Folkestone
EDUCATION TRUST

ASX ANNOUNCEMENT
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MARCH QUARTER ACTIVITY UPDATE

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Folkestone Investment Management Limited (“FIML”) as Responsible Entity of the Folkestone Education Trust (“FET or Trust”) (ASX:FET) is pleased to provide Unitholders with an update regarding the Trust’s recent activities.

ACQUSITION ACTIVITY

PORTFOLIO PURCHASES

FET has negotiated the purchase of two portfolios, comprising 9 established childcare centres for a total value of $63.16 million. Both transactions are for quality operating centres in Brisbane, operated by Avenues Childcare (“Avenues”). The first transaction for five centres, undertaken in February 2018 was for $30.17 million and has settled. The second transaction, for four centres at a value of $32.99 million is expected to settle in mid-April 2018. Both transactions are immediately accretive to distributable income.

The centres all operate at extremely high occupancy and are located in the Brisbane suburbs of Aspley, Carina, Jindalee, McDowall, Norman Park, Paddington, Parkinson, Shailer Park and Sunnybank and represent quality additions to FET’s portfolio.

The FET/Avenues leases are consistent with our triple net structure and have appropriate security arrangements. The lease terms are for 20 years from settlement with further options thereafter. Indicatively, these transactions increase FET’s WALE, as at 31 December 2017 from 9.2 years to 9.9 years.

The transactions will be funded through a combination of bank debt and proceeds from FET’s ongoing asset recycling program. It is expected that FET’s future gearing level, taking into account both Avenues portfolios, but before adjustment for any disposals or valuation adjustments, will be approximately 32 per cent; well within FET’s gearing policy of between 30 to 40 per cent.

In addition to securing a long term mandate with Avenues for new centres, the benefits of the transactions include bringing a higher specification centre and operator to our Queensland portfolio, as well as a greater locational concentration to Brisbane. With further sales expected in Queensland, the transactions will further accelerate the re-weighting of FET’s Queensland portfolio to metropolitan Brisbane and to sites with significantly stronger childcare and real estate fundamentals.

ABOUT AVENUES

Avenues Childcare operate 16 centres in Brisbane and Melbourne, and have a small development pipeline of centres in Brisbane and Sydney. Established in 2003, Avenues has a distinguished track record in childcare operations, reflected in quality centres, locations, continued high occupancy levels, their financial strength and customer satisfaction levels. The Avenues Childcare offering is considered to be outstanding. FET's due diligence of the business operations indicated exceptionally high performance levels on all indicators. The Avenues childcare model is built around the advancement of quality childcare outcomes through education, quality staffing and development and a range of programs and initiatives beneficial to children and families.

THE OPPORTUNITY

FET has entered into an agreement with Avenues to provide new development opportunities within defined geographical areas that suit FET's objectives as well as Avenues' target catchments and growth aspirations.

The Avenues opportunity is consistent with FET's strategy of partnering only with Australia's best quality operators. This new partnership, which includes a mutual commitment to sourcing new development centres in specific locations, adds to other existing FET partnerships with Australia's best childcare operators. These relationships bring not only opportunity, but innovation and gives FET a significant competitive advantage in a market where quality opportunities remain highly sought after.

As predicted, the operational childcare market is witnessing a flight to quality operators, particularly in inner suburban locations. FET's in-house ability to source, design and develop high demand opportunities is a sought after skill which is valued by operators. The partnerships with groups such as Avenues diversifies and enhances FET's income base and operator register, and ensures it remains at the forefront of intellectual and operational advancements.

Mr Mike Wu, Principal of Avenues Childcare said:

"We are very pleased to be partnering with FET. We both share the view that the childcare sector needs a new model for it to advance service offerings and quality. That includes centres that bring new and exciting initiatives to childcare which lift the educational and social outcomes for children and families but also allows parents to return to paid work. Not only does FET share that vision, but they are the only ones with the foresight to understand its value, as well as having the capability and expertise to make it a reality."

DEVELOPMENT PIPELINE

Since 31 December 2017, FET has continued to expand its development pipeline with a further 6 sites added. This includes three contracted sites of which one has settled and another three under exclusive arrangements. The new transactions are consistent with FET's demographic, population growth, economic activity and land value based strategy, together with FET's "best site, best operator and best lease" policy.

These new developments are expected to add approximately $36.7 million in "upon completion" value to the development pipeline. The expected total "upon completion" value of the development pipeline (29 sites) as at 31 March 2018 is approximately $173 million, over a three year period, after accounting for recent completions at Highett and Northcote (completion value $16.65 million), which are now operating. Five existing development centres, all of which are well progressed, are expected to be completed before 30 June 2018. The development pipeline is expected to require approximately a further $20 million in further funding for FY18.

Examples of new centres, developed by FET and which we believe to be some of, if not Australia's best childcare centres, can be seen through the following 'fly-through' videos:

Highett, Vic

Northcote, Vic

Williams Landing, Vic

MARKET CONDITIONS

FET recalibrated its locational strategy in 2016 to account for potential changes brought on by the Federal Government's Jobs for Families Package. The Package addressed the level of support to parents through an increased subsidy pool, although it also introduced means testing as well as a work/activity test that do not apply under the existing system. This new package has passed through Parliament and will commence on 2 July 2018.

Increased supply of new centres in the last two years has provided choice to parents that had been non-existent for some time. The implementation of the National Quality Framework in 2016 has significantly raised standards and outcomes for children and families. With an increasing participation rate (up 11 per cent in five years to 37 per cent[1]), significant population growth (particularly in Victoria at 2.3 per cent, per annum), and increasing growth in the number of 0-5 year olds (+2.6 per cent, per annum), we expect the new supply, if appropriately located, designed and operated, to be absorbed by current and future demand, as well as demand emanating from a contracting Family Day Care sector.

Childcare is also a labour supply mechanism, and this underpins the Government's support for the sector over and above the educational benefits. Employment statistics show that in the 12 months to January 2018, the Australian economy added 399,500 jobs, an increase of 3.3 per cent per annum against a long term average of 1.90 per cent per annum[2]. This rate of increase is greater than the rate of increase in the total civilian population (aged 15 years and over) of 328,500 persons (or 1.7 per cent)[3] and reflects an increasing participation rate, most likely influenced by the rising cost of living.

The labour participation rate increased by 0.1 percentage points to 65.7 per cent in February 2018, the highest since December 2010. Importantly, the female participation rate increased to a historical high of 60.6 per cent, as opposed to the male participation rate at 71 per cent. In the 25-64 age group, 74 per cent of women were now in the workforce[4].

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[1] Early Childhood and Childcare in Summary, March 2017

[2] Australian Bureau of Statistics, Cat. 6202.0 - Labour Force, Australia, Feb 2018

[3] ibid

[4] Australian Bureau of Statistics, Cat. 6202.0 - Labour Force, Australia, Feb 2018

Government data also indicates that of the 691,000 women not in the workforce who wanted a paid job, 50 per cent were caring for their child, compared with just 12.5 per cent of the 407,000 men in the same situation[5].

The combination of increasing population growth and employment growth, further bolstered by the fact that childcare remains the largest obstacle for women to return to the workforce (noting that more women than men found work in the last twelve months), provides the back-drop against which FET has constructed its growth strategy, with a particular focus on areas with a high proportion of working parents where a deficiency in the number and/or quality of childcare centres exists.

FET's locational strategy and pipeline complements these characteristics, and is reliant on not only the locational and design choices, but the quality of the operator relative to the catchment and quality of existing supply. Understanding what drives the operational market and having the right operator relationships, site sourcing and development ability, as well as recognising the "flight to quality" by parents are significant barriers for many market players. Most have sought the "low picking fruit", typically that part of the market which is predictable and a segment currently characterised by limited opportunity and higher risk.

An example of this differential is one of FET's recent centre completions in Melbourne, which opened in March 2018 and will now only accept wait-listed applications. Other FET centres recently completed are tracking well ahead of the operator's expectations.

DEBT FACILITY

FET is finalising an increase in the facility limit of its bilateral facilities by $30 million to $347 million. The facilities are currently drawn to $295 million, resulting in $52 million remaining undrawn and available to fund the second tranche of the Avenues Portfolio ($33 million plus costs) as well as FET's development pipeline. The increase in the facility is equally shared between Australia and New Zealand Banking Group Limited and Hongkong and Shanghai Banking Corporation Limited, on the same terms as the existing facilities.

After completion of the second portfolio of Avenues centres, FET's gearing is expected to be approximately 32 per cent, well within FET's stated gearing policy range of 30 to 40 per cent. Taking into account FET's ongoing asset recycling program, but excluding movements in valuations, FET's gearing is expected to be less than 30 per cent by 30 June 2018.

PROPERTY PORTFOLIO

Highlights in relation to the property portfolio during the first three months of the calendar year to 31 March 2018 include:

- independent valuations of 13 freehold centres have been completed. These valuations have resulted in a 6.4 per cent (+$1 million) increase in value, compared to the Directors' valuations adopted at 31 December 2017;
- two developments have been completed since 31 December 2017 at Northcote and Highett, Victoria. Final value "upon completion" for these assets was $16.65 million, an increase of 39 per cent over initial development forecasts;

[5] Australian Bureau of Statistics, Cat. 6239.0 – Barriers & Incentives to Labour Force Participation, Australia, Dec 2017

- a small number of centres are being marketed for sale before 30 June 2018, including the Melton Medical Centre, subject to pricing expectations being met;
- the development sites at Deepdene, Victoria and Balmain, NSW which are not proceeding, are expected to be contracted shortly, in addition to the disposals noted above. These assets have a value in-excess of $9 million;
- one market rent review has been completed, achieving an increase of 5.0 per cent over the prior year's rental. Twenty-two market rent reviews remain to be completed for FY18;
- eight lease options have been exercised. For the financial year to date, 22 lease options (100 per cent) have been renewed;
- ten lease options will fall due between now and 30 June 2018; and
- the portfolio remains 100 per cent leased.

DISTRIBUTIONS

With respect to the FY18 distribution forecast, Management confirms its full year guidance of 15.1 cents per unit. The March quarter's distribution of 3.755 cents per unit will be paid to Unitholders on 20 April 2018.

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About Folkestone Education Trust

The Folkestone Education Trust (FET) is a listed real estate investment trust (A-REIT) that invests in early learning properties. FET's website, www.educationtrust.folkestone.com.au provides information on FET, its Manager, announcements, current activities and historical information.

About Folkestone

Folkestone (ASX:FLK) is an ASX listed real estate funds manager and developer providing real estate wealth solutions. Folkestone's funds management platform, with more than $1.5 billion under management, offers listed and unlisted real estate funds to private clients and select institutional investors, while its on balance sheet activities focus on value-add and opportunistic (development) real estate investments. www.folkestone.com.au