



## THE PARAGON FUND // JUNE 2014

### PROFILE

<b>Fund Managers</b>	John Deniz & Nick Reddaway
<b>Strategy</b>	Australian absolute return
<b>Inception Date</b>	01/03/2013
<b>Net Return p.a.</b>	22.7%
<b>Total Net Return</b>	31.3%

### PERFORMANCE *(after fees)*

<b>1 month</b>	4.9%
<b>3 month</b>	4.0%
<b>6 month</b>	10.6%
<b>Financial YTD</b>	30.0%
<b>1 year</b>	30.0%

### DETAILS

<b>NAV</b>	\$1.3130
<b>Entry Price</b>	\$1.3150
<b>Exit Price</b>	\$1.3111
<b>Fund Size</b>	\$12.6m
<b>APIR Code</b>	PGF0001AU

### OVERVIEW & POSITIONING

The Paragon Fund returned +4.9% after fees for the month of June 2014. Since inception the Paragon Fund has returned +31.3% after fees vs. the market (All Ordinaries Accumulation Index) +11.2%.

The Australian equity market lost ground versus global peers in June with waning consumer sentiment seeing no less than 7 retail companies including Super Retail Group and Kathmandu, issue profit warnings. Sentiment was also impacted by heightened geopolitical tensions in Iraq sending oil and gold prices higher for the month. Central banks continue to diverge in their views with the RBA on hold, the Bank of England calling for rate rises, the Federal Reserve tapering its quantitative easing, while the ECB and PBOC both announced credit easing measures.

Key drivers of the Paragon Fund performance for June included strong returns from our investment in Liquefied Natural Gas (LNG AU) and emerging graphite company Triton Minerals (TON AU). At the end of June the fund had 24 long positions and 9 short positions.

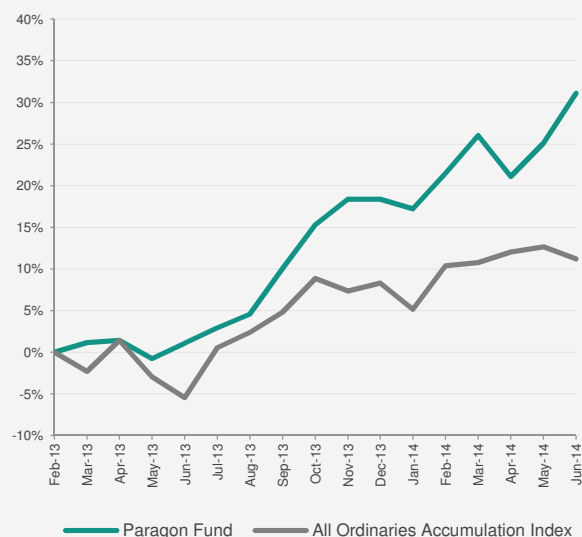
INDUSTRY EXPOSURE	Long	Short	Net
Resources	40.2%	5.1%	35.1%
Industrials	34.4%	9.9%	24.5%
Financials	6.3%	1.9%	4.3%
<b>Total</b>	<b>80.9%</b>	<b>16.9%</b>	<b>64.0%</b>
<b>Cash</b>			<b>36.0%</b>

### STOCK HIGHLIGHTS

#### Oz Minerals (OZL AU)

OZL's South Australian (SA) flagship operation, Prominent Hill, is an open cut mine producing ~100ktpa of copper, 150kozpa of gold and 600kozpa of silver. OZL also holds a portfolio of advanced-stage exploration projects, namely a large-scale greenfield copper and gold project, Carapateena, which if sanctioned is ~5 years from 100ktpa of copper production. Additionally OZL

### HISTORICAL PERFORMANCE *(after fees)*



holds equity interests in a number of listed resource companies including Sandfire Resources (SFR AU).

After a run of consecutive production downgrades, cost blow outs and large cash draw downs in 2H13, OZL has turned the corner having posted solid production upgrades over 4Q13 and 1Q14 which should continue in 2Q14. Prior issues with grade reconciliation in Prominent Hill's inferred resource have been resolved and mining rates at the end of 1Q14 are now well ahead of planned production with the mine plan now adequately feeding its milled production.

In our view, OZL is progressively rebuilding the credibility it lost over the previous 1-2 years with its recovery now in full swing. We forecast OZL's Prominent Hill to go from free cash flow negative to free cash flow positive in 2H14 and we expect its net cash position to have bottomed at ~\$250m in 2Q14.

OZL's disastrous 2H13 was the final straw of years of poor leadership by Terry Burgess, the MD & CEO, who has agreed to step down. OZL will also conduct a strategic review of its other key assets which could see OZL unlock value on



Carapateena and /or a sell down of its interest in SFR. The market is currently giving very little value to both.

At spot AUD FX, copper, and gold prices, OZL is trading on CY15F EV/EBITDA of 4x. Stripping out a conservative \$300m for Carapateena (acquired for US\$250m in CY11) and \$190m for its interest in SFR (at market), implies a proforma CY15F EV/EBITDA of 2x. This is remarkably cheap, both on an absolute and relative basis. Note Pan Aust Ltd (PNA AU) - currently under a \$1.37b takeover offer – is trading on CY15F EV/EBITDA of ~6x, 3 times OZL's pro-forma metrics.

Paragon acquired OZL at \$4/sh with a base case valuation of \$6/sh. OZL is currently trading at \$4.34/sh and we continue to be the long the stock.

## Triton Resources (TON AU)

TON has made an exciting graphite resource discovery at its flagship Balama North project in Mozambique. The project appears to have all the ingredients for a potential world-class discovery including scale, very favourable resource orebody attributes and high-grade.

We discussed our Electrical Vehicle thematic in our Aug 2013 monthly insight into Orocobre (ORE AU), where we highlighted the enormous market potential for lithium. Like lithium, graphite is a vital component of lithium-ion batteries. Despite the name, a 'lithium-ion battery' is mostly graphite and like lithium, its demand growth will be driven by Electrical Vehicle market penetration. The battery segment is currently ~10% of the graphite market and estimated to be growing by ~10% CAGR. Even as global demand for the commodity is surging, China, the world's biggest producer of graphite (~76%), is curtailing mining production in its efforts to reduce pollution.

We had been watching TON for over 12 months as we were interested in its tenement holdings surrounding Syrah's (SYR AU) world-class Balama graphite resource discovered in 1H12. TON's exploration target is 1.2bt at 10% graphite and on our modelling we view this estimate as conservative. Geologically, TON's Balama North project appears to be a natural extension of SYR's Balama project's orebody.

TON has prudently completed early exploration works – ground geochemistry, electromagnetics, surface trenching and shallow aircore drilling – all signalling the potential for a major, high-grade graphite resource. Further, TON's Balama North discovery is easily accessible and has good access to infrastructure (local labour, road and port access).

Upon releasing its first deeper drill hole – an outstanding 200m+ of graphite mineralisation – Paragon initiated a position in TON at \$0.115/sh with a base case fully diluted valuation of \$0.80/sh. Resource delineation is underway and subsequent drilling has been surpassing expectations in both scale and grade. We prudently halved our position at \$0.40/sh. TON is currently trading at \$0.52/sh and we continue to be the long the stock.

## MONTHLY PERFORMANCE BY YEAR

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	TOTAL
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%							10.6%

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

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