PARAGON FUNDS MANAGEMENT

PARAGON AUSTRALIAN LONG SHORT FUND // February 2020

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*
Paragon Aust. Long Short Fund	-14.8%	-12.8%	-16.6%	-6.4%	+6.7%	-16.3%	-0.2%	+2.4%	+7.4%	+66.1%
ASX All Ordinaries Accum. Index	-8.1%	-5.6%	-1.4%	-0.2%	+8.3%	+7.5%	+8.6%	+6.4%	+7.9%	+70.7%
ASX Small Ords. Accum. Index	-8.7%	-5.9%	-2.3%	-1.8%	+1.7%	+2.6%	+8.4%	+7.5%	+5.2%	+42.3%

*Since inception 1 March 2013

OVERVIEW

Amidst a wild month where global Indices initially rose to record highs before falling -16% in the last week on Coronavirus pandemic fears, the Fund fell -14.8% after fees for February. Negative contributors were PointsBet, Xero, Adriatic, Atrum and the bulk of our gold stocks. These were partially offset by Alacer Gold and shorts in Newcrest, Sandfire, Whitehaven Coal and New Hope Coal.

Fears of a pandemic led to panic selling globally as markets attempted to gauge the severity of the economic fallout. This caused US 10yr yields to collapse a further 24% to record lows of 1.15%. US$ gold, whilst initially up >5%, closed flat for the month at US$1,586/oz and A$ gold closed 3.2% up to record highs at A$2,441/oz. Futures markets have swiftly moved to fully price in a 25bps rate cut at the March Fed meeting and pricing in 75bps of cumulative rate cuts by June 2020. Note since the expansion began in June 2009, every time the market fully priced in rate cuts ahead of Fed meetings (1. Jul, 2. Sep & 3. Oct 2019), the cut was undertaken. Rate cuts are coming, which bodes very well for gold and gold equities.

PORTFOLIO INSIGHTS - Gold selling a short-term dynamic; strong outlook maintained

Since the Coronavirus outbreak began, investors globally have been seeking safety in traditional 'store-of-value' assets, including gold and gold equities (moves typically positively correlated 2-3x the gold price), outperforming all other safe-haven assets including the Yen, Swiss Franc, and US 10-year bonds. However, gold and gold equities were then aggressively sold off in the last week of February. This swift selling across global markets, cited as the fastest sell-off in history (quantum inside 1 week), saw gold and gold equities used as a source of liquidity – the main culprits being leveraged money managers liquidating gold to cover margin calls. Unfortunately, this selling activity meant our gold stocks did not work to hedge our portfolio as anticipated, and in fact worked against us. We believe this is a short-term dynamic and expect gold and our gold stock picks to recover, not only providing a good hedge to our other longs, but also to deliver strong alpha over the next 1-2 years. And here is why.

Having successfully invested through gold's last structural bull market, we vividly remember gold's counter-cyclical July-Oct 2008 sell-off through the GFC. As illustrated in Chart 1 overleaf, as the GFC took hold and markets started to sell off, gold performed well with the start of the US Fed rate cutting cycle. Then, as markets plunged in 2H CY08, gold and in turn gold equities also fell, as US real rates (negatively correlated with gold) spiked and gold was sold as a source of liquidity. With further Fed cash rate cuts, US real rates collapsing and Quantitative Easing (QE), investors ultimately saw gold for what it was, and it went on to triple over the next 2.5 years, providing outstanding returns in select gold stock picks. Fast forward to today, Chart 2 overleaf illustrates a very big difference - US real rates have been falling and are now negative and QE has resumed (both are huge drivers for gold), and nations globally are commencing material fiscal stimulus initiatives in an attempt to combat their economic fallout. With further Fed cash rate cuts imminent, we expect that any gold price sell-off will prove to be both limited and short in duration. Our gold stock picks continue to be very well placed.

As fundamental investors, we're holding onto our key high-conviction stock picks whilst increasing hedges via select stock shorts. Whilst these longs may be exposed short-term, many of these stocks will be difficult to get back into without paying materially higher prices once the dust settles on Coronavirus, which it will. Historically, every pandemic eventually settled and was followed by a strong recovery. We are following the data closely, particularly the mortality rate and the rate of change of contracted-virus cases, which pleasingly are both already steadily declining in China. We expect global markets to commence their recovery within a few months.

APPOINTMENT - Haris Khaliqi to join Paragon

We are extremely pleased to announce the appointment of Haris Khaliqi, joining Paragon later this month as a Portfolio Manager, responsible for executing the Fund's strategy alongside John Deniz. Haris has worked in senior and executive roles on the sell-side for the past 10 years. He will bring significant depth and knowledge of the Industrials sectors to Paragon. Having developed strong ties with Paragon in a professional capacity over the last 7 years, we are confident in Haris' philosophical and strategic alignment with Paragon and look forward to him being a strong complement to the team.

FUND POSITIONING & RISK METRICS

Fund Size	$27.1m
Longs	18
Shorts	8
Net exposure	70%
Gross exposure	111%
Index futures	0%
Cash	30%
Beta-adj net exposure/ Average since inception	38%/70%
Correlation	0.4
% Positive Months	61%
Up/Down Capture	75%/53%

UNIT PRICING – LEAD SERIES

NAV (Mid-Price)	$1.5388
Entry Price	$1.5411
Exit Price	$1.5365

FUND FACTS

APIR Code	PGF0001AU
Responsible Entity & Investment Manager	Paragon Funds Management Ltd
Strategy	Aust Equities L/S, Long-bias, Fundamental, Concentrated
Objective	>10% p.a. over 5 yrs
Structure	Unit trust
Domicile	Australia
Pricing/Applications/ Redemptions	Daily
Min. Investment	$25,000
Min. Add/Redemptions	$5,000/$10,000
Administrator	Link Fund Solutions
Prime Broker/Custodian	UBS

PORTFOLIO INSIGHTS (continued)

Chart 1: US$ gold vs S&P500 (in red) vs US Fed cash rate vs US real rates - GFC

US$ gold (in yellow) cyclical bear market from July 2008 to end Oct 2008, as real rates (in green) initially rallied. Then gold resumed its structural bull run from Nov 2008 when real rates rolled over as Fed cash rates (in blue) went to zero, with gold tripling over the next 2.5 years.

Source: Paragon/Bloomberg

Chart 2: US$ gold vs S&P500 vs US Fed cash rate vs US real rates – Present

US real rates (in green) have been falling and now negative (a huge driver for gold), with further Fed cash rate (in blue) cuts imminent. US$ gold poised to break all-time highs over the medium term.

Source: Paragon/Bloomberg