Report
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Fragments

"Investment is the activity of forecasting the yield of an asset over its whole life; speculation is an attempt to forecast the psychology of the market." This classic quote from J. M. Keynes gave rise to a tradition of positive reflections on the possible ways of classifying investors in the vast ecosystem of the markets. Such a schematic distinction of the two large groups has weathered well over time and is still appropriate.

On the one hand, there are those that see asset prices as an end unto themselves. Being the only reality that matters, price is, at the same time, the origin and the final record of any trade. It determines the *raison d'être* of all the efforts in the market: the search for arbitrage opportunities. With this, it is up to the participant, as a valid strategy, to seek out clues that may hint at price trajectories. The tools could be graphs, quantum algorithms, flows or inferences on the psychology of other participants. In the other group, prices are seen as epiphenomena. They reflect the hidden instances that actually determine them. Prices are hyperlinks that provide access to the immense reality of the fundamentals. Here, what truly matters is the value of the assets, which can be examined through several lenses: different timeframes, a macro or sectorial approach, competitive environment, focus on companies and their numerous domains – management, strategy, people, technology, incentives, contracts, and so on.

As our readers know, Dynamo is a specie integrant of this second group which includes a broad category of the so-called *value investors*. And, for us, the more granular our analysis is, the more attainable the value of the companies will be. The more we travel the rugged trail of knowledge in the varied instances that make up the apparently invincible reality of companies, the closer we will be to the source of fundamentals: where insights on value are born, where price behaviors are determined.

The narratives throughout our Reports reflect these principles. Generally, they are texts in which we choose a central argument to focus on and, whenever possible, dive deep into. In this edition, we are going to stray from this standard. Although we have identified common roots and connected elements, we prefer to contemplate several aspects of the ecosystems of companies. These are fragments of observations across multiple domains. What might justify our divergence is that, with this more aggregated approach, we have identified a magnitude of unprecedented transformations taking place in the orbit of companies. The presumption is that the "cubist" approach of the whole can provide a different perspective, comprising elements and making our standard meticulous and segmented analysis more robust.

Competition is characterized as the dispute for preferential access to scarce resources and by the need to outdo the strategies of rivals. The fight for survival and control instigates change on every level, posing a continuous challenge to adapt. The corporate environment emulates the evolving mechanisms in living systems. With this, in its nature, it is behaving like an essentially dynamic process.

In a true capitalist regime, these gears never stop turning. They are always moving, which is intrinsic to the system. As observers of the corporate environment in Brazil over the last thirty years, we have recently noted important changes taking place.

Up until quite recently, companies here were used to more predictable competitive environments. A complex doing business environment, with excessive norms and levels of regulation, wound up offering additional protection to incumbents, toning down entrepreneurial activity and insulating the country from foreign competition. In such an environment, change happens more slowly. Markets remain closed and protected, restricted to a reduced number of known participants, whose strategic movements can be predicted by the competition without too much effort. This is similar to a game of checkers, where the reduced scale of valid initiatives makes the dispute more predictable[1].

For consumers/clients, we also saw a more pacific relationship from a corporate viewpoint. Companies used to dominate the channels of communication for products and to control access to communication tools. Consumer preference seemed well mapped out and domesticated by the marketing and advertising initiatives. So strong was the trust in dominating consumer attitudes that marketing campaigns were designed to run throughout the whole year and were only revised in the following period. Companies set the trends, influenced choice and managed to keep clients in their captive territory. If preferences – which are notably more instable and unbridled – have been well established, there is little left to say about the values that determine them and which are longer-lasting.

Internally, the standard company organization reflected this more stratified world. Rigid and hierarchical structures, centralized regimes of command and control, vertical company structures, compartmentalized office spaces, standardized career plans, meritocracy based on seniority. Guidelines from "strategic planning" ran a long path, seeping down through the several managerial layers, but the distributed intelligence information flow from the base almost never beat gravity in the opposite direction. In a more controlled environment, the speed of answers with perceptions of the collaborators at the edge of the organization or of the end-client's experiences was not a priority. Management techniques developed in the past, such as Total Quality, Zero-Base Budget and PDCA (plan, do, control and act), were often recycled, but always within the same scope of linear management and top-down processes.

As a logical outcome of the combination of these and other elements – a closed country, protected markets, oligopolies, scarce capital, a contained entrepreneur spirit –, we lived in an environment of smothered competition and very little innovation, where changes were discreet, slow and more predictable.

More recent events have been the catalyst for important changes that today draw a very different picture of the reality described above. The arrow of time seems to have sped up, and phenomena that have taken place over the last five years have brought about change in the corporate environment that were unheard of in the previous thirty years. In a schematic format, we have grouped these elements into two broad categories: "digital transformation" and "pandemic." Due to a lack of inspiration, we acknowledge that the denominations are not precise and require some qualification.

"Digital transformation" has become a household term. In fact, it is a phenomenon that has taken on multiple forms and manifests itself in a myriad of domains. We have covered several specific aspects in many Dynamo Reports. We spoke of digital transformation as an extraordinary advance in digital technology, notably in terms of processing capacity and traffic infrastructure which favors the creation of an interconnected world (Dynamo Report 94). We also focused on digital transformation in terms of a rationale for structure, dynamics and properties networks (Dynamo Report 95). We covered the business model that incorporates the more accentuated expression of digital transformation in the corporate environment: the platform-based companies (Dynamo Report 96). We described the challenges that long-term investors face, when analyzing companies, run under a digital transformation model, illustrating the *Mercado Livre* case (Dynamo Reports 97 and 98). We dissected the technical metamorphosis along the tortuous pathway of digital transformation for companies related to both the IT structures and the route towards cloud computing (Dynamo Report 106), and finally we considered how digital transformation can help companies overcome their natural growth limits (Dynamo Report 108).

Now, we are going to look at digital transformation as a way in which integrating digital technology affects the diverse corporate realities, resulting in fundamental changes in the way companies operate and deliver value to their clients.

"Pandemic" is a term that is even more imprecise. We also covered specific aspects of the virus, the desease and the epidemiological perspective (Dynamo Report 102). Now, "pandemic" represents the cognitive, behavioral, psychological and social impacts on the lives of people we have seen over the last extraordinary and surprising year. All this, naturally, under the restricted view of the corporate reality. So, we will be considering individuals as consumers, collaborators, suppliers and shareholders. The prolonged confinement, living with uncertainty, the concern for health and employment, the mandatory eye over the other (which

1 *Unfortunately, in terms of facilitating within the realm of business, progress was much slower than we would have liked, and today we still pursue an agenda of basic and fundamental micro-economic reforms for the country. In the macro sphere, however, we are well aware that frights and uncertainties are never scarce. We have suffered, and continue to suffer, due to not only the over-sized ripples from foreign crises, but also to our own political-institutional immaturity, to chronic fiscal fragility, and to the perpetual distrust in the ability of our currency to absorb all these shocks.*

can save or infect you). All this helped our deliberations mature and paved the way for initiatives. It is no wonder that, for example, there is more concern for the effects of negative externalities from company activities, when climate, biodiversity and inequality issues finally take on the relevance they deserve.

The script for this Report, therefore, is less ambitious. We lay out how, in our opinion, the combination of these two groups with elements of a specific nature, but which come together and intertwine, instigates important changes to several aspects of company's life and to the ecosystem surrounding them. We have never seen such a broad spectrum of fundamental implications taking place at the same time. As a result, the challenge for long-term investors that need to assess the intensity of the resulting force of this new imbroglio is both immense and unprecedented.

Client/consumer Dimension

Changes in consumer preferences are evident and present in several aspects: what they want to consume, how they consume, where they want to consume, why and if they want to consume. In keeping with empirical evidence and behavioral studies, in environments with more uncertainty and fear, individuals become more conservative when prioritizing their needs. As a reaction to the pandemic, before government cash transfers landed in their pockets, people began consuming more essential items and reducing their consumption of accessory items. They became more selective, more sensitive to price and availability. Impulse buying also tapered off, since this type of behavior is more common in brick-and-mortar stores than in digital marketplaces. In addition, the risk of infection and the lockdown brought about an unprecedented fall in physical interaction. Avoiding personal contact, consumers favored those that could offer alternative channels to meet their demands, as well as hygienic and safe choices when buying. The combination of unique elements led to an unprecedented acceleration in online shopping and, at the same time, a blend of online and offline channels, the so-called omni-channel. The retail sector made an attempt to increase their online growth in a few months which had been on hold for at least 10 years. Never, in such a short period of time, had such a broad range of modalities been made available to facilitate shopping: delivery, drive thru with online booking, online order and curbside or store pick up (click-and-collect), online purchasing with in-store exchanges, online order served by exclusive in-store products, in-store customers having access to the entire online assortment (infinite shelf), shipping from the store, research/personalized service in-store and online shopping, online purchasing and sales in-store, and so forth; even groceries were being sold via WhatsApp.

As a result, trends underwent a change that the consumer market had never seen. More supermarkets, fewer restaurants. More household items, less outdoor fun and leisure. More car travel, fewer flights. More online courses, more telemedicine. Even within some segments, like cosmetics, preferences changed: personal care increased, while interest in make-up dropped. Brand loyalty took a beating. Research has shown that 75% of North American consumers shopped in a new store, bought a new brand or tried a new method for shopping throughout the pandemic.

An additional challenge for companies is that this sudden change and the sheer variety of consumer preferences has taken place at a time when the digital aspect has radically transformed the brand-customer relationship. The traditional mono-channel, in which the owner of the brand had exclusive content and control of the one-directional communication, was surpassed by not only the multiplicity of the social media platforms, but also the unprecedented granularity of targeted publicity in digital marketing, and by the reality of the endless aisle in e-commerce. The essence of the communication model changed. Brands that insisted on the previous model of controlling the content of the message are at risk of becoming unauthentic and losing their reach. In the interactive environment, brands must necessarily accept some level of flexibility as a part of the effort to remain relevant today. Communication is no longer a one-way street and has become a dialog. In some cases, it has evolved into a social dimension, in which companies are able to help shape the communities around their products, which generates a feeling of belonging, increasing the loyalty of each individual consumer.

The science of psychology teaches us that, under normal conditions, values and beliefs shape behavior and consumption patterns. In atypical situations, the direction of causality can be inverted and new positive experiences can eventually change the way we think and perceive reality. The pandemic and the digital experience have sparked new routines and habits that, if they become permanent, will offer a horizon of opportunities to companies. Studies show that consumers have positively assessed online shopping experiences in new categories and that, when consumers start buying a category online, their behavior becomes more predictable. Once online, companies that are able to increase their engagement will gain a more loyal consumer. Not to mention the superior economics that comes from increasing engagement, which generates a better ratio between lifetime value and acquisition costs. It is a unique moment that offers companies the opportunity to position their products/brands in such a way as to reinforce and shape behavioral trends that may perpetuate when the event that gave rise to them, in this case the pandemic, is no longer around.

Internal Organization Dimension

The digital transformation has generated deep change in the internal organization of companies. The pandemic has contributed to confirming patterns that are now clearly recognized, at the same time it has helped accelerate trends that had only been in the planning. The changes reverberated across all spaces within the companies and became visible in a myriad of ways. In a simplified fashion, we have chosen to illustrate this in three strains/categories (priority, structure and arrangement) which express these repercussions:

(i) Priority – Client/Consumer Centricity

It has become commonplace to affirm that companies had shifted their business models from the inside out when consumers began to take on the main role in the strategic priorities of executives. In reality, this is a direct result of the transformations we mentioned above. At a time when companies have lost control of the distribution channels and communication tools, coinciding with the moment when consumers have realized their range of choice can be met by a much broader variety of brands/feasible suppliers, there is no alternative for companies other than to recover the direct connection with their clients investing in relationships and knowledge. Within this environment, the balance of power has swapped hands. Companies are chasing empowered customers, invariably competing to offer the more appealing proposal to consumers. On the other hand, they are trying to establish new fidelity connections and preferences pursuing a business model that promotes recurring revenues. And thus, and it could not be otherwise, the consumer experience has ended up driving and shaping all internal activity. If clients' more in-depth understanding has become the underlying script in modern competition, the pandemic, by shaking up individual preferences, has made it even more difficult for companies to correctly read and establish the most appropriate position.

There is a subtle aspect that is overlooked by those that see "client priority" as a mere buzzword. Strictly speaking, digitalizing means converting analogic information using electronic devices to make it processable, storable and transmittable via circuits, equipment and digital networks. As the basic unit of work in digitalization is information, the danger in this venture is to treat the whole process as a matter that is exclusively technical, restricted to trade-offs inherent to the decision to adopt a new technological standard. We are not underestimating the functional relevance of these workings, as we meticulously investigated in Dynamo Report 106. That is not the case. It is that, along with the technical/quantitative repertoire, "consumer priority" summarizes the human aspect that triggers and influences the digital route. The aim and premise of the digital course consists of using technical tools to learn and understand, to establish trust and empathy, to enchant and empower. When humanized, the reach of digital technology does, in fact, become unlimited. It is no wonder that, in our understanding and as an example, Natura has made some remarkable progress in its digital journey.

(ii) Structure

Migrating the technological structure to the cloud, developing systems and apps, integrating digital tools into the logistical and distribution processes, and redefining the concept of physical spaces are examples of changes that are taking places in the internal structures of companies. Each of these projects alone is seriously complex, while they all simultaneously pose a massive challenge when it comes to performance. Companies are being forced to experiment transitions phases, as we had pointed out in Dynamo Report 104. These are moments that are perfect for revealing fundamental instances for long-term investors.

A basic step in this strategy consists of integrating software development into technology support operations and customer service. More than just a functional improvement, it is about promoting a reshape of organizational structures and operational models at companies, which some consider a true cultural transformation as it suggests a change in the mindset and a way the get rid of internal silos. As we outlined in Dynamo Report 106, it is necessary to migrate from a model in which the technology team is seen as being responsible solely for support operations and managing equipment, to being considered a cost center under the budget of the financial director. In the updated design, members of the technology group are transformed into software developers that write apps together with those responsible for operations, comprising a multi-functional team that is also charged with implementation and plays a central role in growing the company. The cloud environment requires this integrated operational model, which simplifies processes and tasks, fosters faster implementation, and allocates resources more efficiently, besides reflecting a faster time to market. Another documented outcome is that this model increases the effectiveness of the teams that are more familiar with the product and that better understand the company's position in the market.

(iii) Arrangement

Companies had already begun to see the value of a more horizontal organizational structure, less hierarchical, assembled in decentralized teams with effective decision-making powers, as a better design, capable of fostering agility that is so desperately needed in the current competitive arena. In Dynamo Report 96, on platform-companies, we noted: *The modern digital world has been transforming the behavior of individuals in all relationship dimensions: personal, familial, social and, of course, professional, with ramifications on companies' culture. There are several vectors that influence this change. The focus on the client makes companies turn outward, rather than inward. User experience shapes and guides internal activities. Information and knowledge start to travel on a two-way street between employees and customers. The network environment, by definition, is less hierarchical. The graphical representation of these networks are circles, where vertices (members) are pairs. Organization charts are more horizontal. When information flows in real time, the hierarchy collapses. The command-and-control structure is justified only in the presence of asymmetry of knowledge.* The arrival of the pandemic highlighted the importance of a swift decision-making environment under a regime of increased uncertainty, whose efficiency depends on the capacity to aggregate collective intelligence from teams and the ability to use and interpret data. It also revealed the precariousness of traditional instruments for routine navigation, such as the annual budget and strategic planning. In many cases, it has been necessary to promote a broad reset of processes, company structures and internal information circuits. In others, the qualification gap has become evident. Corporate annual reports in 2020 show, in an aggregate fashion, expressive growth in the amount of training for several levels of collaborators. They have also revealed that company initiatives to bring more diversity and promote inclusion are a reaction to the understanding that answers to today's challenges need access to broader cognitive backgrounds and cultural experiences.

In parallel to efforts to update the systems, equipment, processes, spaces, routines and training required to adapt teams, in a short period of time, to home offices and the physical contact restrictions, the new reality brought never-seen-before challenges to leadership and the preservation of a vibrant work environment in which company values and culture are not diluted. Deep repercussions were felt not only in the way people connected physically with their work, but also, and above all, emotionally. The environment and work relations have seen unprecedented alterations. Insecurity with personal and family health, social isolation and difficulty in handling the matter of potentially unlimited availability for professional demand brought on psychological stress, overwhelming HR departments in many companies. When the transition period is over, collaborators and companies will adjust to the "new normal" which should contain a balanced dose of ingredients such as: more flexibility, more automation/robotization and the possibility of hiring with no geographical limitations. Some companies will have more independent contractors, while others will probably move in another direction, increasing insourcing. In fact, companies that feel the adverse effects of the digital legacy seek to recuperate any delay by bringing in modern-day intelligence in development and programming.

That is, in the internal dimension of companies, the landscape of recent changes is branched, profound and uncommon, launching a range of unprecedented management challenges.

Markets and Competition Dimension

In past Reports, we had the opportunity to explore aspects of significant repercussions in the digital transformation in the business environment. The digital world exists and expresses itself, in its essence, through network connectivity, where diverse ingredients from the traditional economic rationale live prevail: network effects, demand side economies of scale, positive self-feedback and increasing returns.

Traditional concepts and pillars that sustain the logic of competition in a traditional environment – barriers, economies of scale and scope, lock-ins, decreasing returns – were subverted. Against castles and motes in the "physical" industry, we recall that the digital era is armed with long-range electromagnetic catapults that project enemies through the air into the fortress´ walls, besides tunnels of underground optical fibers providing access to the compartments that were, up until then, unsurpassable. Market leaders are naked; incumbents are vulnerable. Channels with access to markets are free, numerous (omni) and no longer have tolls. Neither are they restricted only to traditional participants in the same sector, but rather put themselves out there within the reach of "foreigners." An e-commerce platform originally aimed at selling books online (Amazon) has threatened retailers and supermarkets. A video streaming company originally aimed at renting DVDs (Netflix) outdoes the studios that produce content; a manufacturer of personal computers (Apple) overthrows the lucrative market of mobile phones; a marketplace for selling used products becomes a powerful ecosystem of online commerce, payments and credit (Meli).

Also unheard of are the speeds of the successful forays into new areas, which makes it even more difficult for companies in the market to build the capacity to come up with answers. Invariably, the dominance of the successful participants in the traditional environment is explained by the accumulation of processes, controls, routines and planning which, using intelligence and discipline, provided incremental advantages over the years. The model changed and today's competition requires boldness and agility. The digital aspect shifted the semantics of the word "legacy" to the other side, where inheritance has become a burden. "What brought us here will not get us there," warn today's linguists. And that is the puzzle that companies find nowadays, hesitating at the fork in the road, between the instinct for preservation and the threat of extinction. The environment where rival strategies are taken on has become more open and dynamic than it was thirty years ago. We have gone from a game of checkers with homogeneous pieces and limited possible displacements to a realm of far-reaching moves and exponential possibilities of a chess board.

The problem would not be so difficult for long-term investors if the matter were simply binary, with a final winner on the unfinished board game. The challenge – and the opportunity – for diligent investors is that the market attributes weights that are relative and differential, at the same time that the game is not linear, nor will it be defined in one or even a few rounds. As an example, Cielo still holds 32% of the acquiring market, and is valued by less than BRL$ 10 bn. Stone, which turned up later and engulfed 9.7% of the business, is a BRL$ 97 bn market cap company. The Brazilian bank Itaú, with a centenary history of growth and resilience, is worth BRL$ 258 bn, and the very new XP, BRL$ 128 bn. The market looks ahead, projects future potentiality and pays very little homage to past achievements. We know that network effects create positive self-feedback, generating an environment of growing returns that tend to increase the differences between competitors. Where platforms are installed, the higher the advantage of a given company and the more it tends to expand; and where there are positive network effects, the growth leads to market expansion. Besides this, the game is dynamic, with actions and reactions, distances may eventually shorten, forces may someday balance, counterattacks may happen – or not. Relative valuations are expected to oscillate, taking into account the growing doubt about the value of companies in the future, making it even more difficult to artfully calibrate, over time, the importance of each investment proposal in portfolios.

Supplier Dimension

Supply chain management was another area in which there was a true revolution in the last thirty years. In the past, suppliers were seen as a potential threat to profitability and the sovereignty of the company. The motto was to avoid any kind of dependence or excessive exposure. Departments of "purchasing and contracting" were managed with the mindset of rivalry only, where negotiations sought to "take out the margin" of the other, jostling forces in a zero-sum game. The extractive mindset prevailed. Good suppliers were those that were redundant, those that could be squeezed and/or replaced without too much trouble.

Technology – here it is again – was also responsible, here too, for engaging the gears of fundamental change. Bar codes, available since the 1970s, had already brough the possibility of a more effective control over the chain, but it was the arrival of enterprise resource planning (ERP) software in the 1990s that introduced the fundamental concept of integration, establishing the bases for a change in the mindset related to suppliers. In this wider view, suppliers came to the same side of the table, becoming, in many cases, more partner-like rather than just rivals. Led by "multinational" sectors, typically the automobile area, new concepts for co-creation, co-production and co-operation spread rapidly. The era of synchronized logistics, just-in-time processes, lean production and reduced inventory levels took off. As a result of becoming more cost efficient and the freeing up of working capital, operational margins and return on capital employed improved everywhere. In another convincing example of the magic power of technology, the game changed, preferentially, to a positive sum. In the technology sector, even more so. The more successful companies were those that first saw an advantage in opening their platforms to foreign developers.

On the other hand, supplier management has become more complex, and the system is more tightly coupled.

Far away occurrences now affect companies' inner workings, reducing the margin for error. The pandemic has highlighted the systemic tail risk causing global chains to come to a halt. With this fright, today, word has it that there will be a partial return to local supplies. Reactions in the same vein include an awakening to the need to develop "digital" intelligence in-house.

More than just a mere rhetorical resource, metaphors are expressions of innovative thought. At Dynamo, we nurture good metaphors. "Supply chain" is one of the most prosperous analogies in the corporate environment. It is just that it recalls the horizontal links in a flat reality. And the world is now circular. Business models and process diagrams are no longer in the traditional time-line format with inanimate boxes and have transformed into circular gears that are mobile, much like the attractive and dynamic aesthetics of flywheels. They are more appropriate configurations to express a world which is seen in a more systemic way. As an exercise – and who knows, maybe proof of our efforts to stay up to date –, we have tried to bring together the main fragments of this Report connecting them in a flywheel design (Figure 1).

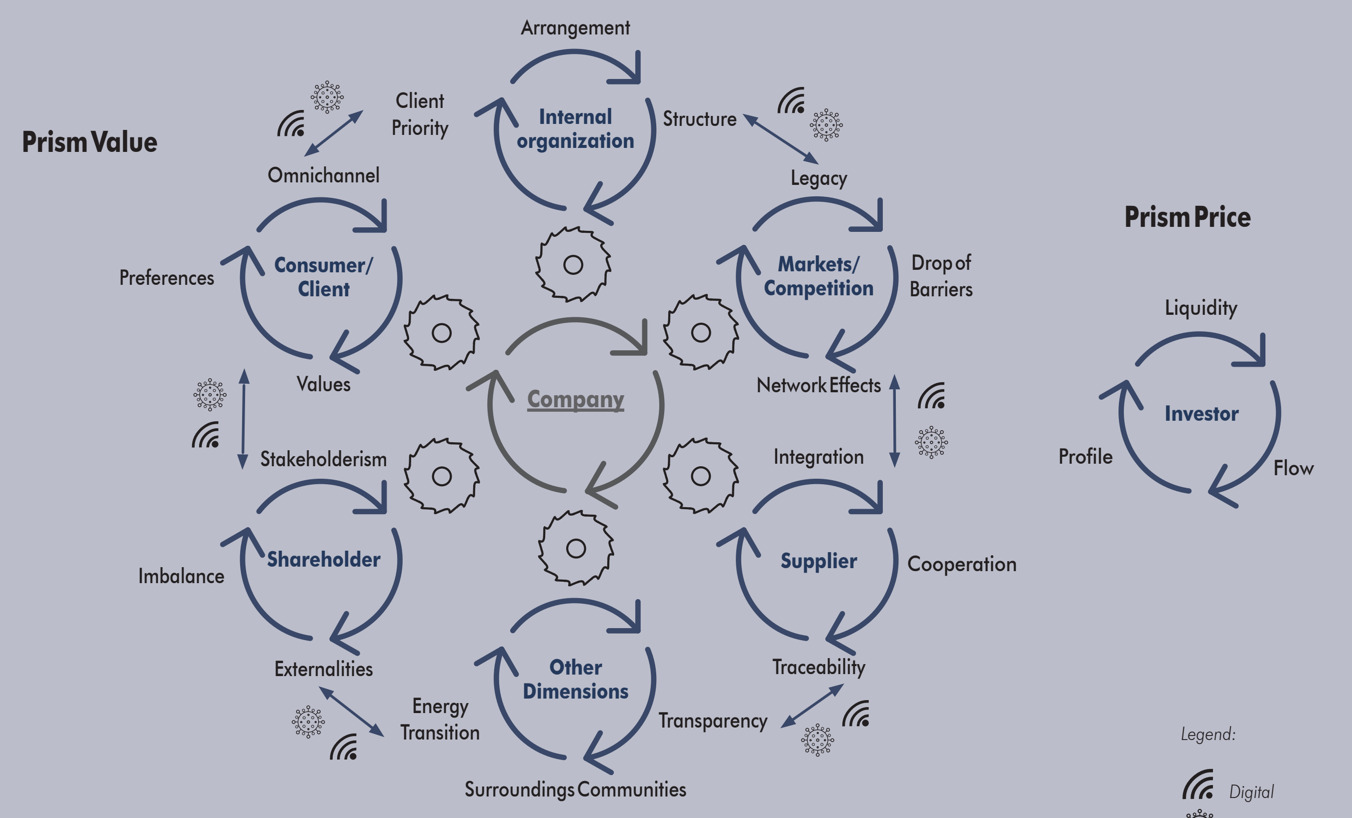
When everything is interconnected, transparency and traceability become relevant properties to qualify the supplier ecosystem. In the ESG era, the risk to corporate reputation extends its nervous extremities to the final point of the last supplier in, let's say, the web (metaphor duly updated). In fact, the Carbon Disclosure Protocol (CPD, 2020) estimates that the greenhouse gas emissions from the supply chain would be, on average, some 11.4 times higher than emissions from the operations of signatory companies. In some segments, such as apparel and retail, the increase is more than twenty times. In the same report, a universe of 8,000 suppliers reported that US$ 1.26 trillion in revenue would be at risk in the next five years due to issues related to climate change, deforestation and insecurity concerning access to water.

Following the amplified exposure of companies, the scope of analysis for the diligent investor has grown in compounding proportions of complexity and domain extension.

Shareholder Dimension

One of the most stable pillars of the corporate ecosystem in the last thirty years was, without a shadow of a doubt, the governance structure. The regime of companies incorporated under legal order that protects profits, and at the same time provides directors incentives to pursue companies' bylaws imposing on them fiduciary obligations has been extremely successful. This has made it possible to

Figure 1 – Flywheel Diagram – Dimensions of the Ecosystem of Companies



Source/Elaboration: Dynamo

pool together competitive resources to finance corporate expansion projects, fostering innovation and rewarding efficiency, with unquestionable results in economic progress and social well-being.

There is no doubt that this general statement has been animated by a number of discussions, litigations, votes, protests, legal opinions and norms, among other institutes, which are part of the corporate citizenship exercise and the improvement in democratic institutions. If the pathway on the activist frontline is tumultuous, scored with subtle progress and sporadic relapses, the guiding line of this conceptual arrangement remains practically rock-solid, much like the understanding that companies should seek out the best possible way to create value and that shareholders would be the residual claimers of corporate profit. In other words, it would be up to them to define what would be left over from the profit after all the rights of society's participants have been met. Aiming to ensure the much-desired identity between maximizing value for shareholders and a social good, some basic premises are required: companies should operate in competitive markets over which they have no influence in the price nor on the rules, and governments need to be able to firmly address the externalities that eventually arise.

The stability of this system has been questioned of late when even shareholders are being reached by the modernization (*aggiornamento*) wave. Along with positive results, there is the perception that the aforementioned conceptual scheme does not go hand-in-hand with reality of the corporate day-to-day, and that in practice companies have imposed externalities onto stakeholders. Within this context of a growing number of shareholders, it would be opportune and legitimate to foster a better balance in governance powers at companies. And, here, there are a several levels of intensity in the proposals for change. Some argue that, if the premises that justify placing shareholders as residual claimers have been violated and investors do in fact have genuine social/ethical concerns, as empirical evidence suggests, the purpose of companies should be expanded to put the maximum focus on well-being – and not on value – for shareholders (see Hart & Zingales, 2017).

Others believe that companies should consider the interests of other stakeholders as "instrumental" acknowledgement, without deviating from the aim of maximizing long-term value for shareholders. And there are those that go further, arguing that the well-being of other stakeholders should be pursued independently of the effects on shareholder value. That is, stakeholderism would be an end unto itself rather than just a means. In this case, company directors should serve equally several bosses. Declarations of support for this reform position come up all the time, despite there being no suggestion to address how this complex system of "pluralist" governance would work in practice. Some voices, however, warn of the hidden dangers under this "illusory promise" of stakeholder governance (see Bebchuk, 2020).

The discussion is lengthy, includes many matrixes, needs to be qualified and, therefore, would deserve more space in another Report. What we have seen is that not all participants in the debate, whether they are investors, service providers or companies, seem to understand the sheer dimension of repercussions of their own positions. Not to mention the cases in which expressed intentions do not befit practical attitudes. Regardless of this, for the purposes of this Report, we affirm that another fundamental territory in the lives of long-term investors is being submitted to undefined moments, which requires attention.

Other Dimensions

More recent times accentuate changes in several other areas with audible repercussions in the day-to-day of companies. A better collective understanding of the gravity of environmental issues has been pushing companies to take a more effective, leading role to mitigate climate risks. Industries that emit more greenhouse gases need to take a position on energy transition (scopes 1 and 2), as do companies exposed to the emissions in some part of their value chain (scope 3). In many cases, this means facing not only relevant trade-offs, but also costly and far-reaching decisions under great uncertainty.

Similarly, there is a growing perception that companies should play a more decisively social role, reinforcing supportive initiatives in surrounding communities. If the merit of this argument in a country with such severe inequalities does not allow debate, a doubt remains once again in terms of the appropriate tuning of the limits of these commitments: how much should these be taken on by the private sector operating under pressure from a competitive arrangement, and how much of an undesired and unintentional effect could they cause, atrophying even more the State's scanty efforts, or/and the timidity of initiatives from civil society. Another long discussion. Anyway, the range of obligations and diligence has expanded for companies.

Someone somewhere defined "digital transformation" simply as "everything you do will be revealed." This is a characteristic of the current world. Customer experiences go viral on the web, concerns of collaborators swiftly appears on the complaint channels, oversights of suppliers quickly affects a brand's reputation. Regulators are globalized, exchanging experiences and highlighting long-standing blind spots. Agencies responsible for inspections now have electronic tools and apply painstaking controls to operations. The digital world retains traces, which are unearthed by hackers, sophisticated fraudsters that represent permanent costs if not heavy losses for companies. Nothing escapes the infinite curiosity of social media, the almost unlimited power of influencers and panoptic ever-watching eyes of the robot-algorithms that trawl the network, not to mention the improved quality of investigative journalism, which is also digitally well prepared. Transparency is a virtue, and all these novelties are making companies better, or not. Demands on directors and executives have increased exponentially, as has the variety of capabilities required. The risk map with some sparkling coordinates on a single page has turned into a sonar radar with continuous 360º tracking. More risk calls for more preparation and more diligence.

Investor Dimension

So far, we have described the size of transformations within the scope of the ecosystem for companies, which are the primary focus of our interest. If we take another step up and go to the level of investors, taking into account the elements that specifically affect the dynamic of markets – asset prices, flows of resources, investor psychology –, we also see new ingredients that increase the complexity of our analysis even more.

Central banks around the world, since the 2008 financial crisis, have been undergoing an unprecedented process of fiduciary currency creation. Successive quantitative easing operations push interest rates and even nominal rates to unexpected levels. This period just happens to coincide with the progress of digital transformation, and the digital world, by definition, is deflationary. The warning bell of inflation, which was always historically a trustworthy alert to highlight poor public policies, has been switched off. Just when we thought we had reached the limits of the expansionist monetary policy experiment, the exorbitant fiscal packages came as an answer to the general halt of economies brought on by the pandemic. And with this, we end 2020 with signs that, in normal times, would be difficult to interpret. Significant drops in products and employment, at the same in which private savings are rising and the prices of some assets are skyrocketing. With a forced reduction in consumption and the generous transfers from the public sectors, the available income to the private sector posted an increase that has not been seen for many years in several countries. At the same time, there is a clear split between losers and winners brought on by the digital divide. Sectors that are labor-intensive suffer; more digitalized segments are entering a virtuous spiral of winner-takes-all or almost-all. Inequalities have become more evident, generating personal insecurity, social unrest and political opportunism.

At a micro level, excessive liquidity has generated sensitive repercussions in the dynamic of flows and the types of participants in the market, mainly with expressive growth of retail investors. There are many possible explanations: (i) proliferation of trading platforms and investment advice promoting broad, remote access to organized markets; (ii) social medias allowing mass publicity of investment content; (iii) relationship networks making it feasible to conduct coordinated actions between widespread investors with immediate and unprecedented repercussions on the price of assets; and even unexpected circumstances mixed together with more simplistic psychological elements, such as: (iv) closed traditional gaming (gambling) houses channeling speculative enthusiasm to online trading; and (v) confined individuals, with more free time and more available income, seeking alternative entertainment.

Much like long-term investors, we are more interested in the determining factors that affect companies than what has moved markets. That explains the disproportionate space allocated to these two matters. On the other hand, we are by no means indifferent to the short-term oscillations that could cause severe repercussions in our Fund´s NAV, as happened in the pandemic panic last year. While we do not base our investment decisions on market speculation, we try to map out the elements that might affect financial flows and the psychology of investors.

Dynamo Cougar x IBX x Ibovespa Performance up to April 2021 (in R$)

Period	Dynamo Cougar	IBX	Ibovespa
60 months	188.2%	132.3%	120.5%
36 months	119.0%	45.0%	38.1%
24 months	79.9%	28.4%	23.4%
12 months	69.4%	51.2%	47.7%
Year to date	2.2%	2.1%	-0.1%

NAV/Share on April 30 = **R$ 1,715.0274344**

DYNAMO COUGAR x IBOVESPA
(Performance – Percentage Change in US$ dollars)

Period	DYNAMO COUGAR* Year	DYNAMO COUGAR* Since Sep 1, 1993	IBOVESPA** Year	IBOVESPA** Since Sep 1, 1993
1993	38.8%	38.8%	7.7%	7.7%
1994	245.6%	379.5%	62.6%	75.1%
1995	-3.6%	362.2%	-14.0%	50.5%
1996	53.6%	609.8%	53.2%	130.6%
1997	-6.2%	565.5%	34.7%	210.6%
1998	-19.1%	438.1%	-38.5%	91.0%
1999	104.6%	1,001.2%	70.2%	224.9%
2000	3.0%	1,034.5%	-18.3%	165.4%
2001	-6.4%	962.4%	-25.0%	99.0%
2002	-7.9%	878.9%	-45.5%	8.5%
2003	93.9%	1,798.5%	141.3%	161.8%
2004	64.4%	3,020.2%	28.2%	235.7%
2005	41.2%	4,305.5%	44.8%	386.1%
2006	49.8%	6,498.3%	45.5%	607.5%
2007	59.7%	10,436.6%	73.4%	1,126.8%
2008	-47.1%	5,470.1%	-55.4%	446.5%
2009	143.7%	13,472.6%	145.2%	1,239.9%
2010	28.1%	17,282.0%	5.6%	1,331.8%
2011	-4.4%	16,514.5%	-27.3%	929.1%
2012	14.0%	18,844.6%	-1.4%	914.5%
2013	-7.3%	17,456.8%	-26.3%	647.9%
2014	-6.0%	16,401.5%	-14.4%	540.4%
2015	-23.3%	12,560.8%	-41.0%	277.6%
2016	42.4%	17,926.4%	66.5%	528.6%
2017	25.8%	22,574.0%	25.0%	685.6%
2018	-8.9%	20,567.8%	-1.8%	671.5%
2019	53.2%	31,570.4%	26.5%	875.9%
2020	-2.2%	30,886.1%	-20.2%	679.0%

2021	DYNAMO COUGAR* Month	DYNAMO COUGAR* Year	IBOVESPA** Month	IBOVESPA** Year
JAN	-7.4%	-7.4%	-8.2%	-8.2%
FEB	-2.1%	-9.3%	-5.3%	-13.1%
MAR	-0.1%	-9.3%	2.9%	-10.6%
APR	8.4%	-1.7%	7.5%	-3.9%

Average Net Asset Value for Dynamo Cougar
(Last 12 months): R$ 6,583.3 millions

(*) The Dynamo Cougar Fund figures are audited by Price Waterhouse and Coopers and returns net of all costs and fees, except for Adjustment of Performance Fee, if due.
(**) Ibovespa closing.

A text that is horizontally broader than vertically deep may not deserve any recognition from our reader. We know that each of the domains mentioned requires more individual space, deeper comments, as well as practical illustrations of company initiatives. We believe, nonetheless, that the option for a panoramic vision is justified. Our work is called analysis, but also involves synthesis. Sometimes, it is necessary to group together isolated fragments to have the benefit of a view in perspective. Complex systems cannot be defined simply by the properties of the separate parts. The several instances that are connected make up a dynamic mechanism. Similar to flywheels, interaction between them generates momentum (movement). Once inertia has been overcome, the system gains energetic efficiency and speed. And everything begins behaving differently.

Never have so many regions that deeply define corporate identity been provoked so intensely at the same time. It is an unprecedented dilemma that companies need to face to deal with this huge number of shifting variables. At the same time, to react swiftly to so many changing templates, companies need to maintain unity and cohesion, to seek out relevance in their markets, to reinvent themselves to compete and innovate in order to grow.

No less challenging is the long-term investor's task of identifying the nature of several components and their connections, as well as understanding the resulting forces that drive this sophisticated system of gears which are the companies.

Rio de Janeiro, May 11, 2021.

Please visit our website if you would like to compare the performance of Dynamo funds to other indices:

www.dynamo.com.br

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