

Letter to My Partner

To this day, there is just one thing that bothers me at Dynamo¹. Not being a founder. Not being there with you and Pedro Eberle when it all started way back in 1993. Exactly 20 years ago. 20 years!²

A fund to invest in public equities in Brazil with a long-term view was an exotic idea in those times. In a country with dizzying inflation and notorious macroeconomic volatility, the good opportunities in the financial markets were elsewhere. Hence my sincere admiration for the courage that you two had to venture out in the very early innings of the Brazilian equity markets³. Warren Buffett was not yet a best seller here, there was no Novo Mercado and the Corporate Law had not gone through the modernization that came long after, with Law 10.303. All companies had controlling shareholders. In several of them, minority shareholders were not considered real partners. They were just funding.

One of the first imprints of our DNA comes from this very origin. You two opted to do what you wanted to do, what was interesting and gave you pleasure, regardless of commercial or financial considerations. On second thought, courage is not the right word. Simplicity, independence and unpretentiousness reflect more precisely what I mean. Something in the style of George Mallory, the alpinist who tried to climb Mount Everest in 1921 and 1922. He tried, but did not succeed. When he was preparing to go back in 1924, a journalist from The New York Times wanted to know the reason for the insistence to climb that mountain. "Because it is there", was the surprising answer from Mal-

lory. And he went on: "what we get from these adventures is just sheer joy. And joy is, after all, the end of life." I remember talking about this story in our first lunch in a restaurant downtown, when you invited me to work at Dynamo, as if it had happened yesterday. It was not by chance that we talked about Mallory's episode. "At Dynamo, we do what we like to do", you told me. The good symbolism was already in place. Twenty years later, we can say that we have climbed and still want to climb quite a few "Everests" together. Because they are there – and we do not know a better job description.

As far as I know, in those times, aside from our friends from Investidor Profissional-IP, almost nobody was interested in fundamental analysis and value investing. It was not in fashion. It did not have the allure and the adrenaline of fast trading, compatible with other adventures. Results took long to appear. It required an almost academic vocation for the deep study of companies, not to mention high doses of patience and persistence.

On the subject of IP, both Roberto and Crico were remarkably kind to Dynamo in their speeches during the celebration of their 25th anniversary. This goes to show that even in a industry like ours, with a reputation for aggressiveness and excessive pragmatism (for lack of a better word) it is possible to compete in a highly ethical manner and with mutual admiration.

Back to our two decades. In our Dynamo Report 1, which had a little more than page and a half (readers probably miss this parsimony), we promised quarterly reports. Four reports per year. Thus we arrive at Dynamo Report 80, the fourth report of the 20th year. When you do the math, we kept our promise. Our history is registered in these reports, which over time became more substantive and emblematic. There is no better way to know us than to follow the thread of these 80 reports. Practically all the obstacles and shortcuts that we faced along the way are described there: technical, cultural and philosophical issues, biases, speculations and analyses. There have been three

1 Obviously, not counting the "y" in our name, which today doesn't bother me anymore. As you explained to me a long time ago, the Anglicism is only there because Dinamo already existed and it was not possible to register the name with an "i".

2 You know by heart countless phone numbers, how many steps it takes to walk from home to the office, the Ebitda of companies that no longer exist and so on and so forth. As such, to pay tribute to your strange mania with numbers, here is our first CNPJ (company registration number in Brazil) just in the unlikely case you may have forgotten it: 72.116.353/0001-62. We obtained it on April 12, 1993. The Cougar fund would begin its operations later in September of that year.

3 It is fair to register that you two were reconnected by our dear friend Rogerio Castro Maia. By doing so, he can justifiably be considered the meta-founder of Dynamo.

different writers and a fair variation in style, but a unified vision of the phenomena of our day-to-day work. First it was you, then it was me, and now it is in the sophisticated hands of Fernando.

Curiously, our 10th anniversary report was written as a self-analysis manifesto. An in-depth look at “our company” using the same analytical instruments that we developed over the years to help us understand public companies. The report is an answer to the Socratic question of who we are, typical of the post-adolescence period. There, we explain the industry that we are in, our track record up to then, and the main aspects regarding the partnership as well as the culture and business of Dynamo. Pretty serious stuff. Ten years later, with the benefit of maturity⁴, I thought it fair to request a chance to write again. I decided to focus the celebration of our 20 years in a letter to you. In the last paragraph, you will understand why it had to be so.

When we launched Cougar (see the totemic Report 1), we made it clear that, as investment managers, our concern was with absolute returns and not with the direct competition with the Ibovespa or even with other managers. In and of itself, not a particularly strategic or ingenious statement. We were simply laying out what we wanted to do with our own money. Thinking like this is another one of our obsessions. We repeat this mantra to everyone who comes to work with us: Dynamo is a firm that invests the capital of its own partners and extends this service to other investors. This is the purest truth. Granted, this mantra always came in handy in moments of difficult decisions. When in doubt, the final decision always follows the logic of “this is what we would do if we were managing only our own money”. Thinking about what would be best for us is the most coherent conduct in the fulfillment of our fiduciary duties. It is also probably the only form of conduct that investors can fully rely on.

With your usual skill and luck to pick good investments (that I envy so much), you continually increased your own investment in Cougar. An example which, to a greater or lesser degree, was followed by everyone here. Lucky us! The people of Dynamo thank you. This is how we built the history of the significant participation that the partners have in our assets under management. We are both quite pleased with the fact that, even without any formal obligation, coercion or even stimulation, everyone here invests a big portion of their compensation and net worth in the funds we manage. They do that completely by free will. This

voluntary act is very significant in all respects. It is one of the most credible signs of what we are, how we work and what we believe in.

Every now and then, I find myself reading an interview with a professional soccer player saying how incredible it is to get paid to do what he loves the most: playing football. When I was a kid playing pick-up soccer, this was my idea of professional paradise. Now I ask you: Isn't this exactly how we feel? Of course I know your answer but the totally rhetorical question serves only to underscore the privilege of working at Dynamo. A privilege well tested over the last 20 years, at least for those who identify themselves with what we do and how we do it. And what is our job? To study companies as organisms which have intelligible functioning rules. These rules may be understood and evaluated when they are thoroughly dissected and monitored closely. “To know more about the company than any other non-insider” is the motto that you like to repeat to educate our youngsters. It is in this immersion, which goes from the most objective technical point to the most inexplicable intuition, that we find the conviction of a discrepancy between price and value of a company. Isn't this how we view fundamental analysis? Numbers, company, management, and business scrutinized in a disciplined way? Wasn't this how we were all trained? You and I a long time ago, but quickly followed by the first team of partner-analysts: Pedro Damasceno, Cristiano, Rudge, Fernando and Carlos Simas[Caca]. All of them are extraordinary professionals today. We owe each one quite a lot. At this point in their lives, they could certainly have their own investment firms if they so wanted, as the many recent successful “dissidences” are there to prove. They could, but they won't. I believe that we will find the same attitude from all of the analysts that came later and are already members of our partnership: Mario, Julio and Gustavo B. Not without a certain dose of emotion, I make the ambitious prediction that we will all be working together for a very long time, maybe even until the end of our (hopefully long) professional lives⁵.

Speaking of working together, time to address another subject: the launching of Dynamo London. Many years ago, we started to talk about the attractiveness of having an extension of what we have been doing for so long in Brazil in another jurisdiction. Together, we thought how great it would be to be able to diversify

4 From where we have to debit various other factors such as, Lipitor, back pain and grey hair.

5 One of the things that gives me the most pride about Dynamo is that the prosperity of the partners did not lead to extrapolations to what could be called conspicuous consumption. Work is not just the means, it is the end. Therefore, we can continue to work without a horizon. This merit has to be credited to you and Pedro Eberle, who naturally set the standard. I should also mention Marcelo Stallone, who was a member of this sensible group while he was with us.

our own personal equity investments, which were, up to that point, restricted to the Brazilian market. It was a very daring idea as it involved considerable changes in our personal lives. Leaving Rio, as much as we complain about the city, is not easy. Like you, I began to like the idea more and more, especially to talk about it. But the will and determination to convince the family, organize the move and travel to other sceneries was only yours, I must recognize. In 2005, there you went to London to start all over again, practically repeating the same route as in 1993. Seriously, where do you get the energy? Different companies, different laws, different regulations, different corporate practices. Everything was different, even more different than we imagined. It was a lot of work. Besides, we had to hear the subtle criticism about the apparent surrealism of a company as small as ours launching an operation abroad. Criticism that was not completely misguided, as we knew. At the end of the day, it would have been more logical and organic to launch a long/short, a hedge fund or a private equity fund right here in Brazil, where we have been for so long, investors know us and we have our business roots. What some of the critics failed to understand was that this was another clear expression of our main driver (sorry for repeating myself): we wanted the diversification for ourselves. Once again there was no commercial consideration, business plan or anything like that. We knew what we were looking for and went for it. In September of 2006 (always in September), we launched Dynamo Fund. With reasonable success, we can say today. Such success has to be credited to our Kings Road partners: you, Carlos Simas, Eduardo and Thiago, in addition to the Europeans Giovanni and Daniel. Others will certainly join in the future. What we could not have foreseen is that, partly as an unintended consequence of the original plan, the two Dynamos, in Rio and in London, would benefit so much from one another. We became less provincial here and, there, we already started with a culture and a working method. Not to mention the exchange of knowledge about companies and industries. All our concerns about the potential disintegration were unfounded. A good video-conferencing system and daily Rio-London direct flights provide us more than enough proximity. To me, the downside of this is that we no longer sit together in the same room every day, like in the old times. Discussing, agreeing and disagreeing prodigally. This was a loss.

This last topic deserves a special chapter. You and I always competed openly in so many instances. To the point that when there was a clear advantage for one or the other, making the game boring, we twisted the rules so as to have a fair game again. Like when we used to play tennis. You covered the doubles court and I only had to worry about

the singles area. And we always had tight matches⁶. We took every discussion about working matters to the limit. For two reasons: first, because of pleasure of listening to the other's arguments, an egotistical mechanism to test our own convictions. It is not by chance that, from time to time, we describe our method for building investment theses as "popperian". All individual ideas percolate so that everyone can try to falsify it. If it survives, it becomes a collective asset⁷. It is not easy to sustain a process like this. Everyone needs to be detached of any vanity and excessive individualism. I may be wrong but, once again, I think we gave the example and established the right paradigm.

The second reason is that in parallel with the professional life – with so many convergences and especially divergences, amidst so many practical, objective and controversial issues – a great friendship arose. A solid friendship. Plutarco, all the way back in the Second Century (yes, that's him! You know me...) said: "I do not need a friend who changes his mind when I change mine and who agrees when I agree. For that, my shadow does better." This is quite a non-trivial attribute. How many times did I find myself in moments of Galileu Galilei whispering to myself, "damn, he is right". I am sure you disagree even with many things in this letter. As it has always been and will always be⁸. We got used to disagreeing in private but, remarkably, also in public. And without any embarrassment, even though others sometimes felt that way. But with the notable wisdom of recognizing the highest conviction side and letting it finally prevail. A permanent arbitration, founded on common sense, reciprocal respect and trust. I do hope that this behavior⁹ is a cool¹⁰ heritage that we will leave here for a very long time.

Many important people played and still play leading roles in this "Tale of Two Cities", Rio and London, as Charles Dickens would describe it. However, as we like to

6 *I did win a few sets, remember? No big deal. I am always impressed by how many people at Dynamo had some past sporting success even though this is not a criteria for hiring. Maybe this is where our common trait of valuing wins achieved by playing by the rules comes from. Cheating to win may even lead to titles but one needs to have a very specific pathology to be happy with it.*

7 *Since I think that very few people actually read footnotes, I can register immodestly that my PHD thesis was about collective action. I read a lot about the subject. It is really amazing how we never had the free rider problem at Dynamo. Not a trace of it. Which goes to show that Mancur Olson was right. The prevention of the free rider is given by the selective incentive. In our case, the incentive was not being excluded from the decisions taken collectively.*

8 *I cannot write a Report without a citation from Darwin. Here I make a self-compliment: "the friends of a man are one of the best ways to measure his value".*

9 *As a tribute to the good Hegel, whom I had to study during an unbearably hot summer, which led me to try to amortize it every chance I have, I was going to write "this dialectic". But, in consideration to you, I didn't.*

10 *Of course, the word "cool" ("bacana") is only in a Dynamo Report because, for the first time ever, you will not read it before it is published.*

say half-jokingly, no one has been as important as Felipe. The construction of an efficient and dependable back office, for many years formed by a team of only two people, Georgito and him, is admirable¹¹. Today, he has already formed two more partners, Emerson and Gustavo K. It is our back office that draws the line between the right and the wrong, the certain and the doubtful, between what we can and cannot do. The determination with which these guys defend the legality and the fairness of what we do gives us tremendous comfort and certainly helped build Dynamo's reputation.

For long-term investment managers, the activity of buying and selling shares is very particular. Loading or unloading a position without affecting the market price, or affecting it minimally, is not a job for just anyone. One needs calm, perseverance and a thorough knowledge of the market for the specific stock. It is not always easy to understand that there are times when doing nothing is the best decision. It is common to confuse active trading with dynamism. Even more common is for the personality of the trader to adjust better to the high adrenaline of the quick gains (and losses) that only the big trading desks can offer. As you usually say, and rightly so, *"long term is boring"*. We owe the serenity we have in this part of our business to the indispensable presence of Andre (our second longest standing partner, preceded only by Pedro Damasceno). On top of everything he did, he also had the competence to form Antonio Pedro, with whom he shares the trading responsibilities today.

Back to more technical issues. To invest with a long-term mind, one needs to escape the liquidity traps created by short-term redemption schedules. This includes certain short-term sacrifices. To cross this Rubicon of contrarian expectations, one must count on patient investors. In the beginning, we only had ourselves, which did make things easier. Then, family and a few close friends. The group started to grow naturally overtime. Curiously, you never had any commercial or marketing talent. Neither did I nor anyone else at Dynamo. This position was always unoccupied. Nevertheless, we still managed to grow. When we launched Puma 1 in 1997, which brought us closer to institutional investors in Brazil, we could not have imagined that we had also started an irreversible change in our investor base. Later on, this experience eventually led us closer to the American university endowments and family offices that have become such relevant investors today. These folks, in addition to

understanding perfectly what we do, also taught us how to build a more modern and better-structured relationship between manager and investors. It was a long way. Like me, you must think of this 20-year history with a very justified sense of pride.

Still in the subject of Puma 1, it was then that our minority shareholder activism became better known. Fun-nily enough, our first Report (ok, I promise it is the last time) already stated that for certain types of positions we would have to be more active as shareholders. Little did we know at the time that this would later be called, quite pompously, corporate governance. We always thought of listed companies as partnerships. Big partners, small partners and controlling partners, all with the same aligned interest of creating value for their common asset, the shares they owned. However, there are some quite complicated issues around this alignment. Short term and long term, leverage, cash, dividends, control premium, risk, etc. How many times have we sat down to discuss these issues in specific cases? And, not surprisingly, how many times did we disagree? I repeat: our productive disagreement is one of the most genuine heritages we will leave to the next generations at Dynamo. Speaking of which, we are already in our third¹², and almost without noticing it. They are young and very welcome. I hope they incorporate our values of work and life soon.

The fact is that Dynamo today belongs to many people. It can be represented by any of our partners, as already happens in so many circumstances. Horizontality has always been one of our objectives for the partnership. We deliberately diluted not only our share of the results but also our hierarchical importance. And, modesty aside - yours and mine - I think we did this quite well. We formed competent people with good character. If we want to last long, decentralization is a priority. And I use this word, decentralization, with a specific aim. This has nothing to do with the common jargon "succession" because we are not exiting gradually or reducing our energy. Not at all. Totally to the contrary. We continue to climb as much as we ever did. What we are doing is increasing the density of the group that makes the decisions and defines the route for the next several years. By doing this, Dynamo will last long and improve continuously.

As you know, it is quite common for people to ask us how we manage to have such a special partnership, with a turnover close to zero. Another one of those tough-

¹¹ It is fair to register here the support that Felipe had, almost from the very start of Dynamo, from Soninha and, soon after that, from Barbara.

¹² In addition to all other partners mentioned in this Report, we have the more recently arrived Tiago, Kassiana, Bernardo, Gabriel, Rapparini, João, Pedro and Ribas.

to-answer questions. This stability is not by design, but, instead, it is consuetudinary. It is a habit, a way of working that was built day by day. It is not a planned culture. We both have great admiration for talent, competence and hard work. But that is not all. It does not suffice if we want to have a partnership capable of sustaining both a way of working and living. There are other values that are equally eliminatory. At Dynamo, everyone knows them. You were always skeptical of vanity, devil's preferred sin. This is very helpful because I think along the same lines. Excess modesty also bothers us. As Rudyard Kipling wrote in the poem *If*, where each verse is a recommendation: "If you can meet Triumph and Disaster and treat these two impostors just the same". I may be wrong, and we should consult the others, but I think these are the waters that we navigate. It is not the tradition in our industry but I have a somewhat speculative conviction that with life becoming ever longer, the idea of working to make money so that we can stop working, the antithesis of ours, is going to lose force. It will be increasingly considered unacceptable and mediocre.

In a very good book about John Lennon and Yoko Ono, Jonathan Cott asked Yoko if she did not feel responsible for the separation of The Beatles. "That's insanity", she replied, "These were four¹³ very talented people who had too many songs for just one group. And I knew that each one of them would blossom out on his own. The Beatles were doing it as four people – it's unusual that four guys should always be together". This made me think about a very particular theme, which is the longevity, or lack thereof, of rock bands in analogy with investment managers. A few years ago, pressured by Rudge, I thought about writing a Dynamo Report about this mystery. I talked to some people and concluded that this phenomenon has no explanation. Why some groups stay together while others separate is really a mystery. There is no bibliography on the subject. Nobody has ventured to derive a theory for these professional matches and mismatches. With that said, enough of looking for explanations for the unexplainable. It is better to move on and simply enjoy what probably is a combination of luck and skill, as we have written in recent Reports.

Bruno, after so many years working together, I have no doubt that I could not have found a better partner. You know this perfectly well. But I would not be so ego-centric and pretentious so as to use our 20th anniversary Report to express my personal gratitude. Never. There is

¹³ In the book, Yoko Ono actually said three because the context of the question, which we have not transcribed here, excluded John Lennon.

another reason for such a personalized report. While I was thinking about the different models for this Gregorian celebration, I spoke with many people in the office. I could see how happy they are and that they expect to be around for many more years to come. Almost a cliché statement about dates like this: "Let another 20 come", was what most said. However, when I asked them what they thought this Report should be about, several diverse ideas popped up. To be honest, some actually had no idea at all. "Whatever, write something cool". It was then that the insight for this Report dawned on me. Talking casually with them about our Dynamic History, from the beginnings in 1993 to today, it became crystal clear how significant you are to all of them. Ethically, morally and professionally. Not too shabby, Mister, quite to the contrary. The conclusion was obvious. Nothing of the usual reports, generic or specific. The correct and more sanguine celebration is the right that I took for myself, in the name of all who work here, to collectively thank you for everything you represent and have done for Dynamo. The right to thank you using this 20th anniversary Report. I hope you like it, Bruno Rocha.

Ah, I almost forgot. If you disagree with too many things that I wrote, which is quite likely, your right to reply is guaranteed. In our 30th anniversary Report.

Rio de Janeiro, December 6th, 2013.

DYNAMO COUGAR x IBX x IBOVESPA Performance in US\$ up to September 2nd, 2013

Period	Dynamo Cougar	IBX	Ibovespa
20 years	29,2%	NA	10,6%
15 years	26,5%	14,7%	9,2%
10 years	27,4%	19,4%	15,6%
5 years	8,9%	-4,5%	-8,1%
1 year	-7,0%	-13,7%	-22,2%

NAV/Share on September 2nd = R\$ 413,280468652

*Dynamo Cougar started its activities in September 1st, 1993. In 2013, September 1st was not a business day, then we considered September 2nd.

DYNAMO COUGAR x FGV-100 x IBOVESPA (Performance – Percentage Change in US\$ dollars)

Period	DYNAMO COUGAR*		FGV-100**		IBOVESPA***	
	Year	Since 01/09/93	Year	Since 01/09/93	Year	Since 01/09/93
1993	38,8%	38,8%	9,1%	9,1%	7,7%	7,7%
1994	245,6%	379,5%	165,3%	189,3%	62,6%	75,1%
1995	-3,6%	362,2%	-35,1%	87,9%	-14,0%	50,5%
1996	53,6%	609,8%	6,6%	100,3%	53,2%	130,6%
1997	-6,2%	565,5%	-4,1%	92,0%	34,7%	210,6%
1998	-19,1%	438,1%	-31,5%	31,5%	-38,5%	91,0%
1999	104,6%	1.001,2%	116,5%	184,7%	70,2%	224,9%
2000	3,0%	1.034,5%	-2,6%	177,2%	-18,3%	165,4%
2001	-6,4%	962,4%	-8,8%	152,7%	-25,0%	99,0%
2002	-7,9%	878,9%	-24,2%	91,7%	-45,5%	8,5%
2003	93,9%	1.798,5%	145,2%	369,9%	141,3%	161,8%
2004	64,4%	3.020,2%	45,0%	581,2%	28,2%	235,7%
2005	41,2%	4.305,5%	30,8%	790,7%	44,8%	386,1%
2006	49,8%	6.498,3%	43,2%	1.175,8%	45,5%	607,5%
2007	59,7%	10.436,6%	68,4%	2.048,7%	73,4%	1.126,8%
2008	-47,1%	5.470,1%	-50,1%	973,3%	-55,4%	446,5%
2009	143,7%	13.472,6%	151,9%	2.603,3%	145,2%	1.239,9%
2010	28,1%	17.282,0%	15,2%	3.013,2%	5,6%	1.331,8%
2011	-4,4%	16.514,5%	-20,6%	2.373,0%	-27,3%	929,1%
2012	14,0%	18.844,6%	11,8%	2.664,3%	-1,4%	914,5%

2013	DYNAMO COUGAR*		FGV-100**		IBOVESPA***	
	Month	Year	Month	Year	Month	Year
JAN	1,7%	1,7%	3,3%	3,3%	0,8%	0,8%
FEB	1,7%	3,4%	-2,7%	0,5%	-3,3%	-2,5%
MAR	-0,9%	2,4%	-5,6%	-5,2%	-3,7%	-6,2%
APR	0,8%	3,3%	-1,4%	-6,5%	-0,2%	-6,4%
MAY	-4,7%	-1,6%	-11,0%	-16,8%	-10,1%	-15,9%
JUN	-8,2%	-9,7%	-9,5%	-24,7%	-14,7%	-28,2%
JUL	-0,5%	-10,1%	-0,5%	-25,0%	-1,7%	-29,4%
AUG	-2,5%	-12,4%	0,1%	-25,0%	0,1%	-29,3%
SEP	8,6%	-4,9%	9,8%	-17,6%	11,3%	-21,3%
OCT	4,8%	-0,3%	3,7%	-14,6%	5,0%	-17,4%
NOV	-5,1%	-5,3%	-6,1%	-19,8%	-8,4%	-24,3%

Average Net Asset Value for Dynamo Cougar (Last 12 months): R\$ 2.024.732.883

(*) 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. (**) Index that includes 100 companies, but excludes banks and state-owned companies. (***) Ibovespa closing.

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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DYNAMO

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