PARAGON FUNDS MANAGEMENT

PARAGON AUSTRALIAN LONG SHORT FUND // December 2016

PERFORMANCE SUMMARY *(after fees)*

	1 month	3 month	6 month	Financial YTD	1 year	2 year p.a.	3 year p.a.	Net Return p.a.	Total Net Return
Paragon Aust. Long Short Fund	+0.8%	-15.5%	-16.4%	-16.4%	+6.8%	+11.7%	+13.1%	+15.1%	+71.5%
ASX All Ordinaries Acc.	+4.2%	+4.4%	+9.9%	+9.9%	+11.6%	+7.6%	+6.8%	+7.5%	+31.7%
RBA Cash Rate	+0.2%	+0.4%	+0.8%	+0.8%	+1.7%	+1.9%	+2.1%	+2.3 %	+8.9%

RISK METRICS

Sharpe Ratio	0.8
Sortino Ratio	1.4
Volatility p.a.	+15.3
% Positive Months	+70%
Up/Down Capture	+80%/+12%

FUND DETAILS

NAV	$1.6143
Entry Price	$1.6167
Exit Price	$1.6118
Fund Size	$80.4m
APIR Code	PGF0001AU

FUND STRATEGY

The Fund is an Australian equities long/short fund established in March 2013. The Fund's strategy is fundamentally driven, concentrated and transparent for investors. Paragon's research process and active portfolio management is overlaid with strong risk management 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.

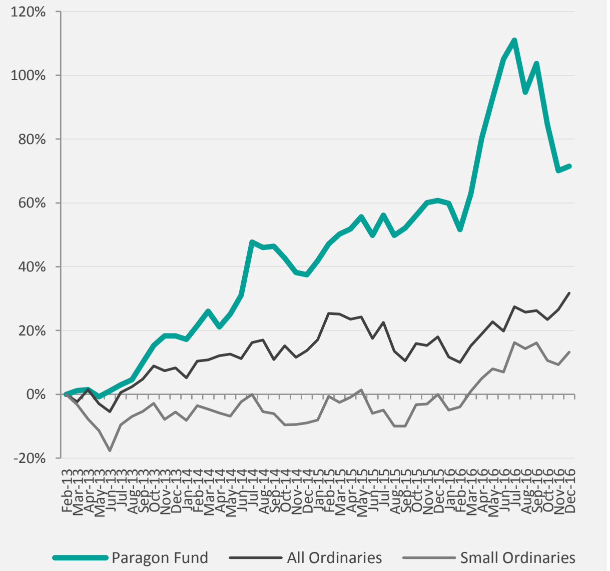
OVERVIEW & POSITIONING

The Fund returned +0.8% after fees for the month of December 2016. Since inception (March 2013) the Fund has returned +71.5% after fees vs. the market (All Ordinaries Accumulation Index) +31.7%.

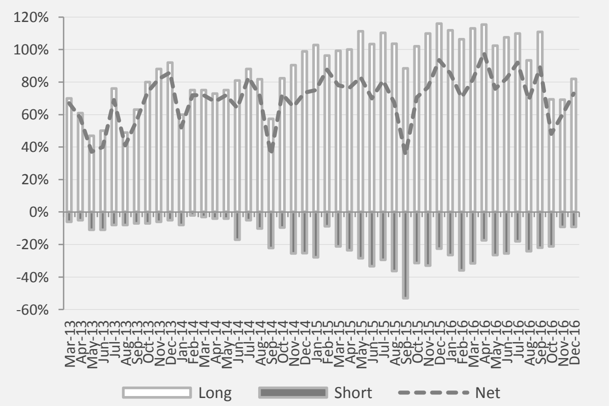
Main contributors to our positive result in December were gains in Australian banks, Macquarie and Challenger, Galaxy and Kidman Resources, offset by our short positions into a rising market. At the end of the month the Fund had 30 long positions and 6 short positions.

INDUSTRY EXPOSURE	Long	Short	Net
Financials	+21.8%	0.0%	+21.8%
Industrials	+20.0%	-7.2%	+12.9%
Resources	+40.3%	-1.9%	+38.4%
Index Futures		0%	0%
Total	**+82.1%**	**-9.1%**	**+73.0%**
Cash			**+27.0%**

HISTORICAL PERFORMANCE *(after fees)*



HISTORICAL EXPOSURE



MONTHLY PERFORMANCE BY CALENDAR 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%	2.4%	-3.8%	4.3%	-4.2%	1.6%	2.5%	2.6%	0.3%	**16.8%**
2016	-0.5%	-5.2%	7.4%	10.8%	7.0%	6.3%	2.9%	-7.8%	4.3%	-9.0%	-7.9%	0.8%	**6.8%**

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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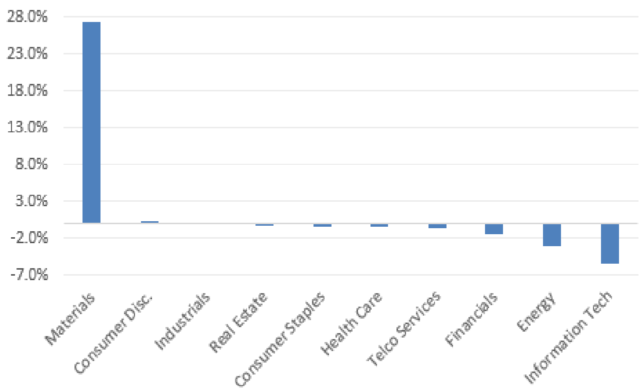
2016 CALENDAR YEAR IN REVIEW

The Paragon Australian Long Short Fund (Fund) delivered a return of +6.8% after fees for 2016, in yet another volatile year for domestic equity investors. Driven by a strong performance in the final two months of the year post Trump's Presidential election victory, the All Ordinaries Index returned +11.6%, the Eurekahedge Australian hedge fund index rose 2.2% and term deposits returned less than +3.0% for the year.

The Fund's positive performance for the year was generated from small and mid-caps - companies with market capitalisations up to $1.5b – not surprising given the outperformance of small and mid-caps over large-caps for the year. Long and pair positions drove the positive performance, while absolute shorts and SPI shorts (for hedging purposes), detracted from overall returns. Attribution from resources was the biggest sector contributor to the Fund.

CY16 Gross Performance Attribution by Sector



Our hit rate for individual stock positions (>+1% vs. <-1% in attribution) was 84%, while broadening out the sample set (>+0.5% vs. <-0.5% in attribution) provided a more disappointing 46%. Our best long performers for the year in terms of contribution to total return were Orocobre (+711bps gross), Kidman (+618bps) and Galaxy Resources (+512bps), and our best shorts were Select Harvest (+59bps) and 1-Page (+58bps). Our worst performing longs were Yowie (-188bps) and Netcomm Wireless (-154bps) and shorts were BHP (-80bps) and South 32 (-71bps).

CY16 was a year of two halves for the Fund. A strong first half of +27.8% net return, driven by gains in our resources holdings (particularly lithium & gold), was followed with a disappointing second half of -16.4%, resulting from being wrong sided by a major and rapid market turn (with what is increasingly looking like the end of the 30+ year decline in bond rates), along with some stock specific issues – as detailed in our October 2016 and November 2016 monthly reports.

What Worked in 2016

We maintained exposure to our continuing themes, many of which we've invested in since inception, as evidenced in our monthly updates over the last 4 years. A standout for 2016 is our electric vehicles theme, with strong performers in companies benefiting from the rise in lithium demand from electric vehicles. Key stock winners included Orocobre, Galaxy, Kidman and Pilbara.

A special mention should go to our investment in Galaxy Resources given the company was one of the best performing ASX300 stocks in 2016 (similar to our picks of LNG in 2014 and Xero in 2013). We first invested in Galaxy in early 2016 at $0.16/sh and have written several times about its strong investment case. We also took advantage of its price correction in August by adding to the position, as discussed in our August 2016 monthly report. Galaxy has been an exceptional turnaround story and has since commenced production at its Mt Cattlin project in WA, into a lithium bull market. As we anticipated, Galaxy has positively surprised on CY17 product pricing and likely to do the same in CY17 production volumes. Galaxy's world class greenfield Sal de Vida brine-based project (still being given next to zero value by the market) is very well placed to de-risk and secure a funding solution in 2017. Despite rerating to $0.60/sh, Galaxy remains cheap, and its global peers continue to trade at >2x Galaxy's key metrics.

What Didn't work in 2016

Most of what didn't work was largely in the last quarter of the year. The magnitude and speed of the turn in the bond market caught us wrong-footed. This rise in bond yields, amplified by Trump's surprise election victory early in November - with his substantial fiscal promises - continued to drive the rotation away from long duration, growth and gold stocks and into cyclicals. The Fund was negatively impacted as it had exposure to sectors that were suddenly out of favour, namely technology, healthcare and gold stocks.

We shorted Estia Health, Sirtex Medical, and Bellamy's during the year, having identified them as all being expensive growth stocks with issues around their outlook. All three stocks fell over 50% on poor profit results later in the year, but we had unfortunately removed all 3 short positions for differing reasons, before the truth was told.

Looking Forward for 2017

The year ahead looks reasonably balanced given the potential for improving global growth and a share market that is no longer cheap on an absolute basis but still relatively attractive compared to bonds and cash. Interest rates and economic growth will be the clear driver for investor returns this year which are again likely to be volatile. Market rotation over the last few months has begun to offer attractive opportunities in Australia within sectors and companies we feel are well placed to grow through the cycle. Several of our key theme-based stock picks are very well placed to do well over 2017, with near term catalysts anticipated to drive their re-ratings. These include companies exposed to lithium, gold, energy, sulphate of potash, the mobile internet and interest rate beneficiaries – financials.

As active managers with a flexible mandate we are well placed to capitalise on current and future opportunities. We believe the outlook for the Fund is strong and look forward to updating investors with our progress.

Thank you for your support in 2016 and we wish you a healthy and successful 2017.