



Paragon Fund Monthly Performance Report

May 2014



PARAGON FUND UPDATE – May 2014

KEY FUND FACTS	
Fund Managers	John Deniz & Nick Reddaway
Strategy	Australian absolute return
Inception Date	01/03/2013
Net Return p.a.	19.7%
Total Net Return	25.2%

PERFORMANCE (after fees)	
1 month	3.2%
3 month	2.8%
6 month	5.5%
Financial YTD	24.0%
1 year	26.2%

FUND DETAILS	
NAV	\$1.2519
Entry Price	\$1.2538
Exit Price	\$1.2500
Fund Size	\$11.3m

COMMENTARY

The Paragon Fund returned +3.2% after fees for the month of May 2014. Since inception the Paragon Fund has returned +25.2% after fees vs. the market (All Ordinaries Accumulation Index) +12.8%.

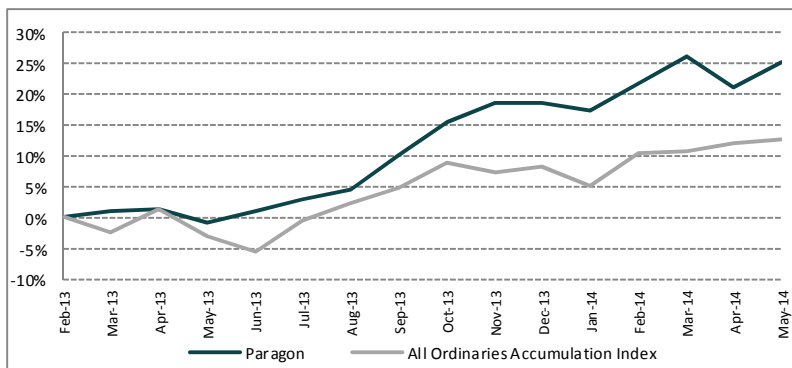
Global equity markets bucked the sell in May adage, posting positive gains in most developed markets with the S&P500 reaching a record high. The domestic market was buoyed by further M&A, as SFG Australia, SAI Global and Treasury Wine Estates all received takeover offers. Iron ore prices continued to weaken, falling over 12% for the month and pressuring related equities while the budget weighed on consumer confidence and retail shares.

Key drivers of the Paragon Fund performance for May 2014 included:

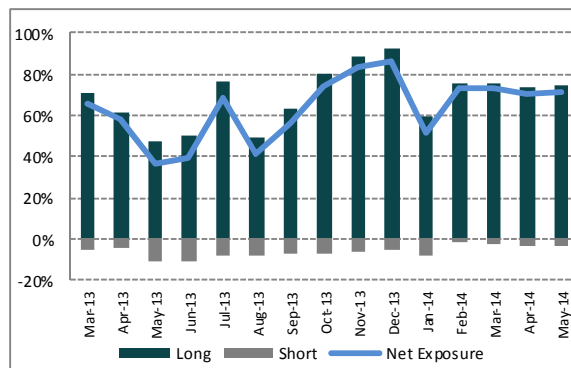
- Strong returns from resource related equities (LNG Ltd and Oz Minerals) as well as Virtus Health
- Receiving a takeover offer in SFG Australia

This month we provide a brief update on our holdings in Liquefied Natural Gas (LNG AU) and SFG Australia (SFW AU).

HISTORICAL PERFORMANCE (after fees)



HISTORICAL EXPOSURE



	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	YTD
2013			1.1%	0.3%	-2.2%	1.8%	1.8%	1.6%	5.3%	4.9%	2.8%	0.0%	18.7%
2014	-1.1%	3.8%	3.6%	-3.9%	3.2%								5.5%

Performance results are presented net of all transaction costs, investment management and performance fees incurred by the Fund. Monthly performance figures are calculated based on the main series using a monthly unit pricing methodology based on historical data.

PORTFOLIO BREAKDOWN

INDUSTRY EXPOSURE			
	Long	Short	Net
Resources	42.0%	0.5%	41.5%
Industrials	29.5%	2.4%	27.1%
Financials	2.6%	0.0%	2.6%
Total	74.1%	2.9%	71.2%
Cash			28.8%

HOLDINGS	
Long	25
Short	2
Total	27

CONCENTRATION	
Top 5	25.6%
Top 10	43.5%



LNG Ltd (LNG AU). We wrote about our holding in LNG in March 2014 outlining our view that LNG Ltd's 100%-owned Magnolia project, in Louisiana USA, is one of the best emerging LNG export projects across the globe. LNG Ltd has continued to deliver on key milestones, de-risking our investment thesis, and as we anticipated the market has substantially rerated the stock.

- We believe LNG Ltd's Magnolia project has huge competitive advantages and LNG Ltd continues to be very well placed to progress through the required Federal and Regulatory approvals, realise binding sales contracts for at least its 4mtpa base-case project (FTA only countries), and in turn the raise the necessary debt and equity funding for its \$2.2b of capex. We continue to view LNG Ltd's Magnolia project's 8mtpa high-case project (both FTA + non-FTA countries) as increasingly likely, and the market is now starting to discount this realisation, following recent key milestones:
 - o Early May 2014, LNG Ltd's Magnolia project completed its key Federal Energy Regulation Commission (FERC) "Filing status" acceptance milestone, catapulting Magnolia into a top 10 US LNG export project. This puts Magnolia on track to be fully approved and financed by 30 June 2015. This then would see Magnolia as a top 5 US LNG export project – on track to be constructed and producing by CY19.
 - o Late May 2014, the US Department of Energy (DOE) outlined a proposal to materially improve and simplify the future non-FTA LNG export regulatory process, essentially abolishing the existing "queue" for US LNG export projects. This proposal substantially de-risks LNG Ltd's Magnolia project's 8mtpa high-case scenario. This DOE change strengthens LNG Ltd's plans to engage with a much broader market of LNG buyers (both FTA-only and non-FTA countries) for binding tolling agreements and with the potential for higher tolling capacity fees.
- Both of the above key milestones de-risk our investment case in LNG Ltd. Our risked 4mtpa base-case valuation is \$1.20/sh. Our un-risked 4mtpa base-case and 8mtpa high-case valuations are \$1.50/sh and \$4.08/sh, respectively. Paragon invested in LNG AU in August 2013 at \$0.20/sh and is currently trading at \$1.36/sh. We have halved our position into LNG Ltd's price strength.

SFG Australia (SFW AU). With ~\$14bn in funds under advice (FUA), SFG is the 8th largest FUA business in Australia, and the largest independent financial planning group. The business has been able to grow by double digits annually over the last few years despite a mediocre equity market through both organic growth and acquisitions.

- We invested in SFG in April 2014 because we believed the market was undervaluing the quality of the business. SFG's valuation was below equity market linked peers and the market overall despite a forecast ~20% return on equity, ~5% dividend yield and a strong (net cash) balance sheet. SFG also offers leverage to positive equity markets and indeed the structural growth in superannuation (superannuation assets are expected to compound at 6% p.a. over the next decade).
- While the company had a strong track record of acquiring and integrating companies, the strategic nature of their business to bigger financial institutions meant they were always a potential target themselves. On 16th May, IOOF launched a friendly, scrip-based takeover of SFW for \$670m, implying a 25% premium. SFW endorsed the bid subject to a competing higher offer.
- If successful, IOOF would catapult from the 5th biggest advice business by FUA to the 3rd biggest, behind only AMP and Commonwealth Bank. With the growth forecast for the superannuation industry and potential synergies in combining the businesses, we feel the bid for SFG certainly makes sense for IOOF. The lack of a significant premium in the bid means there is potential for interest from other parties given the scale benefits SFW could bring. We have a floor price in the IOOF bid and rate a competing higher offer as likely. In this event we feel a bid exceeding \$1/sh is likely and we maintain our holding in the stock.

10th June 2014

Paragon Funds Management