PARAGON FUNDS MANAGEMENT

THE PARAGON FUND // August 2016

PERFORMANCE SUMMARY *(after fees)*

	1 month	3 month	6 month	Financial YTD	1 year	2 year p.a.	3 year p.a.	Net Return p.a.	Total Net Return
Paragon Fund	-7.8%	+0.9%	+28.4%	-5.1%	+30.0%	+15.5%	+23.1%	+20.9%	+94.7%
ASX All Ordinaries Acc.	-1.3%	+2.5%	+14.2%	+4.9%	+10.7%	+3.6%	+7.1%	+6.8%	+25.7%
RBA Cash Rate	+0.2%	+0.4%	+0.9 %	+0.3%	+1.9%	+2.1%	+2.2%	+2.3 %	+8.4%

RISK METRICS

Sharpe Ratio	1.3
Sortino Ratio	2.5
Volatility p.a.	+14.1
% Positive Months	+71.4%
Up/Down Capture	+98%/+2%

FUND DETAILS

NAV	$1.8324
Entry Price	$1.8351
Exit Price	$1.8296
Fund Size	$75.7m
APIR Code	PGF0001AU

FUND STRATEGY

The Paragon Fund is an Australian equities long/short fund established in March 2013. The Fund's strategy is fundamentally driven, concentrated and transparent for investors. Paragon's research process and active portfolio management is overlaid with strong risk management and a focus on capital preservation.

The objective of the Paragon Fund is to return in excess of 10% p.a. after fees over a 3-5yr investment horizon.

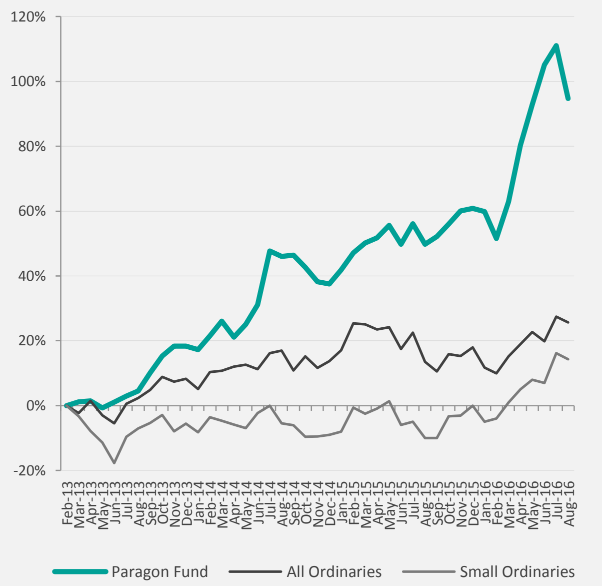
OVERVIEW & POSITIONING

The Paragon Fund returned -7.8% after fees for the month of August 2016. Since inception (March 2013) the Fund has returned +94.7% after fees vs. the market (All Ordinaries Accumulation Index) +25.7%.

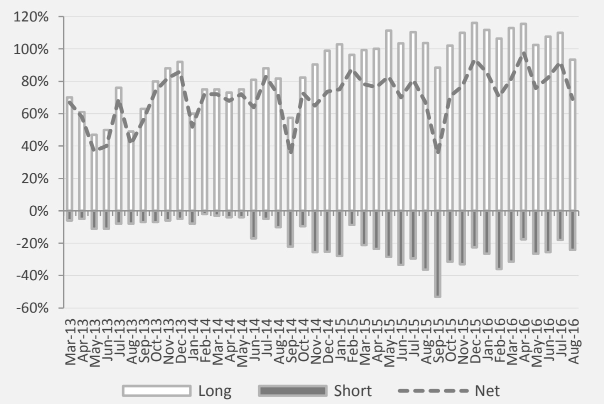
Many of our strong performers corrected in August arising from general profit taking plus some stock specific issues. We elaborate further in our report below. At the end of the month the Fund had 27 long positions and 12 short positions.

INDUSTRY EXPOSURE	Long	Short	Net
Financials	+15.9%	-4.6%	+11.2%
Industrials	+32.7%	-6.3%	+26.4%
Resources	+44.7%	-13.2%	+31.5%
Index Futures		0%	0%
Total	**+93.3%**	**-24.2%**	**+69.1%**
Cash			**+30.9%**

HISTORICAL PERFORMANCE *(after fees)*



HISTORICAL EXPOSURE



MONTHLY PERFORMANCE BY YEAR

	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%	4.9%	12.5%	-1.1%	0.3%	-2.5%	-3.1%	-0.5%	**15.9%**
2015	3.2%	3.6%	2.1%	1.1%	2.4%	-3.8%	4.3%	-4.2%	1.6%	2.5%	2.6%	0.3%	**16.8%**
2016	-0.5%	-5.2%	7.4%	10.8%	7.0%	6.3%	2.9%	-7.8%					**21.2%**

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 lead series using a monthly unit pricing methodology based on historical data.

STOCK HIGHLIGHTS

August was a challenging month and resulted in the Paragon Fund's worst performance since inception. As stated above, many of our strong performers corrected in August arising from general profit taking plus some stock specific issues. These included Galaxy Resources, Blackham, Aconex, Orocobre and Mayne Pharma, accounting for half the negative return for the month. All five of these stocks have been significant contributors to the Fund's strong long term performance, with growth up on cost of: Galaxy +150%, Blackham +700%, Aconex +50%, Orocobre +160%, and Mayne Pharma +80%. Given we typically invest on a medium to long term basis our view on these companies has not changed.

We endeavour to avoid volatility, however we wish to remind investors this is not always possible. Testament to our investment process the Fund has compounded in excess of 20% pa since inception and as active portfolio managers we will continue to capitalise on opportunities as they arise while managing short term drawdowns. Our last drawdown was 6.9% in the 4Q14 which we subsequently made up in 2 months.

In adhering to our commitment to transparency, below we discuss the key stocks that attributed to August performance and why our investment process allows us to have conviction in these holdings and the portfolio overall.

Gold holdings

We continue to have a constructive view on gold, however August saw a correction in all gold equities including our specific holdings. This was largely attributed to increased rhetoric from US Fed officials for rate rises potentially from September, premised on strong jobs data / USA full employment conditions. This drove a 4% pullback in the USD gold price, yet caused a material sell off in the related equities. As US real rates have increased marginally, albeit still negative, we have reduced our AUD gold exposure to ~10% and expect to navigate our way well through the current volatility.

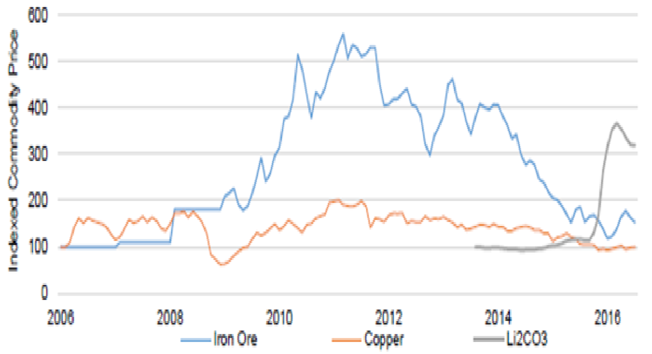
Note AUD gold is within 4% of all-time highs - given offsetting FX - which makes the correction in our AUD gold stocks more surprising. Our AUD gold holdings are all attractively priced, reaping record margins, self-funding their growth and with strong cash flow outlooks. Based on spot AUD gold of A$1750/oz, St Barbara is trading on 5x price-to-cash flow (P/CF) and Blackham 3x P/CF. We expect our gold stocks to continue to perform well as the market turns its focus to strong cash flow generation.

Lithium holdings

The lithium market continues to be buoyant, experiencing unprecedented growth. Two of our largest holdings, Orocobre and Galaxy, were impacted adversely due to announcements of unforeseen delays in achieving full production targets. Strong Chinese spot pricing corrected ~20% off its elevated highs and bearish bulge-bracket broker research predicting material oversupply in lithium from 2017 added to the volatility.

Galaxy fell 15% in August as the company tempered guidance for its Mt Cattlin lithium production for the second half of 2016 and 2017. Orocobre was sold down 7% in August as the company also pushed out its guidance for Olaroz lithium nameplate production (17.5ktpa) by 2 months to November. We were surprised by the negative share price reactions as 1) our modelling has been based on conservatively lower production, given both companies' assets are in ramp up, 2) we expect volume weakness to be offset by strong realised product prices, and 3) we believe that material near-term industry oversupply concerns will prove to be incorrect. Lithium demand should continue to surprise to the upside and new projects coming online on time and at design capacity is also highly unlikely. Galaxy's latest announced delays are a case in point.

As we have expected and written about previously, contract lithium (large volume and hence market indicative) pricing has continued to rise and converge with elevated Chinese spot pricing. We expect the lithium market to more than triple over the next decade and for pricing to remain strong. We draw parallels to the 10yr+ Iron Ore bull market until 2014 driven by China's industrialisation where 1) the global Iron Ore seaborne market more than tripled to 1.5btpa, 2) traded from modest deficits to surpluses over the entire period and 3) resulting Fe prices rose 8x. This took select Iron Ore stocks through a sometimes volatile yet overall exceptionally long bull market run.



Source: Mineral Council of Australia, SNL Mining, Canaccord

We continue to view the fundamentals for lithium and our key stock picks as compelling. We have used the share price weakness in August to buy more Galaxy (at $0.33/sh) given its strong risk-reward (stripping out a very conservative value for its world-class Sal De Vida brine asset implies CY17F PE of 6x and PCF of 5x – outstanding value given Galaxy's strong growth outlook and strategic, solid-margin, low capital-intensity, long mine-life asset mix). As we wrote about in our **December 2015 monthly**, we did the same in Orocobre - where we took the significant price weakness of ~$1.45/sh back in Dec 2015 as an opportunity to substantially increase our position, with the stock more than doubling since.

As we wrote about in our **April 2016 monthly**, we started to take profits in one of our very strong performers Pilbara Minerals in April and then exited fully in May near its highs. We then recycled that capital into another excellent emerging lithium opportunity in Kidman Resources in June, which has made a world class hard-rock lithium discovery in close proximity to existing underutilised infrastructure. Kidman has already started to perform very well for the Fund and we look forward to updating investors on its progress.

Aconex

We wrote about Aconex only last month, updating investors on the company's acquisition of Conject and their latest enterprise client win with Exxon Mobil. August saw the stock fall 20%, initially on profit taking and subsequently after the FY16 results. Management tempered near term revenue growth to 20-25% while maintaining that EBITDA margins would be within 11-16% for the short term while the Conject acquisition was integrated. All long term guidance remained and the visibility they have given their >3yr SaaS contract terms remains a clear strength of the business model.

After the pullback in August the company was trading on forward EV/Sales multiple that is in line with Oracle's most recent acquisitions in the space for inferior companies in terms of quality and size. We saw this as a compelling opportunity to increase our holding.