



## PARAGON AUSTRALIAN LONG SHORT FUND // January 2019

### PERFORMANCE SUMMARY *(after fees)*

	1 month	3 months	6 months	Financial YTD	1 year	2 year p.a.	3 year p.a.	5 year p.a.	Net Return p.a.	Total Net Return
<b>Paragon Aust. Long Short Fund</b>	+0.8%	-4.1%	-18.9%	-24.2%	-36.8%	-6.3%	-1.2%	+5.6%	+7.6%	+54.1%
<b>ASX All Ordinaries Accum. Index</b>	+4.0%	+1.6%	-4.7%	-3.6%	+0.7%	+6.6%	+10.0%	+7.1%	+6.9%	+48.6%
<b>ASX Small Ords. Accum. Index</b>	+5.6%	+1.1%	-7.0%	-7.9%	-3.1%	+8.9%	+11.3%	+7.4%	+4.7%	+31.0%

### RISK METRICS

Sharpe Ratio	0.4
Sortino Ratio	0.7
Correlation	0.4
% Positive Months	59%
Up/Down Capture	73%/-10%

### UNIT PRICE & FUM

NAV	\$1.4506
Entry Price	\$1.4528
Exit Price	\$1.4484
Fund Size	\$40.8m
APIR Code	PGF001AU

### FUND STRATEGY

Established in March 2013 as an Australian equities long/short fund that is fundamentally driven with a concentrated portfolio of high conviction stocks, managed by a dedicated investment team and offering transparency to investors. Paragon's proprietary research and extensive investment process which includes active portfolio management, is overlaid with a strong risk management function and a focus on capital preservation. The objective of the Fund is to return in excess of 10% p.a. after fees over a 3-5yr investment horizon.

### OVERVIEW AND POSITIONING

The Fund returned +0.8% after fees for January. Positive contributions for the month were from Adriatic and Fortescue, and a short in Navigator Global (downgrade). These were in part offset by Northern Star (downgrade), New Century and a short in Wisetech. After the FED caused turmoil by continuing to hike rates and taking a hawkish stance in December, it did a complete backflip in January in response to collapsing markets by - 1) suggesting that they will pause on further rate rises; and 2) turn accommodative in ending their balance sheet reduction ('QT') sooner - driving a recovery in equity markets globally. These are two very big catalysts for 'risk assets' and gold.

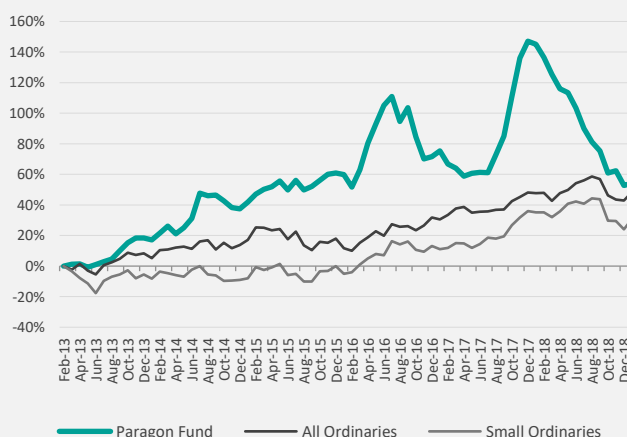
### FUND POSITIONING

Number of Longs	21
Number of Shorts	9
Net exposure	65%
Gross exposure	100%
Index futures	0%
Cash	35%

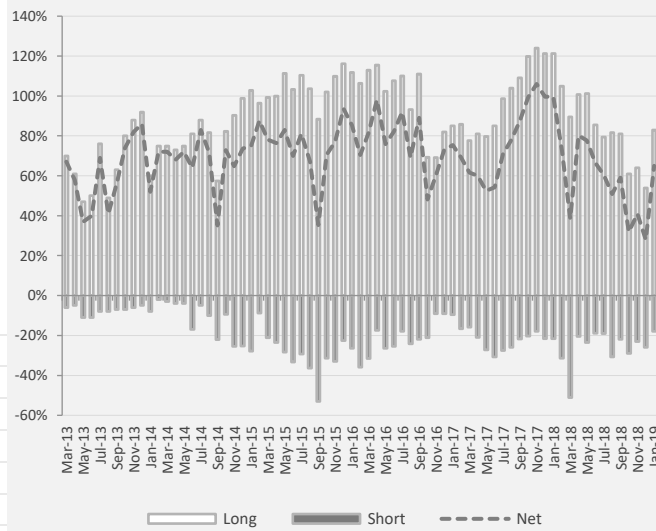
### FUND FACTS

Structure	Unit trust
Domicile	Australia
Applications & Redemptions	Daily
Minimum investment	\$25,000
Min. addition/redemptions	\$5,000/\$10,000
Administrator	Link Fund Solutions
Prime Broker/Custodian	UBS

### HISTORICAL PERFORMANCE *(after fees)*



### HISTORICAL EXPOSURE



### MONTHLY PERFORMANCE BY CALENDAR YEAR

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	YTD
<b>2013</b>			1.1%	0.3%	-2.2%	1.8%	1.8%	1.6%	5.3%	4.9%	2.8%	0.0%	<b>18.7%</b>
<b>2014</b>	-1.1%	3.8%	3.6%	-3.9%	3.2%	4.9%	12.5%	-1.1%	0.3%	-2.5%	-3.1%	-0.5%	<b>15.9%</b>
<b>2015</b>	3.2%	3.6%	2.1%	1.1%	2.4%	-3.8%	4.3%	-4.2%	1.6%	2.5%	2.6%	0.3%	<b>16.8%</b>
<b>2016</b>	-0.5%	-5.2%	7.4%	10.8%	7.0%	6.3%	2.9%	-7.8%	4.3%	-9.0%	-7.9%	0.8%	<b>6.8%</b>
<b>2017</b>	2.3%	-5.0%	-1.6%	-3.2%	1.3%	0.4%	-0.2%	7.3%	7.0%	14.0%	11.9%	4.7%	<b>44.1%</b>
<b>2018</b>	-1.3%	-3.0%	-4.7%	-4.2%	-1.2%	-4.7%	-6.5%	-4.6%	-3.2%	-8.4%	0.9%	-5.8%	<b>-38.1%</b>
<b>2019</b>	0.8%												<b>0.8%</b>

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 daily unit pricing methodology based on historical data.



## Share price life cycle of a high-quality Resources investment

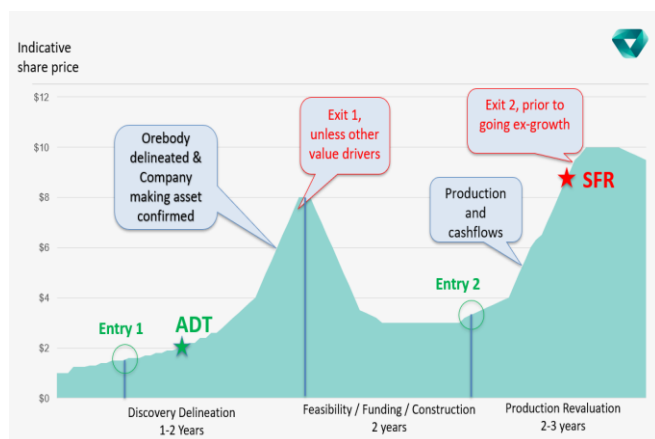
### Adriatic's Zinc discovery continues to surprise to the upside

We previously discussed Adriatic (ADT) in [November 2018](#). Adriatic has made one of the best Zinc-strong polymetallic discoveries at Rupice, its 100% owned Vares Project in Bosnia. Adriatic continues to rate as one of the best Resources stock performers (May 2018 IPO at 20cps; currently at 78cps), with the market appreciating its value potential.

Rupice's orebody is still open to the North and South-East, presenting an excellent opportunity for further scale. In addition, drilling in their prolific northern extension starts within a month, and if homogeneous, should result in an additional ~1mt of ore for every 75m step out. Adriatic's update in January has delineated excellent high-grade polymetallic extensions in the South East, beyond our initial expectations. While our estimates for Adriatic's Rupice polymetallic orebody delineated to date are >6mt at 12% Zinc equivalent, we will not be surprised if the actual outcome is not only larger but also of higher grade.

Chart 1 below, which plots the share price lifecycle of a high-quality Resources investment, indicates where we currently see Adriatic and how we expect it to evolve. Indeed, many Resource stocks we have invested in, including Dacian, Pilbara, Kidman and Sandfire (and Sirius short), have followed this price curve, as they have made economic resource discoveries and then de-risked through development to production. Adriatic is still in a growth phase, building scale and delineating additional resources, thus improving its already strong project economics.

Chart 1: Share price life cycle of a high-quality Resources investment



Source: Paragon

This chart also provides an overview of where Paragon typically enters Resources stocks:

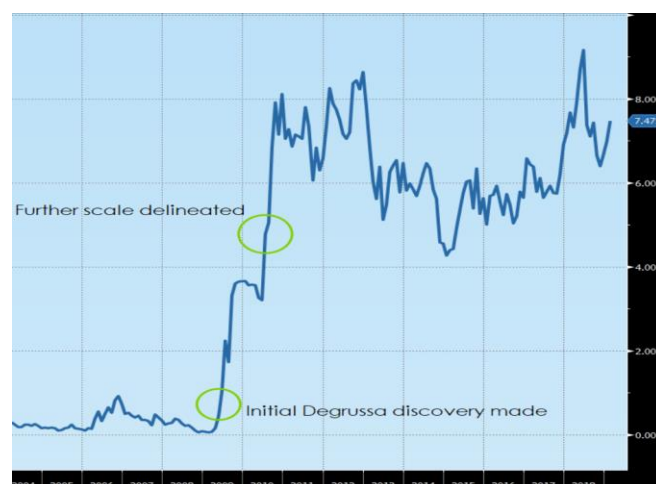
- 'Entry 1' in discovery/delineation phase – Eg. Adriatic, Pilbara, Kidman;
- 'Entry 2' in pre-production/production ramp up phase – Eg. Dacian; and
- 'Exit 1' or 'Exit 2' – taking profits in longs and in some cases going short – Eg. short in Sirius at 'Exit 1'.

We generally avoid the lengthy development and construction phase (middle phase) or when a stock goes ex-growth via a depleting/short mine life, unless there are positive catalysts and value drivers that can see a stock deviate from the usual underperformance norms.

### Adriatic's potential pursued by Sandfire as it attempts to avoid entering ex-growth stage

To further illustrate the point, Chart 2 below is copper-gold stock Sandfire's share price life cycle. Sandfire started as a micro-cap in 2009 making an exceptional copper-gold discovery at Degussa in WA, delineating 10.7mt @ 5.6% Copper and 1.9 g/t Gold supporting ~10yr mine life operation. (Note on a base metals contained equivalent basis, this is around 2x our current estimate for Adriatic's Rupice resource). Sandfire quickly re-rated to a \$1.2b mid-cap company. They comfortably financed and commenced production at Degussa ~2yrs later and have been cash flow positive since.

Chart 2: Sandfire's share price performance; Degussa discovered in 2009



Source: Bloomberg

Now in production, Sandfire has been depleting its Degussa resource inventory. Despite 10 years of extensive exploration and sinking ~\$300m, they have been unable to find additional resources organically. Even following their acquisition of Monty, a much smaller nearby discovery, its short mine life continues to be an increasing issue for Sandfire.

Acutely aware of this, Sandfire's management are busy pursuing growth opportunities around the globe, including a 7% significant shareholding interest in Adriatic. As a sign of the quality of Adriatic's Rupice discovery and exploration upside, Sandfire attempted to raise its significant shareholding in Adriatic to 19.9%. However, the directors and management of Adriatic (holding ~30% interest), working in the best interests of all shareholders to maximise full value, prevented Sandfire's attempt, enabling Adriatic to maintain its strategic appeal.

This dynamic is typical of the entire mid to large cap mining space, where M&A is an ongoing piece of the Resources cycle to replenish inventory and companies such as Sandfire try to avoid going ex-growth.

Adriatic remains well funded, raising equity at 55cps in November 2018. We are confident that Adriatic's 100% owned Rupice is a company-making asset and in time could prove to be as valuable as Sandfire's Degussa (on a \$/t of contained metal basis). We continue to be long Adriatic and look forward to updating investors with its progress.

**DISCLAIMER:** This report has been prepared without taking account of your objectives, financial situation or needs and should not be relied upon as the basis of an investment decision. Paragon makes no representation or warranty as to this report's reliability and does not accept any responsibility or liability in relation to such information or for conclusions which the reader may draw from the report. You should seek independent professional advice before making any decisions regarding the content of this report, including a decision to invest. The Product Disclosure Statement for the Paragon Australian Long Short Fund is available from our website at [www.paragonfunds.com.au](http://www.paragonfunds.com.au). There is no guarantee against loss resulting from an investment in the Fund and past performance is not a reliable indicator of future performance.