Principals will commence employment once Folkestone has successfully raised gross proceeds of at least \$20 million under the capital raising;
- Folkestone may terminate employment at any time on 12 months notice;
- the EREP Principals may terminate employment at any time on 6 months notice; and
- the EREP Principals must not solicit Folkestone employees or compete within a defined restraint area for the period of 6 months following termination of employment.

8.6 RESOLUTION 8 – APPOINTMENT OF GARRY SLADDEN AS A DIRECTOR

Garry is a business and strategic adviser who has a diversified business background in the areas of property, private equity, business operations, banking and finance, having held the position of General Manager Operations at Consolidated Press Holdings for six years and more recently (2007) the role of Group Operations Executive for a property investment, development and funds management group. Garry is Chairman of Trafalgar Corporate Group and Ashton Manufacturing Pty Limited, and a non-executive director of Endeavour Healthcare Limited.

8.7 RESOLUTION 9 – APPOINTMENT OF ROSS STRANG AS A DIRECTOR

Ross is a consultant to Kemp Strang, a Sydney commercial law firm. Ross is one of Kemp Strang's founders and was a partner in the practice for over 30 years. Ross has extensive experience in commercial property, construction and securities matters on a board front and is well known in legal and wider circles. He is a non-executive director of Mirvac Funds Management Limited and Mirvac Wholesale Funds Management Limited, and a member of the Australian Institute of Company Directors.

8.8 RESOLUTION 10 – PARTICIPATION IN PLACEMENT BY GREG PARAMOR

As set out in sections 4.7 and 8.2 of this Explanatory Memorandum, it is currently proposed that the first component of the Capital Raising will comprise a placement to institutions and sophisticated investors.

Subject to Shareholder approval, Greg Paramor (or an entity associated with Greg Paramor) currently intends to participate in any placement component of the Capital Raising by subscribing up to a maximum of 40 million Folkestone Shares. Such Folkestone Shares will be issued on the same terms as all other Folkestone Shares at an issue price of not less than 8 cents per share. The Folkestone Shares will be issued within one month of the date of the Resolutions being approved.

9. GLOSSARY

Definitions

In this Explanatory Memorandum, unless the context otherwise requires:

Term	Meaning
ABN	Australian Business Number.
AEST	Australian Eastern Standard Time.
ASIC	The Australian Securities and Investments Commission.
ASX	ASX Limited (ABN 98 008 624 691) or, as the context requires, the financial market known as the Australian Securities Exchange operated by it.
ASX Listing Rules	The official listing rules of the ASX.
Board	The Board of Directors of Folkestone Limited.
Capital Raising	The capital raising to be undertaken by Folkestone to raise gross proceeds of a minimum of \$20 million and up to a maximum of \$100 million to recapitalise the Company as set out in this Explanatory Memorandum.
Corporations Act	The Corporations Act 2001 (Cth).
Direct Investments	Real estate related assets held on Folkestone's balance sheet.
Employment Agreement	The employment agreements to be entered into by the EREP Principals whereby they will become employees of Folkestone.
EREP	Equity Real Estate Partners (ABN: 93 138 110 826).
EREP Principals	Greg Paramor, Jonathan Sweeney and Adrian Harrington collectively.
Executive Chairman	The Chairman of the New Board who is a member of Folkestone management.
Executive Director	A director that is a member of Folkestone management.
Executive Incentive Performance Rights Plan or Plan	The Executive Incentive Performance Rights Plan proposed to be implemented as part of the New Strategy as described in section 8.4 of this Explanatory Memorandum.
Expiry Date	Has the meaning set out in section 8.4.
Explanatory Memorandum	This Explanatory Memorandum.
Folkestone or the Company	Folkestone Limited (ABN: 21 004 715 226).
IRR	Internal rate of return – the discount rate that results in a net present value of zero for a series of future cashflows.
Meeting	The general meeting of Shareholders held so Shareholders can consider and, if thought fit, approve the Resolutions which is to be held at 10:00am on 17 February 2011 in the offices of Deloitte, Level 10, 550 Bourke Street, Melbourne VIC 3000, as detailed in the Notice of Meeting.
Net Total Assets	Total assets less liabilities as disclosed in Folkestone's Statement of Financial Position for the appropriate financial year.
New Board	The New Board comprising Greg Paramor, Non-Executive Chairman (Executive Chairman with effect from the date of successfully raising \$20 million under the Capital Raising), Hugh Gurner, Non-Executive Director, Garry Sladden, Non-Executive Director and Ross Strang, Non-Executive Director.
New Strategy	The new business strategy of Folkestone focusing on value-add, opportunistic, real estate investment, development and funds management, which the New Board is proposing to implement.

9. GLOSSARY Continued

Non-Executive Director	A Director of Folkestone that is not a member of Folkestone management.
Notice of Meeting	The Notice of Meeting which this document accompanies.
Performance Rights	A performance right issued pursuant to the Executive Incentive Performance Rights Plan.
Plan Rules	The rules governing the operation of the Executive Incentive Performance Rights Plan.
Registry	Link Market Services Limited.
Resolutions	The Resolutions set out in the Notice of Meeting.
Share or Shares	A Share in Folkestone Limited.
Share Sale Agreement	The share sale agreement between Folkestone and the shareholders of EREP whereby Folkestone is to acquire 100% of EREP's share capital dated 10 January 2011.
Shareholder	The holder of a Share.
Total Shareholder Return	The total return on a Folkestone share to Shareholders comprising the movement in share price plus any dividends paid.
Vesting Date	Has the meaning set out in Section 8.4.
VWAP	The volume weighted average price of the Shares.



By mail:
 Folkestone Limited
 C/- Link Market Services Limited
 Locked Bag A14
 Sydney South NSW 1235 Australia



By fax: +61 2 9287 0309

Folkestone Limited

ABN 21 004 715 226
 (Incorporated in Victoria)



All enquiries to: Telephone: 1300 554 474 **Overseas:** +61 2 8280 7111



X99999999999

SHAREHOLDER VOTING FORM

I/We being a member(s) of Folkestone Limited and entitled to attend and vote hereby appoint:

STEP 1

APPOINT A PROXY

the Chairman
 of the Meeting
 (mark box)

OR if you are **NOT** appointing the Chairman of the Meeting as your proxy, please write the name of the person or body corporate (excluding the registered shareholder) you are appointing as your proxy

or failing the person/body corporate named, or if no person/body corporate is named, the Chairman of the Meeting, as my/our proxy and to vote for me/us on my/our behalf at the General Meeting of the Company to be held at 10:00am on Thursday, 17 February 2011, at Deloitte, Level 10, 550 Bourke Street, Melbourne VIC 3000 and at any adjournment or postponement of the meeting.

Proxies will only be valid and accepted by the Company if they are signed and received no later than 48 hours before the meeting. Please read the voting instructions overleaf before marking any boxes with an **X**

STEP 2

VOTING DIRECTIONS

Resolution 1
 Change of Business

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 6
 Issue of Performance Rights to
 Jonathan Sweeney

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 2
 Capital Raising

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 7
 Issue of Performance Rights to
 Adrian Harrington

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 3
 Issue of Shares to the EREP Vendors

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 8
 Appointment of Garry Sladden as a director

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 4
 Executive Incentive Performance Rights Plan

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 9
 Appointment of Ross Strang as a director

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 5
 Issue of Performance Rights to Greg Paramor

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Resolution 10
 Participation in placement by
 Greg Paramor

For	Against	Abstain*
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

i * If you mark the Abstain box for a particular Item, you are directing your proxy not to vote on your behalf on a show of hands or on a poll and your votes will not be counted in computing the required majority on a poll.

STEP 3

IMPORTANT - VOTING EXCLUSIONS

If the Chairman of the Meeting is appointed as your proxy, or may be appointed by default and you do not wish to direct your proxy how to vote as your proxy in respect of Items 4, 5, 6 and 7 above, please place a mark in this box. By marking this box, you acknowledge that the Chairman of the Meeting may exercise your proxy even if he/she has an interest in the outcome of those Items and that votes cast by him/her for those Items, other than as proxyholder, would be disregarded because of that interest. If you do not mark this box, and you have not directed your proxy how to vote, the Chairman of the Meeting will not cast your votes on Items 4, 5, 6 and 7 and your votes will not be counted in calculating the required majority if a poll is called on any those Items.
 The Chairman of the Meeting intends to vote undirected proxies in favour of Items 4, 5, 6 and 7.

STEP 4

SIGNATURE OF SHAREHOLDERS - THIS MUST BE COMPLETED

Shareholder 1 (Individual)

Sole Director and Sole Company Secretary

Joint Shareholder 2 (Individual)

Director/Company Secretary (Delete one)

Joint Shareholder 3 (Individual)

Director

This form should be signed by the shareholder. If a joint holding, either shareholder may sign. If signed by the shareholder's attorney, the power of attorney must have been previously noted by the registry or a certified copy attached to this form. If executed by a company, the form must be executed in accordance with the company's constitution and the *Corporations Act 2001* (Cth).



HOW TO COMPLETE THIS PROXY FORM

Your Name and Address

This is your name and address as it appears on the company's share register. If this information is incorrect, please make the correction on the form. Shareholders sponsored by a broker should advise their broker of any changes. **Please note: you cannot change ownership of your shares using this form.**

Appointment of a Proxy

If you wish to appoint the Chairman of the Meeting as your proxy, mark the box in Step 1. If the person you wish to appoint as your proxy is someone other than the Chairman of the Meeting please write the name of that person in Step 1. If you leave this section blank, or your named proxy does not attend the meeting, the Chairman of the Meeting will be your proxy. A proxy need not be a shareholder of the company. A proxy may be an individual or a body corporate.

Votes on Items of Business - Proxy Appointment

You may direct your proxy how to vote by placing a mark in one of the boxes opposite each item of business. All your shares will be voted in accordance with such a direction unless you indicate only a portion of voting rights are to be voted on any item by inserting the percentage or number of shares you wish to vote in the appropriate box or boxes. If you do not mark any of the boxes on the items of business, your proxy may vote as he or she chooses. If you mark more than one box on an item your vote on that item will be invalid.

Appointment of a Second Proxy

You are entitled to appoint up to two persons as proxies to attend the meeting and vote on a poll. If you wish to appoint a second proxy, an additional Proxy Form may be obtained by telephoning the company's share registry or you may copy this form and return them both together.

To appoint a second proxy you must:

- (a) on each of the first Proxy Form and the second Proxy Form state the percentage of your voting rights or number of shares applicable to that form. If the appointments do not specify the percentage or number of votes that each proxy may exercise, each proxy may exercise half your votes. Fractions of votes will be disregarded.
- (b) return both forms together.

Signing Instructions

You must sign this form as follows in the spaces provided:

Individual: where the holding is in one name, the holder must sign.

Joint Holding: where the holding is in more than one name, either shareholder may sign.

Power of Attorney: to sign under Power of Attorney, you must lodge the Power of Attorney with the registry. If you have not previously lodged this document for notation, please attach a certified photocopy of the Power of Attorney to this form when you return it.

Companies: where the company has a Sole Director who is also the Sole Company Secretary, this form must be signed by that person. If the company (pursuant to section 204A of the *Corporations Act 2001*) does not have a Company Secretary, a Sole Director can also sign alone. Otherwise this form must be signed by a Director jointly with either another Director or a Company Secretary. Please indicate the office held by signing in the appropriate place.

Corporate Representatives

If a representative of the corporation is to attend the meeting the appropriate "Certificate of Appointment of Corporate Representative" should be produced prior to admission in accordance with the Notice of Meeting. A form of the certificate may be obtained from the company's share registry.

Lodgement of a Proxy Form

This Proxy Form (and any Power of Attorney under which it is signed) must be received at an address given below by 10:00am on Tuesday, 15 February 2011, being not later than 48 hours before the commencement of the meeting. Any Proxy Form received after that time will not be valid for the scheduled meeting.

Proxy Forms may be lodged using the reply paid envelope or:



ONLINE

www.linkmarketservices.com.au

Select the 'Proxy Voting' option on the top right of the home page. Choose the company you wish to lodge your vote for from the drop down menu, enter your holding details as shown on this form, and follow the prompts to lodge your vote. To use the online lodgement facility, shareholders will need their "Holder Identifier" (Securityholder Reference Number (SRN) or Holder Identification Number (HIN) as shown on the front of the proxy form).



by mail:

Folkestone Limited
C/- Link Market Services Limited
Locked Bag A14
Sydney South NSW 1235
Australia



by fax:

+61 2 9287 0309



by hand:

delivering it to Link Market Services Limited, Level 12, 680 George Street, Sydney NSW 2000.

If you would like to attend and vote at the General Meeting, please bring this form with you.
This will assist in registering your attendance.