



Paragon Australian Long Short Fund

January 2022

www.paragonfunds.com.au

*Since inception - 1 March 2013

PERFORMANCE DATA <i>(after fees)</i>	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	-12.8%	-11.8%	+5.4%	+3.3%	+29.0%	+25.0%	+25.4%	+11.6%	+13.3%	+204.2%
ASX All Ordinaries Accum. Index	-6.6%	-4.4%	-3.3%	-2.3%	+9.7%	+4.4%	+10.8%	+9.1%	+8.2%	+102.2%
ASX Small Ords. Accum. Index	-9.0%	-8.0%	-4.6%	-4.0%	+6.7%	+6.0%	+10.2%	+9.7%	+6.5%	+75.2%

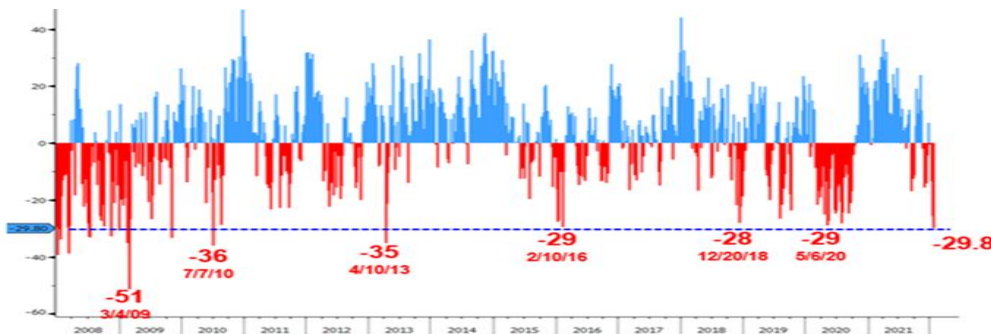
OVERVIEW

The Fund returned -12.8% after fees in January, a direct result of the violent 'risk-off' sell-off in the 2nd half of the month. Global Indices were all hit: -8.5% (Nasdaq), -5.3% (S&P500) and -9.7% (Russell2000), as were local Indices: -9.0% (Small Ords AI) and -6.6% (All Ords AI). Global markets encountered extreme volatility, initially from the ongoing sell-off in long-duration technology stocks, which then spilled over to the rest of the market after an increasingly hawkish Fed responding to high inflation (FOMC on 25th January). Political tensions between the USA and Russia over their Ukraine-invasion threats added to the volatility (although any invasion and then sanctions would be very good for Oil, Palladium and Nickel). Lithium Power (LPI) was our only real winner, along with our shorts, with the balance of the portfolio correcting amid the global sell-off.

Rising rates environments favour value, cyclical, and resources stocks, where the latter in particular act as a great inflation hedge. Strong absolute and relative outperformance from resources can be seen in various historical examples including the 1970's and 2002+. In addition, in every rate hike cycle since 1972, commodities have returned +19% and outperformed the S&P500 by +9%. As discussed in our monthly updates and recent webinars, over the past 6-9mths, we have been actively decreasing exposure to technology stocks and increasing exposure to resources including nickel and 'old-energy' oil.

Investor sentiment at the end of January was at historic pessimistic levels (see chart 1 below by Fundstrat) and at extremely oversold levels - rivalling both the 4Q18 Fed-driven and 1Q20 Covid-driven market bottoms. Whilst we're aware of the nervous narrative around the Fed possibly making a monetary policy error (by going too far with cash rate rises and QT), they haven't done anything yet and are still printing money until 30 March 2022!

Chart 1: AAII % bulls less % bears sentiment survey – current sentiment is top 5 worst since 2009



2022 Outlook: Strong micro factors from de-carbonisation to outweigh macro concerns

In our latest [quarterly webinar](#), we discussed our Fund's deliberate high net-exposure with the intention to capitalise on the supercycle underway in the resources sector. Whilst we're expecting volatility this year due to the macro concerns outlined above, these will be significantly outweighed by the globe's decade+ long micro drivers from de-carbonisation and electrification (see chart 4 overleaf). Investment here will likely be >US\$2t/yr, representing strong tailwinds this year. Despite the current sell-off, battery-EV minerals fundamentals are strengthening. Lithium prices continue to accelerate and breaking records of US\$52,500/t+, Nickel is at 11-year highs of US\$22,000/t (see chart 2 overleaf) and NdPr Rare Earths price is at 10-year highs of US\$130/kg (see chart 3 overleaf). Given the outlook for long-term material deficits, high prices for these commodities will remain for some time and will drive an ongoing major M&A cycle. During the sell-off we happily added to our position in LPI which arguably has the best (highest grade) conventional Lithium-brine development asset globally. Remarkably, it still trades on a modest P/NPV of 0.25 and has near terms catalysts to drive its ongoing re-rating. Finally, whilst already the largest single investor in the Fund, John Deniz will be re-investing all of his after-tax proceeds from the performance fee just earned.

FUND POSITIONING & RISK METRICS

Fund Size	\$54.3m
Longs	28
Shorts	10
Net exposure	97%
Beta-adj net exposure/ Average (rolling 12mths)	80%/93%
Gross exposure	149%
Cash	3%
Index Futures	0%
Correlation	0.52
% Positive Months	61%
Up/Down Capture	113%/72%
Liquidity (% saleable inside 10BD)	84%

UNIT PRICING

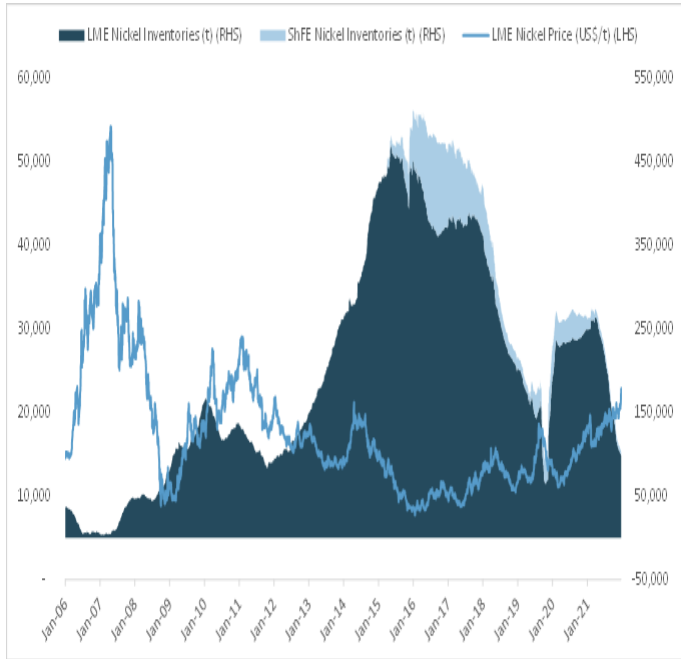
NAV (Mid-Price)	\$2.4813
Entry Price	\$2.4851
Exit Price	\$2.4776

FUND FACTS

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

Chart 2: Nickel price strengthening as inventories deplete towards critical levels.

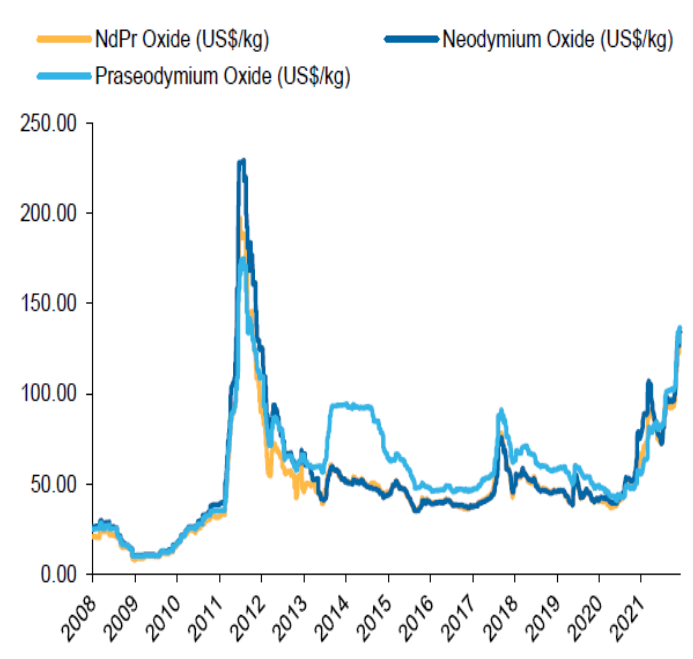
Contracts for immediate delivery are trading at a US\$508/t premium to those in three months, the highest premium since a historic squeeze in 2007. 2007 supercycle redux?



Source: LME, Euroz

Chart 3: Key rare earth NdPr prices at 10yr highs. NdPr prices increased 45% in the 4Q21 to US\$133/kg, following a 26% rise in 3Q21.

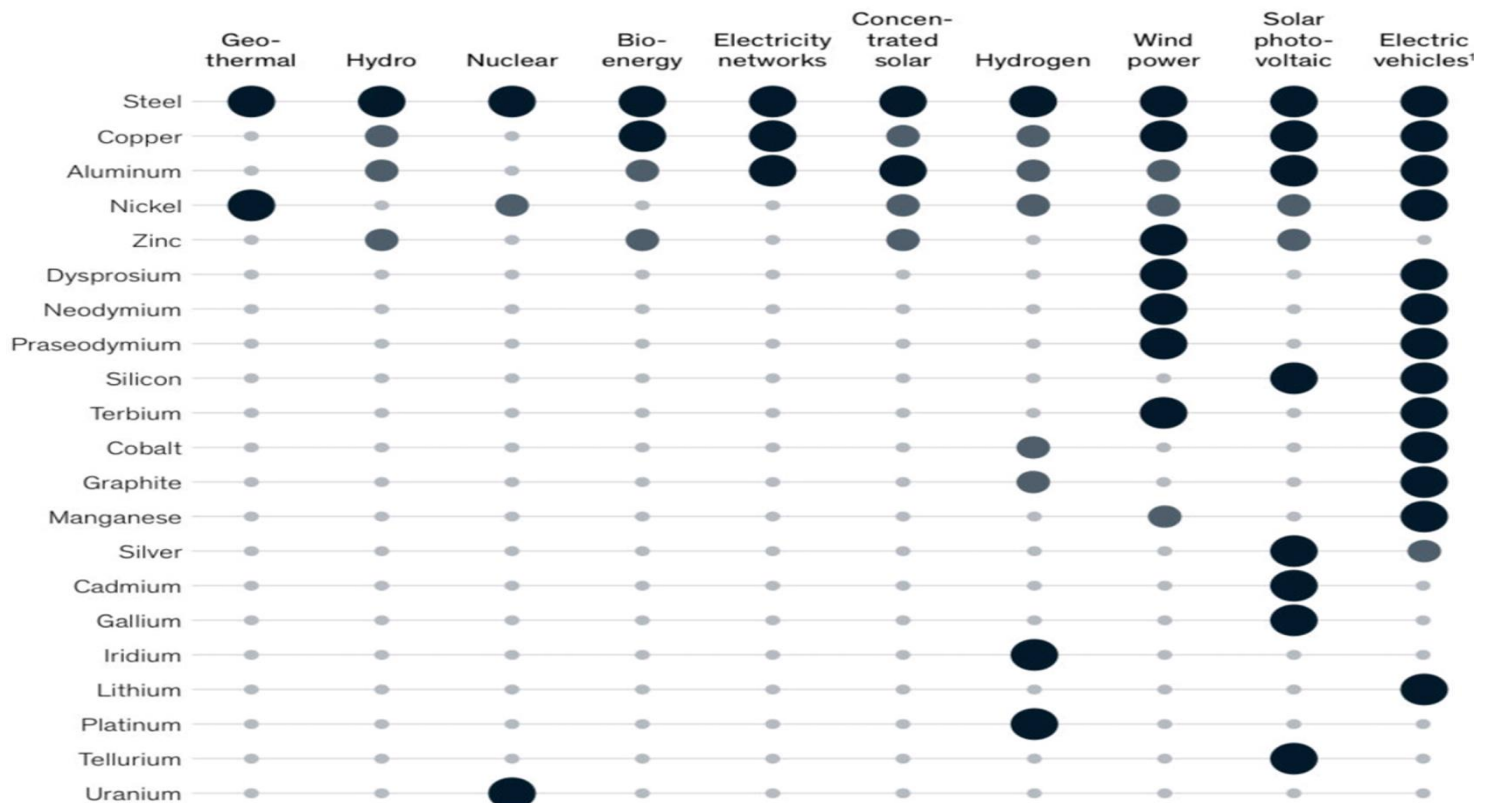
NdPr deficits are growing despite China's recent increase to its CY22 rare earth production quotas by 20% for both mining and refining. A much bigger supply response is needed.



Source: Macquarie Research

Chart 4: Materials critical for decarbonisation transition (where large and dark bubble size denotes high importance).

With limited capital and our concentrated positioning, it's hard to be everywhere, but this chart shows clearly why we're bullish long-term on Lithium, Nickel, Copper, Rare Earths NdPr, which are in high demand across so many verticals such as EV, Solar, Wind power generation and Hydrogen.



Source: IEA, McKinsey

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