PARAGON FUNDS MANAGEMENT

THE PARAGON FUND // APRIL 2015

PROFILE		PERFORMANCE *(after fees)*		DETAILS	
Fund Managers	John Deniz & Nick Reddaway	**1 month**	+1.1%	**NAV**	$1.4622
Strategy	Australian absolute return	**3 month**	+7.0%	**Entry Price**	$1.4644
Inception Date	01/03/2013	**6 month**	+6.5%	**Exit Price**	$1.4600
Net Return p.a.	+21.3%	**1 year**	+25.3%	**Fund Size**	$29.3m
Total Net Return	+51.9%	**Financial YTD**	+15.7%	**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. The managers' research process and active portfolio management is overlaid with strong risk management and a focus on capital preservation.

OVERVIEW & POSITIONING

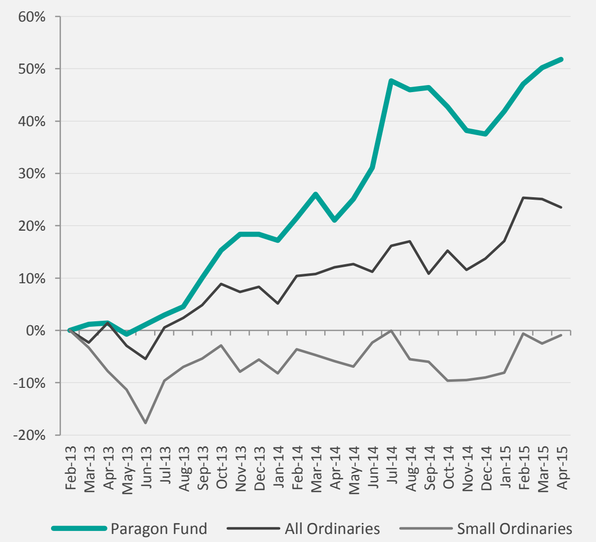
The Paragon Fund returned +1.1% after fees for the month of April 2015. Since inception the fund has returned +51.9% after fees vs. the market (All Ordinaries Accumulation Index) +23.5%.

The Australian equity market fell in April as Australia's major banks were sold after comments from APRA suggested capital requirements would be addressed sooner than expected and as the Australian 10yr bond rate rose 30bps off its lows. Australia's resource sector rallied driven by strong gains in both oil and iron ore, driven by a weaker USD and a less negative oversupply outlook. China was again the global standout, the Shanghai Composite gaining 18.5% for the month on stimulus measures.

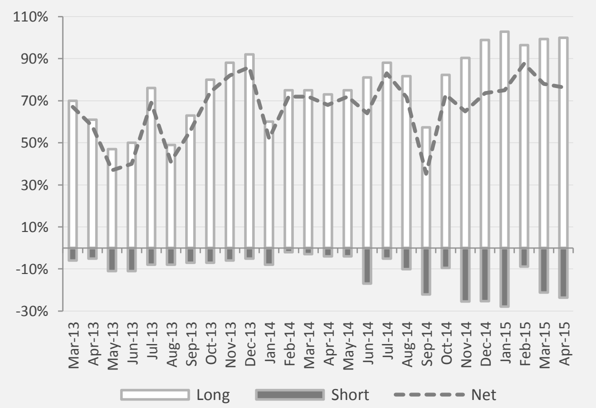
Key drivers of the Paragon Fund's performance for April included solid returns LNG Ltd, Oz Minerals, Mayne Pharma and Metals X. Short positions across USD exposed companies also contributed. At the end of the month the fund had 29 long positions and 13 short positions.

INDUSTRY EXPOSURE	Long	Short	Net
Resources	45.1%	-1.3%	43.8%
Industrials	34.3%	-15.5%	18.8%
Financials	20.6%	-6.8%	13.8%
Total	**100.0%**	**-23.6%**	**76.4%**
Cash			**23.6%**

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%									**10.5%**

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

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STOCK HIGHLIGHTS

LNG Ltd (LNG AU)

We have written about LNG Ltd previously (March 2014 and May 2014), outlining our reasoning behind investing in what remains one of the best emerging LNG export projects across the globe. We also wrote in December 2014 that we had closed out the last of the position (acquired at an entry price of $0.20/sh) at an average of $3.86/sh, largely avoiding LNG's ~50% price correction amid the oil market crash.

This month we take the opportunity to outline why we have bought back into LNG Ltd at a time where its volatility provided an attractive re-entry point.

The oil market collapse in late 2014 put to question three key risks to the LNG Ltd investment case: 1) Magnolia not achieving FERC approval as a consequence of US Oil & Gas exploration and production potentially collapsing, resulting in lower levels of cheap US gas reserves available for LNG export; 2) Magnolia project returns becoming uneconomic due to falling oil-linked LNG toll pricing and 3) Magnolia not securing bankable tolling customers nor achieving Final investment decision (FID) and ultimately financial close on its $3.5b total capex funding required to develop its 8mtpa (now base case) capacity LNG export project.

With respect to the 3 keys risks above, our research post December critically reaffirmed LNG Ltd's ability to secure FERC approval, bankable tolling customers, achieve FID and financial close based on the following: 1) Despite the oil market crash and falling US drill rig count, US gas supply has kept increasing – and there is still an abundance of cheap US gas – a key condition precedent for FERC approving more US LNG for export. 2) Despite lower oil prices, Magnolia's project economics remain strong, premised on Magnolia's capex advantage (capital intensity of US$440/t, or ~1/3 of its global peer average) combined with its LNG tolling fee of US$3/mmbtu. 3) Magnolia's competitive advantages provide LNG Ltd a firm window to secure bankable tolling customers short LNG before 2020 when we expect Magnolia to be in production. Note many of Magnolia's peers are highly capital intensive mega LNG projects, which in this lower oil price environment are uncompetitive and/or uneconomic.

Since re-entering LNG Ltd in March 2015 at $3/sh, our investment case has been further de-risked as the company has announced (in April 2015) its first and much anticipated partner to underwrite its 8mtpa Magnolia project. Meridian LNG will progress to a (imminent) binding 20-year liquefaction tolling agreement (LTA) for 2mtpa with a tolling fee above US$3/mmbtu with LNG Ltd's Magnolia project. Meridian will in turn deliver US LNG to E.ON, a EU28b investment grade German utility. This will be the first of 4-5 binding LTA's the Magnolia project is targeting to sign in 2015 in order to achieve financial close on its 8mtpa project. LNG Ltd is advancing several other LTA's with customer s across Europe, Central & South America and Asia, well in excess of its projects 8mtpa capacity requirement.

Paragon has risked base-case and high-case valuations for LNG Ltd of $5.50/sh and $11/sh, respectively. LNG Ltd is currently trading at $4.48/sh and we continue to be long the stock.

QANTAS (QAN AU)

We wrote about our long position in Qantas in our November 2014 monthly. The company was taking steps to right the ship that was close to sinking in 2013, undergoing a significant restructuring in order to curtail costs while simultaneously exhibiting more rational behaviour towards domestic capacity growth. Then in the middle of 2014 the oil price started to crack under rising supply and weak demand. We wrote in that monthly when brent crude was above US$80/bbl, some US$30/bbl off its peak:

> "While the net fuel benefit in 1H FY15 is likely to be ~$30m, the future earnings benefit to falling oil is significant such that should oil continue to hold closer to US$60/bbl next year as we expect, Qantas should produce a FY15 EBIT number in excess of $700m, some 40% ahead of consensus and warranting a share price closer to $3/sh next year based on Qantas's historical EV/EBITDAR multiple of 5x."

With our negative view on oil, we did not feel that most observers of the company were yet to price in the change that had been undertaken within the business that was now coming within sight of a debt free, dividend paying balance sheet. Nor had they priced in the potential for oil to continue its decline and in November less than 30% of analysts covering the stock recommended it as a buy. After writing that monthly, the brent crude price went on to fall to as low as US$45/bbl in January 2015, with the main input cost for airlines, jet fuel, following a similar path. With the rapid decline in oil, estimates for Qantas's FY2015 EBIT moved from below $400m to over $1.1b while the Qantas share price moved from our $1.65/sh entry price to touch $3.50/sh in April 2015. Not surprisingly, over 70% of analysts today now believe the shares are worth buying.

We don't consider airlines generally to be a long term investment proposition given the competitive industry, high level of operating leverage and significant variable input costs (oil) and reiterate the quote from Warren Buffett in our November monthly:

> "How do you become a millionaire? Make a billion dollars and then buy an airline"

There is potentially more upside in the Qantas share price but from here the gains get harder. Oil price benefits have been accounted for, as has the company's restructuring program. Qantas now trades at a valuation much closer to global airline peers and with peak profitability likely in 2016, we don't think the company should trade at a significantly higher multiple to its own historical average multiple of 5x EBITDAR.

Brent crude oil prices have rallied back above US$65/bbl as the USD has weakened, demand prospects have risen out of both Europe and China, and US oil production activity has fallen sharply. The catalyst for originally buying shares in the company, weaker oil, is now the catalyst to sell the shares and we have sold the last of our holding at $3.35/sh.

BUSINESS UPDATE

Paragon is excited to announce the appointment of UBS as Prime Broker and Custodian to the Paragon Fund, replacing Merrill Lynch International, effective from 24th April 2015. UBS AG will undertake all prime brokerage services for the Fund and UBS Nominees, a member of the UBS group, will also act in the capacity of custodian.

Paragon will always seek to engage Tier 1 service providers as part of its overall risk management strategy. UBS is a market leader in Australia, with world class capabilities, resources and people, a strong financial position and an exceptional reputation. UBS will provide Paragon competitive pricing, superior research and the best availability of stocks for shorting (which will allow Paragon to execute its investment strategy without any restrictions).

As part of this changeover, Paragon has reissued the Fund's PDS, dated 27 April 2015, and is available from our website at www.paragonfunds.com.au (or via the following link http://www.paragonfunds.com.au/). We encourage both existing and prospective investors to download and familiarise themselves with the new PDS.

This latest PDS replaces the previous PDS dated 1 February 2014 and Supplementary PDS No 3 dated 31 October 2014, by incorporating all additional disclosures previously reported in the SPDS, as well as updating all relevant disclosures regarding the Prime Broker and Custodian. Note that any new applications are required to be submitted using the new Application Form dated 27 April 2015. Applications received using the previous form will generally not be accepted from May onwards.

Paragon Fund's half year Financial Report to 31 December 2014 has also been finalised and is available to investors from our website at www.paragonfunds.com.au (or via the following link http://www.paragonfunds.com.au/important-information/).