Eschler Asset Management LLP

www.eschlerasset.com

Dear Partners,

Eschler Recovery Fund (ERF) fell 10.7% net of fees and expenses in 2018 in U.S. Dollars (B share class). Over the past three years this is still well ahead of U.S. equity total return and hedge fund benchmarks. Moving forward my goal is to achieve a double-digit net annualised return since inception. What is the score in Sterling and Euro terms? Below are ERF returns net of all fees and expenses in U.S. Dollars, Sterling and Euros compared to relevant total return benchmarks (in local currency). The reason returns look better in Sterling and Euro terms is that these currencies have depreciated vs. the U.S. Dollar. If this situation reverses in coming years rest assured I will be doing my best to ensure that the fund's U.S. Dollar returns speed ahead of a falling U.S. Dollar!

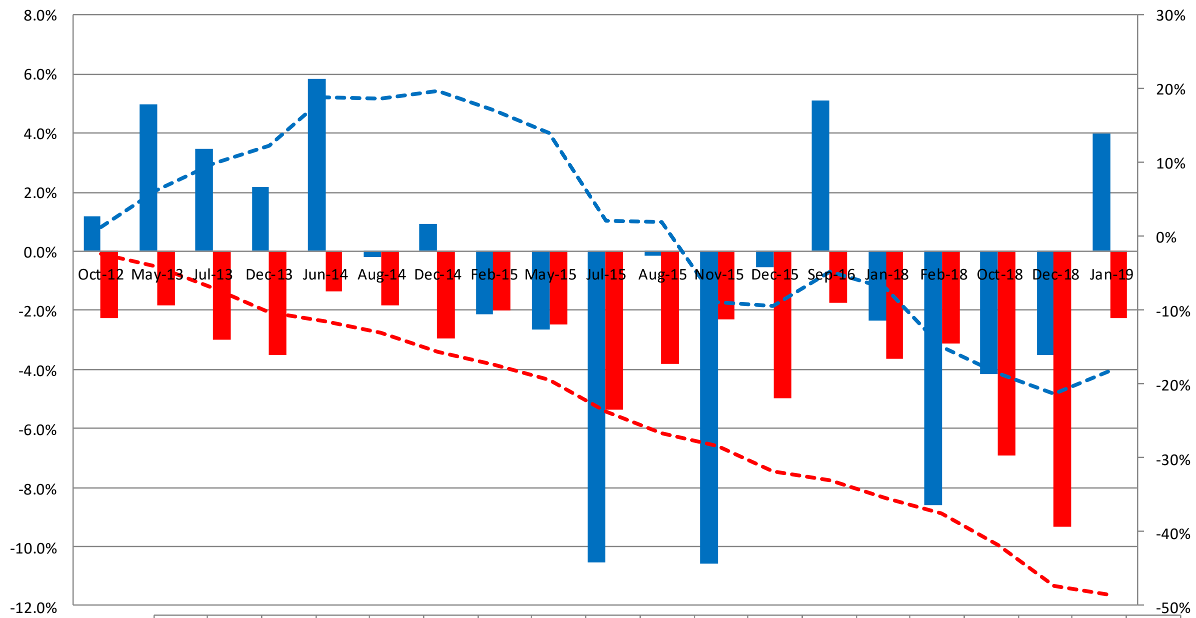
		Annualised Net Total Returns		
				Inception[3]
	2018	3-year	5-year	(8 Oct 2012)
Eschler Recovery Fund - NET USD[1]	**-10.7%**	**10.3%**	**3.9%**	**4.5%**
HFRX Equity Hedge Index USD	-9.4%	-0.9%	-0.3%	1.6%
Russell 2000[2]	-11.0%	7.3%	4.4%	9.3%
S&P 500[2]	-4.4%	9.2%	8.5%	11.3%
Eschler Recovery Fund - NET GBP[1]	**-5.4%**	**15.7%**	**9.4%**	**8.5%**
HFRX Equity Hedge Index GBP	-3.9%	4.9%	5.1%	5.6%
FTSE AIM All-Share[2]	-17.1%	6.6%	1.6%	4.5%
FTSE All-Share[2]	-9.5%	6.1%	4.1%	6.7%
FTSE 100[2]	-8.8%	6.8%	3.9%	6.1%
Eschler Recovery Fund - NET EUR[1]	**-6.5%**	**8.4%**	**7.7%**	**6.7%**
HFRX Equity Hedge Index EUR	-4.9%	-1.8%	3.5%	3.8%
Euro Stoxx Small Cap Index[2]	-13.2%	2.5%	4.2%	7.7%
Stoxx Europe 600 Index[2]	-10.3%	0.7%	3.9%	6.8%
Euro Stoxx 50 Index[2]	-11.3%	0.7%	2.9%	6.4%

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

…………………………………………………

ERF continues to own a small collection of businesses in industries whose entire market has contracted 70%, 80% and even 90%+ from the highs of the past decade. To add insult to injury, these industries kept right on falling last year: As a group, gold stocks fell 15.8% (HUI Gold Index), silver stocks fell 22.4% (Global X Silver Miners ETF), uranium stocks fell 22.1% (Global X Uranium ETF) and oil service stocks fell a whopping 45.2% (PHLX Oil Service Sector Index)! These four areas comprise over three-quarters of ERF's net asset value, spread across 24 securities.

Last summer I gave a talk at the Value Investing Seminar in Trani, Italy (co-hosted each year by Ciccio Azzolini and Whitney Tilson) on this very subject of investing in cyclical industries. ERF's investment in gold-related stocks, featuring prominently in the above talk, comprises half the current portfolio. I still see this holding as a useful alternative to more traditional hedging approaches such as holding a lot of cash, running a large short book or buying put options. One outcome of this equity asset allocation is very low correlation (<15%) with the stockmarket. Compound ERF's returns in all months that the S&P 500 fell more than 1% and, compared to the S&P 500, one would be left with over 60% more capital. It looks like this:



	Oct-12	May-13	Jul-13	Dec-13	Jun-14	Aug-14	Dec-14	Feb-15	May-15	Jul-15	Aug-15	Nov-15	Dec-15	Sep-16	Jan-18	Feb-18	Oct-18	Dec-18	Jan-19
ERF NET	1.2%	5.0%	3.5%	2.2%	5.9%	-0.2%	0.9%	-2.1%	-2.7%	-10.5%	-0.2%	-10.6%	-0.5%	5.1%	-2.3%	-8.6%	-4.1%	-3.5%	4.0%
S&P 500	-2.3%	-1.9%	-3.0%	-3.5%	-1.3%	-1.8%	-3.0%	-2.0%	-2.5%	-5.4%	-3.8%	-2.3%	-5.0%	-1.7%	-3.6%	-3.1%	-6.9%	-9.3%	-2.3%
Cumulative	1.2%	6.2%	9.9%	12.3%	18.8%	18.6%	19.7%	17.2%	14.1%	2.1%	1.9%	-8.9%	-9.4%	-4.8%	-7.0%	-15.0%	-18.5%	-21.4%	-18.2%
Cumulative	-2.3%	-4.1%	-7.0%	-10.2%	-11.4%	-13.1%	-15.6%	-17.3%	-19.4%	-23.7%	-26.6%	-28.3%	-31.9%	-33.1%	-35.5%	-37.5%	-41.8%	-47.3%	-48.5%

....

By major category ERF's largest contributors were shorts, uranium shares and the sole private investment, MDNA Life Sciences (formerly known as Mitomics and finally hitting huge milestones.) On the negative ledger, gold and silver shares, oil services shares, Biglari Holdings and Bank of Cyprus detracted the most. Biglari Holdings fell 59% last year, in what can only be described as comeuppance for the company's sole capital allocator, Sardar Biglari. I am betting that Mr Biglari's pride and competitive spirit compel some sorely lacking shareholder-friendly decisions very much within his control.

The ~19% stake in Cracker Barrel alone is now worth over twice Biglari Holding's market cap and there are other assets of varying quality to boot. Bank of Cyprus fell 54%, right along with the risk of holding the shares (at least in my view) which now trade at 0.24x book value and 3-4x run-rate earnings (6-8% RoE).

……………………………………………

The top ten holdings in the fund are now: Sandstorm Gold, Abitibi Royalties, Goodwin Plc, MDNA Life Sciences, Agnico-Eagle, Energy Fuels, Buenaventura, Altius Minerals, Now Inc. and De La Rue Plc. I'm very excited about the free cash flow generation potential and stewardship of these companies.

……………………………………………

Each January, courtesy of Professor John Hussman I re-read "*Loving Your Enemies*" by Martin Luther King Jr (included with his January Market Comment.) It's a hard subject but a useful path for humanity. Conventional wisdom has it that bear markets are the enemy of investors' well-being. On the contrary, for the disciplined long-term investor the opposite is true. "*You make most of your money in a bear market, you just don't know it at the time*" said the late Shelby Davis. But none of this stuff is easy! To nourish my inner stoic last year I read some of Seneca's musings, heard Jordan Peterson's lecture at the Cambridge Union and watched Mohnish Pabrai's wonderful The Ten Commandments of Investment Management.

Here are some of Eschler's core tenets:

Value Approach: The only reliable statistical exceptions to the Efficient Market Hypothesis are the excess returns displayed by small caps, value and momentum. The latter is not for me so I stick with small cap value. Forecasting the future is a fools' errand but a good price, made possible by Mr Market's occasional moodiness, can protect against the risks arising out of false precision. I've been known to occasionally use a spreadsheet but wholeheartedly agree with Mohnish Pabrai's Commandment Five: "*If the idea requires Excel, it's an automatic pass!*" They don't reveal themselves all too often, but when they do true bargains should be obvious.

Contrarian: Choosing to run an active, long-term, deep-value, public markets strategy is itself contrarian in today's market. But when looking for value in under-the-radar cyclical areas, acting contrarian is mandatory. For me, being contrarian in today's market means, for example, avoiding large swathes of the US stockmarket. The number of US-listed companies has fallen by half over the past 20 years while the number of professional investors has skyrocketed. One result is that the Russell 2000 trades at over 50x trailing GAAP earnings per share including the loss-making constituents that comprise 1/3 of the index.

Long-term: Akin to the private equity approach I aim to own businesses for three to five years or longer. Indeed a seven-year time horizon would invite even less competition but, like loving your enemies and loving bear markets, this is much easier said than done. The merits of deploying long-term capital in the public, as compared to private markets include better liquidity, lower fees, less leverage and more transparency. The public market investor can also use market volatility to his/her occasional advantage and can make up for a lack of control by partnering with founders and owner-operators instead of hired guns.

Alignment: I agree with Mohnish Pabrai's Commandment One: *Thou shall not skim off the top.* I'm always looking for company managements that have the same type of skin in the game that I do. Their behaviour tends to be better and one can learn by observing their capital allocation skills. I beneficially own 14,294 shares of ERF comprising ~28% of the fund and largely my entire liquid net worth outside of property. ERF Management fees have averaged well below 0.5% of average net assets over the last two years (and zero before that).

....

My fellow director Casey McDonald and I are very pleased to welcome four new investors into the fund over the past year. There are now 14 entities invested in the fund. I'm hopeful that the 15th investor will significantly increase fund assets in coming months and put us on a trajectory for growth. The 15 investor mark will necessitate re-registration with the Cayman Monetary Authority. One unintentional consequence of this is that all investors in the fund will be required to have subscribed the minimum US$ 100,000. The fund remains open for subscriptions on a monthly basis and we look forward to welcoming new investors over time. With Reporting Fund status the fund is currently available to UK-resident investors as well as offshore and US tax-exempt investors. The annual audit will be posted to the portal shortly.

On the business side I'm extremely pleased to announce that John Pryce-Robertson will be joining Eschler as Chief Operating Officer from 1 February 2019. John brings an excellent skill set to the role and will be instrumental in ensuring our infrastructure supports growth. With a solid six-year trackrecord, in-house fund structure and AIFM, regulatory platform and a solid introduction network we are looking forward to the future.

I would like to extend my gratitude to my colleagues in the office, Mark Walker of Tollymore Investment Partners, Christian Putz of ARR Investment Partners and Mikael Henriksson of Cognition Investment Partners, as well to Richard Rothwell for his counsel and my wife, Dr Lara Eschler de Ris. I look forward to and am grateful for our continued partnership.

Theron de Ris
London, UK
24 January 2019