Paragon Fund Monthly Performance Report

March 2014

PARAGON FUNDS MANAGEMENT

PARAGON FUND UPDATE – March 2014

KEY FUND FACTS	
Fund Managers	John Deniz & Nick Reddaway
Strategy	Australian absolute return
Inception Date	01/03/2013
Net Return p.a.	24.0%
Total Net Return	26.2%

PERFORMANCE (net of fees)	
1 month	3.6%
3 month	6.4%
6 month	14.7%
Financial YTD	25.0%
1 year	24.8%

FUND DETAILS	
NAV	$1.2623
Entry Price	$1.2642
Exit Price	$1.2604
Fund Size	$10.3m

COMMENTARY

The Paragon Fund returned +3.6% after fees for the month of March 2014. Since inception the Paragon Fund has returned +26.2% after fees vs. the market (All Ordinaries Accumulation Index) +10.7%.

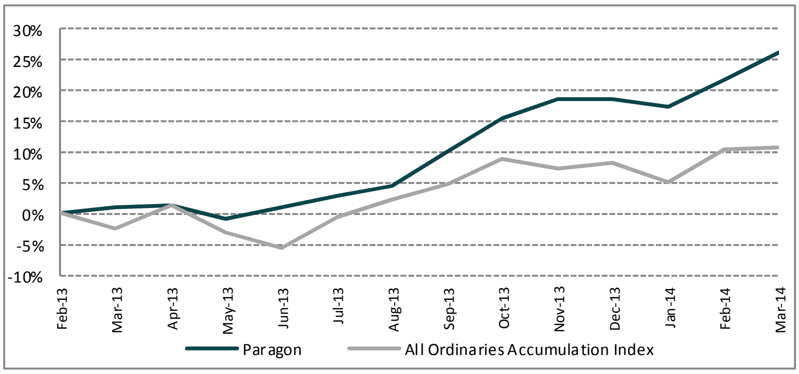
Global equity markets were subdued in March as ongoing concerns were raised over the health of the Chinese economy (financial stability and growth). A seemingly more hawkish Federal Reserve saw market watchers bring forward their expectations for interest rate rises in the US which had ripple effects on in the short end of the bond market and long duration equities. One of the more surprising developments for the month was the rise of the AUD (+4%) as Australian economic data improved along with RBA outlook commentary.

Key drivers of the Paragon Fund performance for March included a combination of:

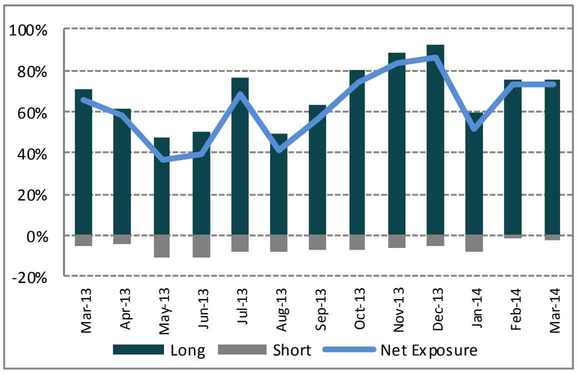
- Continued solid returns from core holdings in G8 Education and Donaco
- Strong gains from machine to machine (M2M) technology company NetComm Wireless, and Liquefied Natural Gas.

In this report we discuss our holding in an emerging infrastructure company exposed to the US shale gas revolution: Liquefied Natural Gas (LNG AU).

HISTORICAL PERFORMANCE (net of 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%										6.4%

Performance results are presented net of all transaction costs, investment management and performance fees incurred by the Fund

PORTFOLIO BREAKDOWN

INDUSTRY EXPOSURE			
	Long	Short	Net
Resources	30.2%	2.1%	28.2%
Industrials	41.7%	0.0%	41.7%
Financials	3.4%	0.0%	3.4%
Total	**75.4%**	**2.1%**	**73.3%**
Cash			**26.7%**

HOLDINGS	
Long	25
Short	3
Total	28

CONCENTRATION	
Top 5	29.5%
Top 10	46.1%

Global Liquefied Natural Gas (LNG) – market dynamics

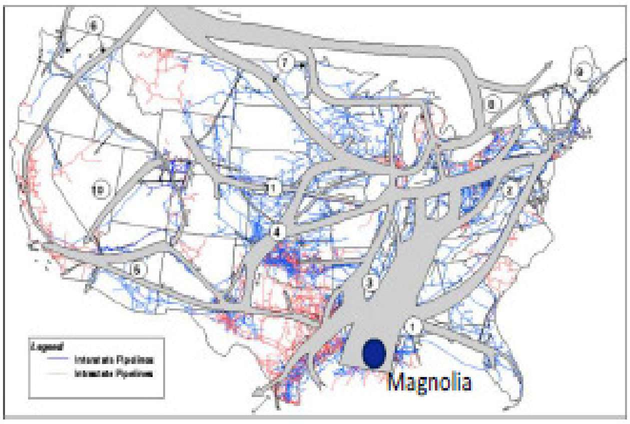
Current global demand for LNG is ~240 million tonnes per annum (mtpa) and is expected to grow to ~530mtpa by 2030. This increase is largely driven by strong forecasted demand across non OECD Asia due to economic and population growth as well as a shift to cleaner energy sources. Note LNG is ~1/600th of the volume of its natural gaseous state, hence is converted to its liquid form for global transportation.

Existing LNG supply and projects currently under construction make up ~330mtpa of global supply, therefore leaving a supply gap of ~200mtpa. Competing for this supply gap is a long list of proposed global LNG projects, which collectively offer over 600mtpa - more than 3 times the 200mtpa of new supply required. With such abundance, only a select few proposed development LNG projects will proceed.

North America emerging as one of the world's key LNG export growth markets

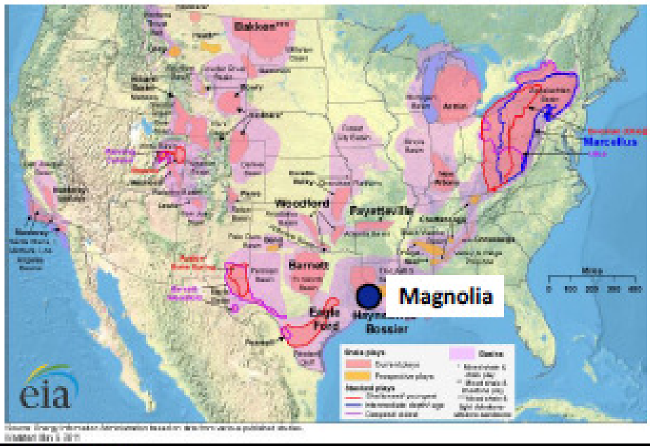
Technological advances have seen the emergence of the North American Shale Gas industry since 2006 which has driven USA gas resources to 2,800 Trillion cubic feet (Tcf), over a 75% increase - nothing short of an American Energy revolution. Utilising its world-class pipeline infrastructure (see Figure 1), Shale gas has helped the USA go from an LNG importer to an LNG exporter. Despite the increased shipping costs vs. other LNG export markets this abundance of cheap gas has elevated the USA to a genuine supply alternative to global LNG consumers pursuing diversified, competitively priced, secure supply.

Figure 1: Extensive access to pipeline infrastructure



Source: LNG ltd

Figure 2: Abundant gas supply



Source: LNG ltd

The USA's increasing gas supply was a key driver for recent federal change that saw the approval of gas for export. As a result, there are now approximately 25 LNG projects throughout North America (USA and Canada) seeking to export over 300mtpa of LNG. We believe less than half the proposed North American projects are likely to proceed, given various project specific risk factors (permitting &/regulatory approvals, extended lead times, uncontracted capacity) and competition from projects in other parts of the world, including Australia, Russia and East Africa.

Key determinants to any global LNG project proceeding successfully include the availability of competitively priced gas reserves, all permitting &/or regulatory approvals, security of supply, competitive capital and operating costs, binding gas sales and purchase contracts ("take or pay"), and a reasonable construction lead time to market. Underutilised, available infrastructure, as with select North American projects, offer strong cost and project lead time advantages.

The prize these projects are seeking is reflected in the fortunes of Cheniere Energy, Inc (NYSE: LNG US).   The company is now valued with an Enterprise Value of US$22b, over 20x where it was in 2010.   Cheniere's first of 2 LNG export projects is coming online in CY15, via its 27mtpa Sabine Pass LNG project in Louisiana which has been successfully de-risked from conceptual design to Federal approvals, through to funding and construction. Cheniere's second LNG export project is its earlier stage, 13.5mtpa proposed Corpus Christi project, scheduled to come online in CY19.

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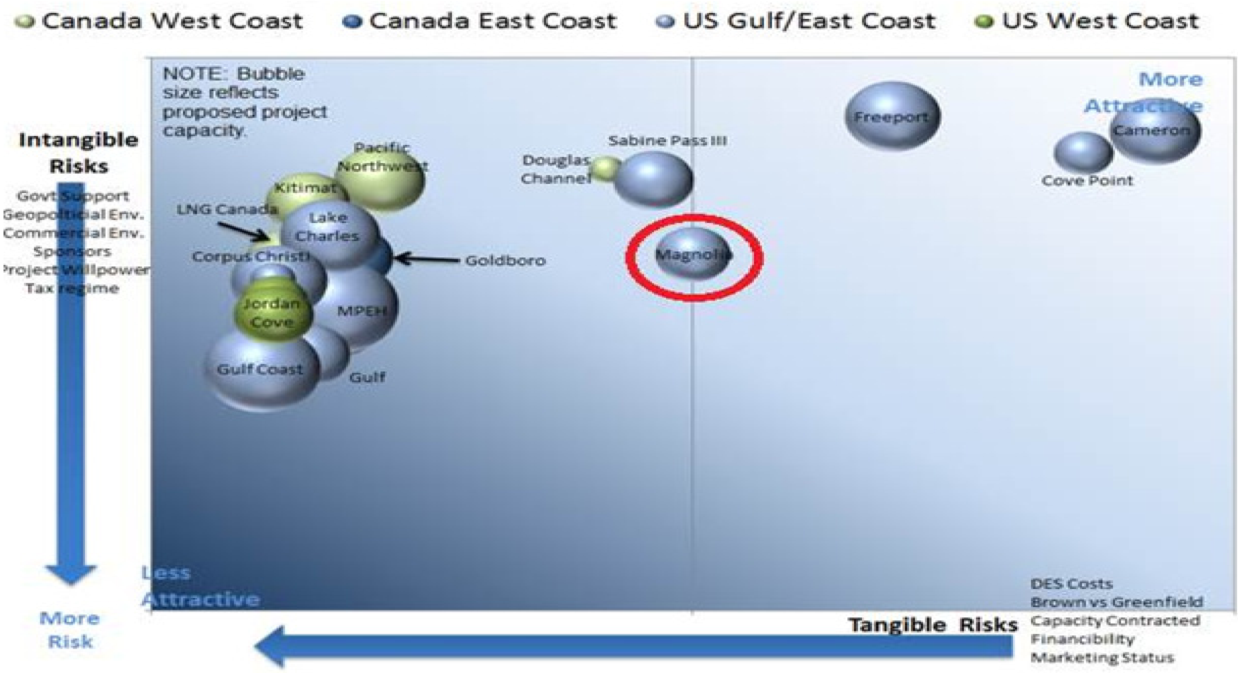
LNG Ltd (LNG AU) – an emerging LNG infrastructure investment, with key project advantages

We view LNG Ltd’s 100%-owned Magnolia project, in Louisiana USA, as one of the best LNG export projects across the globe. LNG Ltd is quite simply, an infrastructure investment. Its Magnolia project will treat, liquefy and store LNG and in-turn receive a tolling/processing fee in return for a guaranteed LNG production capacity. This annuity-style revenue will cover operating costs and provide a fixed margin for the project. Off-take partners will be responsible for delivery of natural gas at their own expense to Magnolia, and marketing and the delivery of LNG.

LNG Ltd’s Magnolia project has progressed into the top 10 US projects in terms of timeline to achieve export of LNG – set to produce LNG by 2019. Over the next 12 months, we view Magnolia as a top 5 US LNG export project, once through Federal Energy Regulation Commission (FERC) “Filing status” approvals. IHS CERA (a global leading energy economic research advisory firm) share this view, already ranking the Magnolia project within the top 5 of potential projects that will be successful – approved, financed and built.



Source: IHS CERA 2013

USA gulf coast LNG export facility projects like Cheniere’s Sabine Pass and LNG Ltd’s Magnolia both have strategic advantages for permitting and construction. These include a centralised and transparent regulatory process for environmental permitting, state and local community support, world-class fabrication facilities, skilled lower cost labour for construction and access via waterways for delivery of major components.

Magnolia is well placed to receive the required Federal and Regulatory approvals, realise binding sales contracts for at least its 4mtpa base-case project (4 20yr Take or Pay contracts totalling 7mtpa have been signed, approval to export up to 8mtpa for FTA countries), and in turn the necessary debt and equity funding for its $2.2b capex for its 4mtpa project construction. The 4mpta base-case project has low capital intensity of US$550/mtpa which compares very favourably to global greenfield project averages of US$1,200/mtpa and Australian brownfield project averages of US$1,000/mtpa. The 8mpta high-case project’s capital intensity is even lower at US$430/mtpa due to economies of scale. The underutilised Kinder Morgan Louisiana gas pipeline, which will transport natural gas from US gas reserves to LNG Ltd’s liquefaction terminals, is located on Magnolia’s site.

LNG Ltd has executed a binding equity agreement with Stonepeak Infrastructure Partners to fund 100% of the equity required at Final Investment Decision (FID) estimated at US$660m whereby Stonepeak receive ~50% project equity based on benchmark IRR criteria with LNG retaining a free carried interest of ~50%.

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PARAGON FUNDS MANAGEMENT

Paragon invested in LNG AU in August 2013 at $0.20/sh having a risked base-case valuation today of $1.00/sh. Our un-risked 4mpta base-case and 8mtpa high-case valuations are $1.55/sh and $2.45/sh, respectively. We forecast that once LNG Ltd's Magnolia 4mtpa base-case project is fully operational, from CY19, it will generate annuity-style EBITDA of ~US$180m pa (LNG 51% equity interest). A Magnolia 8mtpa high-case project can generate annuity-style EBITDA of ~US$360m pa (LNG 51% equity interest). We view the 8mtpa high-case scenario as increasingly likely. LNG Ltd is currently trading at $0.53/sh and we continue to be long the stock.

15th April 2014

Paragon Funds Management

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