

**GLADSTONE PACIFIC NICKEL LIMITED**  
**(ACN 104 261 887)**

**EXPLANATORY MEMORANDUM**

**IMPORTANT NOTICE**

This Explanatory Memorandum contains an explanation of, and information about, the Resolutions to be considered at the 2007 Annual General Meeting of the Company. It is given to the Company's Shareholders to help them determine how to vote on those Resolutions.

Shareholders should read this Explanatory Memorandum in full, because individual sections do not give a comprehensive review of the proposals contemplated in this Explanatory Memorandum. This Explanatory Memorandum forms part of the Notice of Annual General Meeting and should be read with that Notice.

If you are in doubt about what to do in relation to the Resolutions you should consult your financial or other professional adviser.

The Glossary at the end of this Explanatory Memorandum gives the meanings of expressions used in this Explanatory Memorandum where the meaning is not given in the Notice of Annual General Meeting or in the body of this Explanatory Memorandum.

This Explanatory Memorandum is dated 23 October 2007.

1. Item 1 set out in the Notice of Annual General Meeting relates to receipt of the directors' report, financial report and auditor's report for the financial year ending 30 June 2007 and requires no special explanation
2. Item 2 set out in the Notice of Annual General Meeting relates to the election of directors.

Pursuant to the Company's Constitution:

- a director appointed by the Board since the previous AGM; and
- one third of the directors and
- a director if they did not retire at this AGM would at the next AGM, have held office for more than three years

must retire, and may offer themselves for re-election.

Mr James Henderson retires as a non-executive director by rotation in accordance with the Company's Constitution and offers himself for re-election.

Mr Henderson has served on the Board since 17 March 2005 and has played a significant role in the development of the Company's strategies. He has been active in promoting awareness of the Company and the Gladstone Nickel Project and was instrumental in the Company's US\$40 million capital raising. Further details of his background are set out in the Directors report section of the Company's Annual Report.

The Board recommends that shareholders pass the resolution set out in item 2 of the Notice of Annual General Meeting.

3. Item 3 set out in the Notice of Annual General Meeting concerns a proposed issue of fully paid ordinary shares in the capital of the Company as part consideration for what is, in

effect, the indirect acquisition by the Company of a 49% interest in a nickel limonite deposit in New Caledonia.

## **BACKGROUND**

On 18 August 2007 the Company entered into an agreement, in French, (**SMGM Agreement**) which, if it becomes free of both conditions precedent and condition subsequent, will secure for the Company a very large part of the nickel ore the Company will need, to proceed with the Gladstone Nickel Project.

The parties to the SMGM Agreement are the Company, its New Caledonian subsidiary (Gladstone Nouvelle Calédonie SAS (**GNC**)), a New Caledonian mining company Société Minière Georges Montagnat SARL (**SMGM**) and its shareholders LaSociété MO5, Mr Georges Montagnat and Mrs Janine Decamp (**Shareholder Group**). LaSociété MO5 is a New Caledonian civil partnership the members of which are members of the Montagnat family.

The SMGM Agreement was amended on 31 August and 11 September 2007 but the amendments do not bear on any matter relevant to the Resolution in item 3 of the Notice of Annual General Meeting.

The SMGM Agreement provides (subject to conditions precedent) for SMGM to be spun off into two separate New Caledonian companies. To one of those companies, to be called Ouinne SAS (**Ouinne**), certain mining concessions, located in the Ouinne area on the east coast of the South Province of New Caledonia, owned by SMGM (**Ouinne Tenements**) will be transferred along with an amount of cash equivalent to approximately US\$100,000. The Shareholder Group will become shareholders in Ouinne as a result of the spin off of SMGM

Once the spin off has been completed Ouinne will operate as an incorporated joint venture between GNC and the Shareholder Group to explore for and mine nickel limonite ore from the Ouinne Tenements. GNC will contribute an initial cash amount equivalent to US\$98,000 towards the joint venture's working capital requirements. Funding for exploration and evaluation will be provided, by way of loans by GNC (49%) and the Shareholder Group (51%) GNC will have the right to appoint 2 of 4 directors of Ouinne and a range of important decisions will require unanimous resolution of the directors or shareholders of Ouinne.

GNC's initial shareholding in Ouinne will be nominal. In due course (at least 3 years after the spin off of SMGM is completed) GNC will acquire from the Shareholder Group additional Ouinne shares to bring its shareholding to 49% (**Additional Shares**) This will reduce the Shareholder Group's shareholding to 51%. The consideration for this acquisition will be US\$5,000,000 (paid by the Company into escrow and to be paid to the Shareholder Group, as a deposit, when the SMGM spin off is completed) and a number of fully paid ordinary shares in the capital of the Company (**Consideration Shares**). For a detailed discussion concerning the proposed issue of the Consideration Shares see the discussion in the section headed "Proposed Share Issue" below.

The date on which the acquisition of the Additional Shares will take place, and on which the Company will allot and issue the Consideration Shares (**Sale Date**) is the later of the business day following:

- (a) the date that is three years and one day after the SMGM spin off is completed;
- (b) the date on which sufficient funding to construct Stage 1 of the Gladstone Nickel Project becomes available; and
- (c) the date on which Ouinne has received final approval from the New Caledonian Mining Commission for the development of a mine on the Ouinne Tenements.

Under the SMGM Agreement the Company has until 31 December 2009 (or if the Company elects to pay the Shareholder Group a non-refundable additional;US\$1,000,000, 31 December 2010) within which to obtain the funding necessary to construct Stage 1 of the Gladstone Nickel Project.; failing which the Shareholder Group can:

- terminate the SMGM Agreement;
- get back the Ouinne shares held by GNC for US\$1; and
- keep all the money which has been paid under the SMGM Agreement (including the US\$5,000,000 deposit).

If the SMGM Agreement is terminated under this provision the Company and GNC must forego all of the loans then owing to them by Ouinne. This requirement regarding funding for the construction of Stage 1 of the Gladstone Nickel Project represents a condition subsequent to the SMGM Agreement.

The Company has, under the SMGM Agreement already commenced, at its cost, drilling on the Ouinne Tenements to confirm the existence of, and quantify, the nickel limonite resources on the Ouinne Tenements as soon as possible. If a JORC Code compliant ore reserve of at least 30 million dry tonnes, grading at least 1.35% nickel, is not established on the Ouinne Tenements, with New Caledonian mines department approvals to mine that reserve in place, by 30 June 2008 the Company has the right to terminate the SMGM Agreement. Termination by the Company has the same consequences as if the SMGM Agreement were terminated by the Shareholder Group due to funding for the construction of Stage 1 of the Gladstone Nickel Project not having been obtained by the relevant dates (as described above), save that GPNL will be entitled to a refund of the US\$5,000,000 deposit.

Development of a mine on the Ouinne Tenements is, according to the SMGM Agreement, to be funded, to the extent possible on reasonable commercial terms by external borrowings. The remainder of the required funding is to be provided by the Company or GNC and the Shareholder Group, as loans, in proportion to shareholdings in Ouinne. However, the Shareholder Group can opt out of providing its share of these funds and, if it does so, the Company or GNC will have to make up the shortfall, also as loans. Repayment of loans will have priority over other payments to shareholders and will be made annually so as to effectively amortise the shareholder loans over the expected life of Ouinne's mines. Loans will be unsecured and will carry interest at the New Caledonian Bank Rate from time to time. Accrued interest will be capitalised annually.

Importantly the SMGM Agreement provides for Ouinne to supply all limonite ore mined from the Ouinne Tenements to the Gladstone Nickel Project against an annual shipping schedule proposed by the Company and settled in negotiation with Ouinne. The Company triggers the commencement of supply by giving at least six months prior notice to Ouinne of the initial shipment date. From that initial shipment date the Company must take a minimum of 500,000 wet metric tonnes per year of nickel limonite ore from Ouinne. A pricing schedule (involving alternative formulae) has been agreed for the supply of ore by Ouinne to the Gladstone Nickel Project. The agreed formulae are consistent with current New Caledonian market practices for supply of nickel ores.

The conditions precedent to the SMGM Agreement are:

- (a) the New Caledonian Tax Office giving written confirmation regarding certain aspects of the spin off of SMGM into two new corporations,
- (b) the Company's shareholders approving the issue of the Consideration Shares;
- (c) TSX approving of the issue of the Consideration Shares; and

- (d) a standard Australian foreign investment condition.

These must be satisfied by 31 December 2007 (or a later agreed date) failing which the SMGM Agreement will terminate. In that case the escrowed deposit of US\$5,000,000 would be returned to the Company together with interest earned on it. The Australian foreign investment condition has now been satisfied.

### **PROPOSED SHARE ISSUE**

The Consideration Shares that the Company must issue to the Shareholder Group on the Sale Date, as part consideration for GNC's acquisition of the Additional Shares, comprise 12,000,000 fully paid ordinary shares in the Company's capital, ranking from issue equally with all other fully paid ordinary shares comprised in the Company's capital, as that number may be adjusted as provided in the SMGM Agreement.

The SMGM Agreement provides for the number 12,000,000 to be adjusted if, on the Sale Date, the market value of the Company's shares is other than US\$5.42. This adjustment has been agreed principally to reflect an agreed value for a 49% interest in Quinne of US\$70,000,000. The effect of the adjustment is to ensure that the minimum value of the Consideration Shares will be US\$65,000,000 upon issue (the remainder of the US\$70,000,000 being made up of the US\$5,000,000 deposit paid in cash).

At market values above US\$5.42 there will be a reduction in the number of the Company's fully paid ordinary shares that comprise the Consideration Shares; that reduction being:

- at market values up to US\$5.83 per share a number of the Company's fully paid ordinary shares representing the incremental value, above US\$65,000,000, of 12 million of the Company's shares; and
- at market values above US\$5.83 per share a number of the Company's fully paid ordinary shares representing the US\$5,000,000 deposit paid to the Shareholder Group. In this case the value attributed to a 49% interest in Quinne, through the Consideration Shares, could exceed US\$70,000,000

At market values below US\$ 5.42 there will be an increase in the number of the Company's fully paid ordinary shares that comprise the Consideration Shares so that the total value of the Consideration Shares is equal to US\$65,000,000.

For the purposes of the adjustment to be made to the number of the Company's fully paid ordinary shares that comprise the Consideration Shares market value of the Company's shares will be the volume weighted average of the selling prices of the Company's shares achieved, on all stock exchanges on which the Company's shares are listed, over the 30 business days before the Sale Date (converted to US Dollars at exchange rates determined by the Company (or if there is a dispute as to exchange rates, then determined by the Company's auditor)).

The persons comprising the Shareholder Group will take the Consideration Shares in the same proportions as they currently own shares in SMGM.

### **THE SHAREHOLDER APPROVAL REQUIRED**

Rule 7 of the Company's Constitution prohibits the Company, without Shareholders' approval, in any period of 12 months, issuing or agreeing to issue a number of securities which represents more than 15% of the aggregate of the number of its shares that were on issue 12 months previously and certain shares issued during that 12 month period (**Base Share Number**).

Where there is an agreement providing for the issue of shares, the relevant time to test whether or not Rule 7 necessitates the obtaining of shareholder approval is not when the shares are issued but when that agreement is entered into. The unadjusted number of the Consideration Shares is 12,000,000. That number represents 31.3% of the Base Share Number as at the date the SMGM Agreement was entered into. As that percentage exceeds 15%, and albeit that the Consideration Shares will not be issued for more than 3 years (and the relevant percentage is likely to then be less than 15%) Rule 7 requires that Shareholders approve of the proposed issue of the Consideration Shares.

The Resolution set out in item 3 on the notice of Annual General Meeting seeks shareholder approval for the issue by the Company of the Consideration Shares when they are due to be issued under the SMGM Agreement (namely on the Sale Date) to the persons to whom they are to be issued (namely the persons comprising the Shareholder Group). If passed, that Resolution will permit the Company to issue, as the Consideration Shares 12,000,000 of the Company's fully paid ordinary shares plus or minus the number of those shares representing the adjustment to be made under the provisions of the SMGM Agreement (as discussed in the section above headed "Proposed Share Issue") regardless of the number of those shares and the percentage they then represent of:

- the Base Share Number;
- the number that would be the Base Share Number if calculated on the Sale Date instead of the date of the SMGM Agreement; and
- the total issued capital of the Company on the Sale Date.

The passing of that Resolution will not have any effect on the number of shares in the Company's capital that the Company can issue before the Sale Date without Shareholder approval, either by increasing or reducing that number. Shares issued with the approved of Shareholders are not, under Rule 7, taken into account in determining whether or not the 15% allowed under that Rule will be exceeded. That 15% is calculated only in respect of the Company's shares that are on issue when the calculation is made. As the Consideration Shares will not be on issue before the Sale Date the permitted 15% will not be calculated on a number of shares that includes the Consideration Shares.

## **EFFECT OF ISSUE OF CONSIDERATION SHARES ON CAPITAL STRUCTURE AND CONTROL**

It is not possible for the Company to predict, at this time, exactly how many of the Company's shares will comprise the Consideration Shares or what percentage of the Company's issued share capital the Consideration Shares will be when they have been issued. This is because:

- in the case of number, it is impossible to predict what the Company's shares will trade at over the 30 business days leading up to the Sale Date (a date which is more than 3 years away) and what the relevant currency exchange rates will be during that period. Currently the Pound Sterling to US Dollar and Canadian Dollar to US Dollar exchange rates would be relevant due to the Company's shares trading on AIM and TSX; and
- in the case of percentage, the number of the Consideration Shares cannot be predicted for the reasons given above; and
  - the amount of the funding required to construct Stage 1 of the Gladstone Nickel Project is not currently known (in the Company's announcement of its interim results for the six months ended 31 December 2006, made on 12 March 2007, the Company announced that the then pre-feasibility level capital cost estimate was in the order of US\$2.8 billion);

- the percentage interest that the Company will retain in the Gladstone Nickel Project at the time the funding package for its construction is assembled is not known (it is likely the Company will seek one or more major corporations to become participants in the development of the Project resulting in the Company not owning 100% of the Project at that time);
- the mix of equity and debt in the funding package for the construction of the Project is not known and will depend, among other things, on the level of debt that can be negotiated at the relevant time having regard to then prevailing market conditions.

It is possible, but your directors think it is very unlikely, that the Shareholder Group could collectively become the major shareholder in the Company and, at the extreme, control more than 50% of the voting power in the Company. The directors believe a more likely scenario is that the Shareholder Group will collectively hold somewhere between 6% and 20% of the voting power in the Company as at the Sale Date.

## **DIRECTORS RECOMMENDATION**

Stage 1 of the Gladstone Nickel Project, as it is currently proposed for the Company's integrated definitive feasibility study, requires at least 3 million dry metric tonnes of imported nickel limonite ore, grading in the order of 1.40% nickel, per annum for at least 25 years.

For some time the Company has been pursuing a strategy of securing an ownership interest in an off shore ore supply source, believing that having an ownership interest in a significant proportion of the imported ore required for the Project will give the Project greater security than relying only on ore supply agreements or arrangements supported by short term leasing arrangements.

The SMGM Agreement is the initial outcome of that pursuit and is a very significant event for the Company, achieved at an important time, in terms of maintaining the schedule for the Gladstone Nickel Project's development. Based on the Company's internal review of the results of extensive drilling carried out by SMGM on the southern part of the Ouinne Tenements (5,728 metres drilled), the Board believes that the Ouinne Tenements contain a resource of a size and grade that would significantly support the Gladstone Nickel Project and the Company's objectives. The northern part of the Ouinne Tenements is relatively unexplored but drill results indicate the area is highly prospective for nickel laterite of sufficient grade to meet the requirements of the Gladstone Nickel Project. Very importantly the Ouinne Tenements are located close to deep water shipping channels.

Based on the information above the directors of the Company unanimously recommend that Shareholders vote in favour of the Resolution set out in item 3 of the Notice of Annual General Meeting.

## **4. Glossary**

In this Explanatory Memorandum the following expressions have the following meanings respectively:

<b>Expression</b>	<b>Meaning</b>
AIM	Market of that name operated by London Stock Exchange Plc
Board	The board of directors of the Company
Gladstone Nickel Project and the	A high pressure acid leach plant, refinery and

<b>Expression</b>	<b>Meaning</b>
Project	related infrastructure proposed to be established at Gladstone, Queensland, nickel laterite mining and beneficiation operations proposed to be conducted at Marlborough, Queensland, nickel laterite mining and exportation operations proposed to be conducted in the south western Pacific region (including New Caledonia) and all necessary related infrastructure and operations the subject matter of the integrated definitive feasibility study currently being conducted by the Company.
GPNL or the Company	Gladstone Pacific Nickel Limited ACN 104 261 887 and its wholly owned subsidiaries.
CIM Standard (43-101)	The standards of the Canadian Institute of Mining for reporting mineral resources
Resolution	A resolution set out in the Notice of Annual General Meeting
Shareholder	A holder of Ordinary Shares in the Company
SMGM Agreement	Includes the agreement as so defined elsewhere in this Explanatory Memorandum as it may be amended from time to time in any manner not material to the subject matter of the Resolution set out in item 3 of the Notice of Annual General Meeting.
Stage 1	The initial stage of the Gladstone Nickel Project: <ul style="list-style-type: none"> <li>• described in the SMGM Agreement as involving at least one autoclave with a planned annual production of 25,000 tonnes of nickel metal; and</li> <li>• as being studied in the Company's integrated definitive feasibility study, involving two autoclaves with a planned annual production of 60,000 tonnes of nickel metal</li> </ul>
TSX	Toronto Stock Exchange