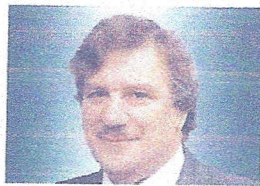


Control of Folkestone could change without offer to all shareholders

BRYAN FRITH



A SYDNEY versus Melbourne contest appears to have developed over control of the small property developer Folkestone.

Folkestone at present is based in Melbourne but if a proposal put forward by well-known property expert Greg Paramor is approved, control of the company will shift to Sydney.

Paramor has been involved in the real estate and funds management industry for more than 35 years. He was a co-founder of Growth Equities Mutual, Paladin Australia and the James Fielding Group and is a former CEO of Mirvac.

Until recently the Folkestone board was solidly in favour of the Equity Real Estate Partners proposal, which involves Folkestone acquiring EREP, a real estate investment management company owned by Paramor, Jonathan Sweeney and Adrian Harrington; replacing the existing board with a new board and installing EREP to manage the company; and undertaking a capital raising to raise between \$20 million and \$100m.

Such a proposal was mooted last April when Folkestone made a placement to the shareholders of EREP, which gave Paramor and his associates a 6.43 per cent shareholding in the company, and Paramor and Hugh Gurner joined the board.

Ironically that has worked against Paramor.

The proposal was finally formalised last month and, because Paramor is on the board, he and his associates cannot vote their shareholding under the ASX listing rules.

Last month, the board suddenly switched its support to a rival proposal said to be by the sharebroker Bell Potter, but the driving forces behind it appear to be the Melbourne identities Alex Waislitz, the son-in-law of the late Richard Pratt, who heads the family business Thorney Holdings, and Bill Bowness, a property developer and director of Centro Retail Trust.

Thorney owns 10 per cent of Folkestone, while Bowness's Wilbow Pty owns just on 11 per cent, giving an aggregate of 21 per cent of the capital.

EREP's proposed capital raising would involve a placement to institutions and sophisticated investors and a public offer in which existing shareholders would have a priority entitlement which would be pro-rata to their existing holdings and in effect is tantamount to a de facto rights issue.

The EREP proposal would also be structured so that no one party could emerge with control of Folkestone post the capital raising.

The EREP camp nominated a minimum issue price for the capital raising of 8c a share but added it was intended that it would be significantly above that price.

The Bell Potter proposal initially involved an underwritten 2.5-for-one renounceable rights issue at 10c a share to raise \$25m.

Folkestone commissioned KPMG to compare the EREP and Bell Potter proposals but has not disclosed its conclusions. The EREP camp believes the accounting firm did not consider the Bell Potter proposal to be superior to the EREP proposal. The Folkestone board said it considered the Bell Potter proposal to be superior to the EREP proposal.

The shareholders meeting would still proceed to enable the shareholders to decide on the two proposals but was postponed from February 17 to February 22 to give shareholders more time to decide their position.

On Monday, the day before the rescheduled meeting, Folkestone revealed that Bell Potter had revised its underwriting to a two-for-one renounceable issue at 12.5c a share to raise \$25m (same amount, different ratio) and also disclosed that the EREP camp had raised its minimum issue price to 12c a share.

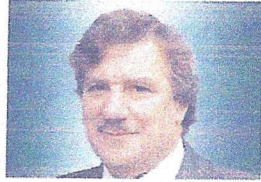
The Folkestone board declared that it had "exercised its business judgment" and determined that the revised Bell Potter proposal was the superior proposition and recommended that shareholders vote against the EREP proposal. At the same time they postponed the shareholders meeting for second time, until March 9, to give shareholders sufficient time to consider the two proposals.

The revised Bell Potter proposal only surfaced after proxies had closed for the February 22 meeting, and the EREP camp believes there were sufficient to have secured approval for their proposal. A delay in the meeting would give Folkestone time to try to persuade shareholders to change their proxy votes.

Folkestone claims that Paramor and Gurner are conflicted, but so are the incumbents as they would lose their board seats under the EREP proposal but retain them under the Bell Potter proposal, which they support.

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Folkestone contends there is uncertainty about the EREP capital raising because it is not underwritten. EREP counters that it has a signed mandate letter from its financial advisers Macquarie Bank, Moelis and BG Capital and a letter of support from Commonwealth Bank but cannot obtain a legally binding underwriting without the commitment of the Folkestone board, which it will only give to the Bell Potter proposal.

The main reason advanced by Folkestone for favouring Bell Potter is that a renounceable issue is fairer to shareholders and will have a much less dilutive impact than the EREP proposal. But EREP's proposed placement is a plus because it would introduce new shareholders and create greater market liquidity, whereas the Bell Potter alternative would maintain the existing concentrated ownership and poor market liquidity.

In fact, it could increase the concentration of ownership. Bowness has undertaken to take up his rights while Thorney has agreed to sub-underwrite \$10m of the Bell Potter issue, which means they could end up with more than 35 per cent of the capital. That smacks of a transaction which could see control of the company change hands without a takeover offer to all shareholders, and which might interest the Takeovers Panel. Moreover, Bowness and Thorney would be able to apply for more than their entitlement, to be satisfied from any shortfall and would also be free to buy the rights on the market.

Folkestone has greeted each increase in the issue price as if it is a takeover offer for the company. In fact, the more the issue price rises towards the market price, the less likely it is that shareholders will take up their entitlement and the greater the shortfall to go to the sub-underwriters. Folkestone's current share price is 13.5c, only 1c above Bell Potter's issue price.

Folkestone last raised capital in late 2009 through a \$9.5m two-for-one renounceable rights issue, underwritten by Patersons to \$8.2m, at 15c a share — a discount of 45 per cent to the then share price of 27c. Yet it raised only \$3.2m — a shortfall of 60 per cent to the underwriting, which had to be picked up by the underwriter and any sub-underwriters.

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