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RECOVERY FUND 2018 THIRD QUARTER UDPATE

Recovery Fund fell 1.1% (net) in Q3 2018 and ended the period down (3.6%) year-to-date. With October off to a perky start, an investment since the fund's inception six years ago returned 6.4% net (as of October 9th) trouncing the HFRX Equity Hedge Index—but trounced by the S&P 500 total return.

	2018				Annualised Returns		Since Inception
	Q1	Q2	Q3	YTD	3-year	5-year	6-year
Eschler Recovery Fund - NET [1] [3]	-11.2%	9.9%	-1.2%	-3.6%	18.4%	6.1%	6.0%
HFRX Equity Hedge Index[2]	1.0%	1.0%	-0.7%	-1.4%	3.2%	2.4%	3.2%
Russell 2000[2]	-0.1%	7.8%	3.6%	11.5%	16.9%	11.1%	13.9%
S&P 500[2]	-0.8%	3.4%	7.7%	10.6%	17.1%	13.9%	14.5%

(1) Results are for an investor since inception in B share class, net of all fees with a "high watermark" threshold.
(2) S&P 500 & Russell 2000 indices include reinvested dividends. HFRX Equity Hedge Index (HFRXEH) on Bloomberg.
(3) 2012 results are for 3 months (8/10/12 - 31/12/12).

The tame return in Q3 belied fierce moves at the industry level. The big story of Q3 was opposing moves in the precious metals shares, on the one hand, and energy/uranium shares on the other. The precious metals book fell 11.7% (return on average capital) outperforming the Gold Bugs Index (HUI) down 19.2%; and the energy/uranium book rose 22.7% crushing both the Oil Service index (OSX) -3.5% and the Global X Uranium ETF +3.4%. During this tough stretch for the precious metals book the negative correlation with energy/uranium was an unexpected gift.

Top 5 Q3'18 Returns		Bottom 5 Q3'18 Returns	
Goodwin Plc	+50%	Agnico-Eagle	-17%
Energy Fuels	+45%	Fortuna Silver Mines	-23%
Now Inc.	+24%	First Majestic Silver	-26%
Tesla short	+18%	Continental Gold	-29%
Pharma Bio-Serv	+44%	Sandstorm Gold	-10%

The price of vanadium oxide (V2O5), a compound of vanadium (23 on the periodic table) used to strengthen steel, has increased 264% YoY to $27/lb in China. V2O5 is also a key input in energy storage with Vanadium Redox Flow Batteries or (VBRs) used to store wind and solar power. Fund holding Energy Fuels Corp. traditionally mined vanadium as a uranium by-product. 4 million lbs of the stuff sit in pond solutions at the company's White Mesa mill in Utah, the only permitted mill in the U.S. with a vanadium circuit. V2O5 is 5x more prevalent in Energy Fuels' mines than uranium itself but was not economic as a standalone activity until now. Energy Fuels now has a window to generate bonanza profits over the next few years, first by extracting the V2O5 from the ponds and second by upgrading the La Sal Complex mine plan to mine out the neglected zones with highest vanadium content. The cost of producing vanadium ranges from $3.57/lb (Largo Resources) on the low side to $12/lb for high cost producers, with an incentive price for new capacity of $10/lb. For the next 16-20 months Energy Fuels will be producing 200,000 – 220,000 lbs of high-purity (premium-priced) V2O5 from the ponds, to be followed potentially by larger scale conventional mining once a just-commenced six-month pilot is complete (the company has M&I reserves of 31 million pounds worth 2.6x the current $315 million market cap at spot prices). This extra $3-4m of initial monthly cash flow is a welcome boost as we wait for spot uranium to rise above production cost. When it does, Energy Fuels will (a) still be around given by far the strongest working capital position amongst peers even before considering the vanadium cash flow and (b) be exceptionally well-positioned to capitalise on the uranium upcycle with >4 million pounds per year of capacity ready to go within 12 months of a production decision. Up 92% over the past several months since purchase and now 7.8% of NAV, I am hanging on to Energy Fuels shares for dear life.

Like late 2015, precious metals shares are in the dumps. Prices in the industry are back to the same eye-catchingly low levels of three years ago, reflecting the value destruction of the past cycle and a complete disinterest by mainstream investors in contrarian investments. That period while uncomfortable created the dynamic for 2016, a great year for the fund. If history rhymes, these shares are due some serious catch up. A recent pick up in M&A suggests it is again cheaper to buy than build. Share price recovery may not ensue immediately. But when it does the move will be violent and without warning. It may happen as broader markets stall out. Having a full position ahead of time will be imperative.

Today's precious metals book has somewhat less optionality than back then (fewer developers) but equally strong risk-reward (less downside if I'm wrong). Core positions have a lot more going for them than just the gold price, in particular production growth and exploration upside. As compared to three years ago, fund holdings in this industry sport more robust business models (two of the largest are "royalty" models with high margin and ROIC), balance sheets and cash flow generation. This implies a narrower range of up- and downside scenarios, but equally attractive risk-reward.

I am optimistic about the fund right now, just like I was three years ago. Back then I found few takers. This time around, it remains to be seen whether more curiosity surfaces to displace what has been stubborn disinterest in these themes.

I am pleased to welcome to the office Mark Walker of Tollymore Investment Partners LLP and Christian Putz of ARR Investment Partners Ltd., both independent emerging managers for which Eschler is acting as the regulated AIFM. Mark runs a long-term, concentrated, bottom up equity strategy. Christian runs a global thematic equity long-short strategy. Both have impressive multi-year trackrecords. It's good to have a bit more company around here and I look forward to sharing resources and ideas with them.

Theron de Ris
Portfolio Manager
10 October 2018