Report
Dynamo 49

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Going Public - I

There is no doubt that the major happening in our capital market is the new cycle of initial public offerings (IPOs). Since Natura´s deal in May 2004, no less than 30 companies went public through transactions involving approximately R$17.7 billion[1]. There have been eleven initial offerings in 2006 alone, and further nine are currently under CVM (Brazilian Securities and Exchange Commission) review. During these two years, there have been 21 block trades of existing publicly traded companies, amounting to another R$14.5 billion sold.

In addition to this extraordinary volume, initial public offerings have attained prices significantly higher than historical levels. While *Ibovespa* companies have been traded at P/E multiples of close to 11.1x and EV/EBITDA of 4.8x, IPOs average multiples reached 18.8x and 9.2x, respectively[2]. Even with the recent market adjustment, 73% of IPOs companies have outperformed *Ibovespa*, and, in 40% of cases this difference exceeds 25%. Attached hereto is a table of the IPO database utilized in this Letter.

As an example, we create a hypothetical IPO performance index, where the only weighting parameter is the size of transactions. In this case, the absolute return of the Index since the cycle commenced up to May 30 would be 193% in nominal *Reais*, as compared with 117% of the IBX and 86% of the *Ibovespa* (chart 1).

Based on these figures, we can see that IPOs have been highly successful. As investor, Dynamo had a marginal involvement in this success. We invested in some of these companies, i.e., Natura, ALL, Localiza, Lojas Renner, Tractebel, Vivax. In some cases, we sold our investment but, even in the case of these shares, prices carried on rising after our sale. Two of these companies are gradually gaining greater importance in our portfolio, as we increasingly believe in their business and get to know management better. Nevertheless, to date, no IPO has become one of the Fund's major positions.

Despite the excellent quality of most of these companies coming into the market, their valuations assume significant future growth. Here at Dynamo, we have always hesitated to pay up front for a cash flow indicating a low margin for negative surprises. However, we also know that even our most basic investment principles are not foolproof convictions and must be regularly tested *vis-à-vis* the realities of the market. In this context, we dedicate no small effort to strive to understand the nature of these recent events and certainly do not discard the possibility of, one day,

(1) *In this sample, we have considered the offerings of companies that really have gone public although, legally, they already were, such as CPFL, TAM, Lojas Renner, Cyrela, Tractebel, Rossi, and Gafisa.*

(2) *The parameter applied here was the 2005 and 2006 arithmetical average of the multiples of the Ibovespa companies weighted at their percentage of the index (data from UBS Bank). In the case of IPO companies, we took the arithmetical average of the implicit distribution price multiples.*

Our Performance

During this first quarter, the shares of Dynamo Cougar went up by 14.5%, while *IBX* appreciated 13.8% and *Ibovespa* 13.7%. Over the last ten years, the Fund yielded a return of 25% pa in US dollars and 22.5% pa over *IGP-M*. During this same period, *Ibovespa* gained 13.2% pa in US dollars and 10.9% pa above inflation measured by the *IGP-M*, while the *IBX* attained 17.1% pa and 14.8% pa, respectively.

The year opened well with its positive 2005 heritage: interest and exchange rates going down, as well as Country risk, and Bovespa at new highs. With the additional entry of foreign money and a significant increase in daily liquidity, January guaranteed the gain of the whole quarter. The following chart, presented in our last Letter and updated for this first quarter, shows that 2005´s tendencies continued through the beginning of this year. Since then, political noises on the domestic scene have increased, international concerns hovered on the horizon (changes in the FED team, Japan's inflation) to the extent that *Bovespa's* profitability was replaced by volatility.

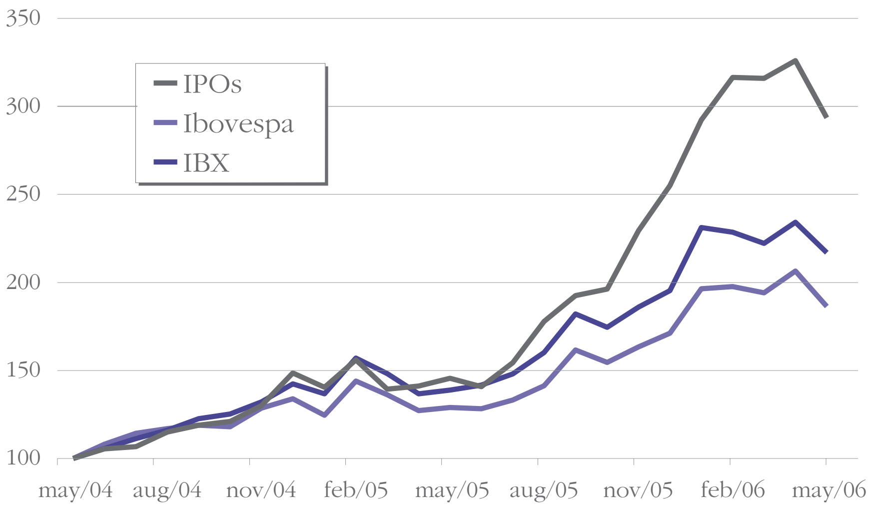
Dynamo Cougar took advantage of these favorable winds to present a good performance.

reinvesting in some of these companies, if the respective valuation so permits.

Our idea now is to share with our readers some of our thoughts, experiences, and evaluations of this IPO market. Given the range of the material, we decided to split the topic into two Letters. After this brief introduction, in this Letter we investigate what *motivates* companies to go public, with particular attention to the intentions of the issuers *vis-à-vis* the incentives signalized by market circumstances. In our next Letter, we shall analyze two other topics: i) whether some *standards* of IPO cycles in other countries are also present here, and ii) the internal mechanics of the *processes* of these transactions, when we shall also review Dynamo's competitive position in this context.

But first, please note that if, on the one hand, we recognize the increasing value of the investments that we have already sold or have not come to acquire, on the other hand, we have further reinforced the convictions that drive the profile of the Fund's current portfolio. Thus, if this collective economic growth projected on the success of these new companies actually occurs, the resulting scenario will be most promising for the main allocations of our portfolio, which consists of prominent and time-tested companies, with competent management, disciplined capital, and more interesting valuations.

Chart 1 – IPOs index x Ibovespa x IBX (base 100 may/2004)



Source: Economática, Dynamo

Motivations

Going public is one of the major decisions in a company's history. There are three basic reasons that lead a company to issue securities to be traded in the market:

i) To finance growth and reduce cost of capital. The company concludes that somewhere in time capital markets must play a vital role to enhance its growth strategy by providing resources at competitive costs;

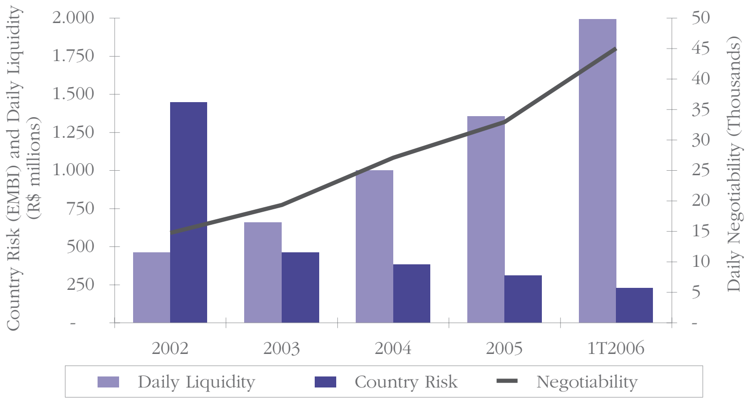
ii) As an institutional strengthening. This includes a number of different intentions: to increase the exposure of the company and its brand name, to search for more professional management, to perpetuate corporate culture, allowing employees to become shareholders and/or promoting the succession process, to increase monitoring toward the company, and submitting to the scrutiny of new partners;

iii) As a mean of wealth liquidity and risk diversification for shareholders and/or their successors. In this instance, the company goes public through a secondary offering, where market investors substitute stakes of founders or of financial groups that came in at previous stages.

Academic studies suggest that most companies' chief motivation for go-

Our Performance

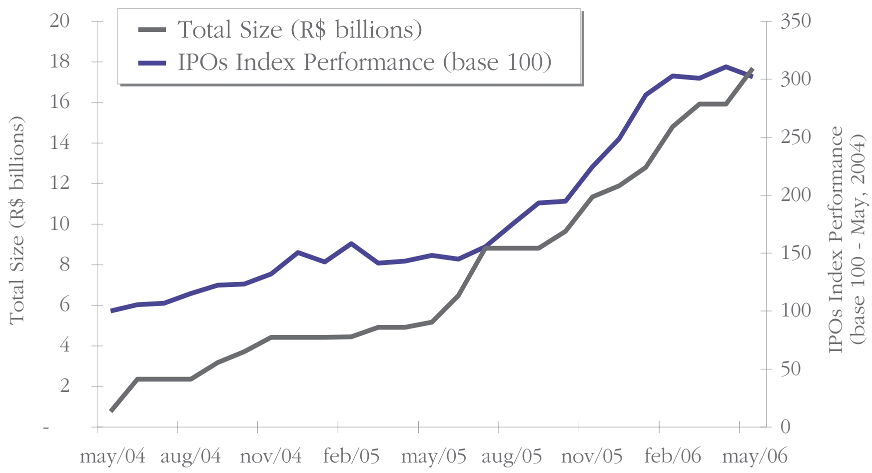
Brazilian Coutry Risk x Liquidity and Negociability in Bovespa



Source: Economática, JPMorgan, Dynamo

Our chief positions performed very well for the period, notably, Itaúsa and Gerdau, and the intermediary position highlights were Duratex, Coelce, and ALL. On the whole, our portfolio showed little change during this quarter, and its liquidity and concentration levels remained slightly above our historic ones. Even after the positive performance of many companies, we remain confident in the fundamentals of our investments.

Chart 2 – IPOs: Size and Performance



Source: Cias, Economática, Dynamo

ing public is usually reason i) above[3]. However, our own experience gleaned from examining recent IPOs in other markets (chiefly, the US and the UK), prevents us from arriving at such conclusive results. Companies have gone public targeting investments and acquisitions, but we have also noted the presence of a number of secondary deals, such as providing liquidity for strategic investors and private equity funds. As a general rule, over the last five years, companies in these two markets have returned more capital to their shareholders via dividends and share repurchases, than they have required money from the market for their capitalization.

This remark seems to more accurately reflect the current pattern of our local initial offerings cycle. Let us examine some of the figures: 51% of the resources obtained to date came from secondary shares sales. Only 42% of the total resources were declared to be destined to investments – both in expansions or acquisitions. The remaining seven percent are for debt payments. In most cases, dividends paid out on the year following the IPO were greater than those of the year preceding the offering. At the same time, few companies recorded substantial capex growth after these transactions[4]. Only two companies on the list are less than five years old and only a further two have been around for less than ten years[5]. In other words, the great majority of IPOs are relatively well established companies, where the demand for primary capital, when this happens, is more likely to arise from consolidation opportunities in their sectors than from the need to invest in expansion projects, which is more common to the early stages of corporate life cycle. Nevertheless, of sixteen companies that allegedly issued shares aimed at future acquisitions, to date, only a few – Dasa, Cosan, Totus, and very recently, ALL – succeeded in acquiring material assets.

This brings us to consider that the proceeds raised by these companies are over estimated. In our understanding, the basic explanation for this does not arise from a sudden deterioration in these businesses environment[6], but for more prosaic reasons. Including a primary stake in the offering improves investors' perception of the quality of the transaction, by easing the antagonism of an exclusively secondary sale (previously, issuer sells/investor buys; now, issuer dilutes/investor buys), while simultaneously suggesting the company's potential to accelerate future growth, and with this trend, giving the impression that investors would be paying a lower adjusted multiple. Moreover, due to the same problem of asymmetrical information, it wouldn't be elegant to explicitly state that the issuers are selling the company simply because they can get a good price. Lastly, the size of the deals also matters in attracting certain investors, in addition to assuring the interest of the bankers and their post-market efforts.

As a rule, the primary rationale for this IPO cycle appears not to be a need for money to finance a specific stage of corporate growth via new projects. It is too early to reach any reliable conclusions, but evidence suggests that factors other than the business cycle, the industry's own dynamics, or competitive pressures, have forced companies into a choice favoring capital market. And this interpretation is consistent with recent statistics on the investment rates to GDP in Brazil and with the aggregate data on industry capacity. According to polls taken with entrepreneurs and executives – also backed by our own empirical evidence – the level of confidence remains low as does the propensity to engage in investment projects. Recent data on new oncoming secondary follow-ons serve only to reinforce this argument[7].

We also cannot attribute the main motive for this sudden rash of IPOs to the second reason. Natura was the only com-

(3) *Just as an example, in a US market survey, Mikkelson, Parth and Shan (1997) report that 85% of the companies interviewed said that they went public to finance working capital and 64% to go through new investments (non-excluding destinations). In another survey of 366 CFOs, Brau and Fawcett (2004) determined that the main reason given by executives for a company to go public is the opportunity to obtain funds for future acquisitions. (As always, the complete references cited can be found in our website).*

(4) *The exception, which merits mention, was Gol, which has already spent all the resources obtained in its two offerings.*

(5) *The criterion applied here was to consider the age of the "corporate projects" themselves. In this case, companies resulting from privatizations, such as ALL and Tractebel, or those that resulted from the merger of existing assets, such as CPFL, Energias do Brasil, and OHL, despite going public only recently, would be considered 'older'.*

(6) *This could even justify the delay in three companies' investments: two in the electric utilities sector (CPFL and Energias do Brasil) and a toll-road concession company (OHL Brasil), which were taken by surprise by the energy price ceilings in the public "new energy" auctions, and by the timing delays of the federal concessions program, respectively.*

(7) *Follow-ons are share offerings that occur after the initial one. They can be primary issues but, in this cycle, have been predominantly secondary.*

	NATURA	GOL	ALL	CPFL	Grendene	DASA	Pto Seguro	R. Maças	Submarino	Localiza	TAM	L. Renner	EdB	OHL	Cyrela
Operational															
Gross Revenues (L12M) - R$ million	2.041	1.683	1.041	8.954	1.402	466	3.085	35	361	634	5.075	1.321	3.851	338	656
EBITDA (L12M) - R$ million	334	354	308	1.623	364	113		9	27	210	443	112	818	207	165
Age (years)	37	4	7	94/9	33	40	59	42	5	32	29	93	107/9	8	43
Gross Revenues (CAGR L3Y)	28%	144%	27%	17%	35%	22%	14%	42%	68%	15%	17%	18%	13%	72%	36%
Gross Revenues (CAGR N3Y)	21%	43%	19%	10%	21%	21%	14%		46%	17%	19%	20%	12%	11%	26%
Capex (Average L3Y) - R$ million	19	103	258	1.324	38	207	102		7	996	335	113	1.514	529	
Capex (Average N3Y) - R$ million	55	1.766	822	1.400	34	160			25	1.500	635	203	1.842	490	16
Pay-out (LTM)	19%	0%	0%	2%	100%	0%	36%		0%	62%	0%	0%	0%	0%	76%
Pay-out (NTM)	72%	14%	10%	8%	100%	0%	54%		26%	35%	16%	82%	16%	0%	25%
Use of the Proceeds:															
Net Debt						30%		17%	67%			69%			
Working Capital		30%		10%		19%		53%	18%		10%	19%	10%	10%	
Capex/Aquisition		70%	100%	90%		51%	100%	30%	15%		90%	12%	90%	90%	100%
Offering															
Data	26/5/04	29/7/04	29/7/04	29/9/04	27/10/04	17/11/04	18/11/04	22/2/05	30/3/05	23/5/05	14/6/05	30/6/05	13/7/05	14/7/05	21/9/05
Corporate Governance "Level"	NM	Nível 2	Nível 2	NM	NM	NM	NM	NM	NM	NM	Nível 2	NM	NM	NM	NM
Size (R$ Million)	768	1.009	588,2	817,88	536	380	328	16	473	247	543	774	1.119	431	785
Primary	0%	54%	45%	83%		29%	24%	100%	29%		70%	30%	99%	31%	65%
Secondary	100%	46%	55%	17%	100%	71%	76%		71%	100%	30%	70%	1%	69%	35%
% Sold	21,75%	20,27%	30,00%	10,52%	17,30%	36,00%	24%	25%	48%	34%	21%	98%	39%	39%	35%
Oversubscription - Nx	9,00	4,50		3,00	8,10	10,00	5,00	1,00	6,00	2,50	2,20	1,50	2,00	1,50	8,00
Filling	144-A	144-A	144-A	144-A	144-A	144-A	144-A		144-A	144-A	144-A	144-A	144-A	144-A	144-A
Sellers Breakdown															
Family/Private Owners	100%	24%			100%	25%	100%			17%	47%	100%		100%	100%
Financial Investor (PE)		76%	100%	100%		74%			100%	83%	53%		100%		
Institutional Investor/Government						1%									
Investors Breakdown															
Brazilian	18%	52%	20%	20%	19%	36%	21%	8%	25%	5%	17%	12%	74%	18%	19%
Foreign	67%	12%	80%	60%	65%	50%	71%	5%	75%	87%	74%	86%	26%	73%	72%
Individuals	15%	36%		20%	16%	14%	8%	87%		8%	9%	2%		9%	8%
Performance															
Performance - First Day	15,6%	5,4%	13,2%	0,1%	12,1%	20,0%	6,4%	1,3%	0,0%	0,0%	0,0%	4,1%	11,2%	1,1%	23,7%
Performance - Since IPO	228,2%	159,7%	214,1%	67,5%	-48,4%	127,5%	94,1%	-57,5%	114,6%	222,6%	180,5%	208,1%	49,7%	38,9%	88,4%
Performance x Ibovespa	70,0%	48,6%	78,6%	6,9%	-67,5%	50,9%	28,1%	-66,8%	52,4%	117,3%	91,8%	112,0%	5,1%	-1,1%	55,5%
Performance x IBX	46,9%	24,8%	50,8%	-5,9%	-70,4%	34,1%	14,3%	-68,8%	42,0%	103,1%	81,1%	101,4%	0,0%	-6,5%	52,8%
Performance x Governance Index (IGC)	33,6%	11,1%	34,9%	-14,6%	-72,8%	23,6%	6,1%	-70,5%	35,4%	94,3%	73,2%	90,6%	-5,4%	-11,1%	46,1%
Daily Liquidity (R$ Million)															
1st Month	15,4	11,1	10,6	9,4	13,7	7,3	7,4	0,3	11,7	2,7	7,8	6,7	7,5	4,6	21,2
3 Months	9,0	5,3	7,2	5,5	7,7	5,8	4,8	0,1	5,7	2,8	5,8	6,4	6,3	3,7	18,7
Last 30 days	15,1	9,8	0,1	6,4	3,1	7,2	7,0	0,0	16,3	6,5	28,2	12,2	4,6	6,7	10,8
% number of trading days below IPO price	0,0%	11,7%	0,0%	32,5%	90,1%	0,0%	0,5%	98,7%	28,8%	8,9%	8,2%	0,0%	0,0%	0,0%	0,0%
IPO Multiples															
EV/EBITDA	7,8	7,7	5,68	5,4	6,9	8,2			14,7	3,75	6,1	7,4	6,4	6,3	10,8
P/L	10,6	13,9	12,5	14,9	11,6	22	6,79		29,9	7,2	7,4	17,6	9,6	16,6	24,9

	Nossa Caixa	Cosan	Tractebel	UOL	Copasa	Vivax	Rossi	Gafisa	Company	TOTVS	Equatorial	ABN	CSU	Brasil Agro	Lupateck
Operational															
Gross Revenues (L12M) - R$ million	6.004	1.960	2.577	531	1.564	304	418	518	156	247	884	434	336		212
EBITDA (L12M) - R$ million		367	1.418	105	568	99	44	65	23	30	189	90	60		56
Age (years)	88	69	8	9	42	9	44	51	23	22	47	12	14		26
Gross Revenues (CAGR L3Y)	2%	16%	34%	-5%	20%	111%	49%	6%	40%	40%	27%	14%	33%		46%
Gross Revenues (CAGR N3Y)	10%	22%	8%	8%	10%	16%	20%	25%	n/d	18%	13%	n/d	n/d		n/d
Capex (Average L3Y) - R$ million	294	1.678	38	84	1.028	156	1	12	14	16	68	27	70		46
Capex (Average N3Y) - R$ million		1.298	57	47	2.418	174	6	29	n/d	10	123	n/d	n/d		n/d
Pay-out (LTM)	51%	0%	95%	0%	54%	0%	13%	0%	30%	25%	25%	33%	71%		62%
Pay-out (NTM)	25%	0%	95%	0%		0%		25%	n/d	25%	n/d	n/d	n/d		n/d
Use of the Proceeds:															
Net Debt						14%	11%	5%							
Working Capital					10%	38%	5%	20%	7%	7%			50%		20%
Capex/Aquisition		100%		100%	90%	48%	84%	75%	93%	93%	100%		50%	100%	80%
Offering															
Data	26/10/05	16/11/05	7/12/05	14/12/05	6/2/06	6/2/06	13/2/06	16/2/06	23/2/06	7/3/06	30/3/06	25/4/06	27/4/06	27/4/06	11/5/06
Corporate Governance "Level"	NM	NM	NM	Nível 2	NM	Nível 2	NM	NM	NM	NM	Nível 2	NM	NM	NM	NM
Size (R$ Million)	830	770	923	555	723	470	900	816	245	400	470	480	341	518	429
Primary		100%		50%	100%	13%	72%	61%	74%	71%	40%		29%	100%	36%
Secondary	100%		100%	50%		88%	28%	39%	26%	29%	60%	100%	71%		64%
% Sold	25%	27%	11%	26%	28%	59%	48%	40%	45%	47%	49%	56%	39%		43%
Oversubscription - Nx	10,00	11,00	5,00	13,00	4,00	12,00	7,00	13,00	6,60	6,00	6,50	7,50	8,00	2,00	13,80
Filling	144-A	144-A	144-A	144-A	144-A	144-A	144-A	144-A	144-A	144-A	144-A	144-A	144-A	144-A	144-A
Sellers Breakdown															
Family/Private Owners			77%	32%			100%		100%	71%		74%	100%		43%
Financial Investor (PE)				68%		100%		100%		12%	100%	26%			42%
Institutional Investor/Government	100%		23%							17%					15%
Investors Breakdown															
Brazilian	22%	19%	37%	21%	26%	20%	20%	28%	25%	31%	23%	9%	26%	18%	28%
Foreign	71%	72%	55%	71%	74%	70%	80%	72%	64%	69%	68%	65%	64%	82%	62%
Individuals	7%	8%	8%	8%		10%			11%		10%	26%	10%		10%
Performance															
Performance - First Day	17,6%	15,8%	8,8%	16,7%	4,7%	10,6%	0,0%	29,5%	18,8%	6,3%	17,0%	5,9%	-2,8%	10,0%	6,0%
Performance - Since IPO	41,0%	191,7%	25,8%	-33,8%	-19,1%	20,2%	-26,0%	8,1%	-24,8%	16,9%	-2,8%	-11,8%	-16,7%	14,0%	-2,5%
Performance x Ibovespa	12,8%	149,0%	13,1%	-39,7%	-18,8%	20,7%	-26,6%	13,6%	-19,0%	19,7%	1,4%	-1,0%	-7,5%	26,5%	6,4%
Performance x IBX	9,1%	143,3%	10,7%	-41,3%	-18,7%	20,8%	-26,6%	12,5%	-19,6%	18,0%	-0,4%	-1,6%	-10,8%	22,0%	5,0%
Performance x Governance Index (IGC)	6,8%	145,6%	12,1%	-41,2%	-18,2%	21,6%	-24,8%	14,3%	-18,0%	19,8%	1,7%	-0,3%	-10,8%	22,0%	5,3%
Daily Liquidity (R$ Million)															
1st Month	29,7	33,5	19,7	25,2	13,8	13,8	29,6	27,7	7,0	11,2	19,4	13,5	12,7	1,8	12,6
3 Months	17,6	31,0	12,2	12,4	9,6	10,9	24,7	23,4	6,6	11,2	19,4	13,5	12,7	1,8	12,6
Last 30 days	6,1	33,2	6,0	5,5	3,2	5,9	15,4	12,6	3,8	11,2	19,4	13,5	12,7	1,8	12,6
% number of trading days below IPO price	0,0%	0,0%	0,0%	74,6%	51,1%	0,0%	43,2%	1,4%	32,3%	57,5%	5,0%	59,7%	63,3%	4,5%	31,4%
IPO Multiples															
EV/EBITDA		7,6	6,4	22,00	5,3	9,0	18,3	19,2		14,1	5,1	8,6	6,2		10,4
P/L		29,3	9,9	26,33	9,7	62,55	23,3	31,9		21,9	9,4	13,0	25,8		19,4

Source: Cos, Banks Coordinators, Economática, Dynamo

General Note: We use to adjust data for extraordinary itens and/or relevant accounting provisions. As for the extension of the table, notes would be too long, and this time we decided to present 'crude' numbers. Only as an exemple, Vivax P/E adjusted for cable licences depreciation and for premium over bookvalue over Canbras aquisition would be 13,4x instead of 62,5x.

Nomenclature: L12M - Last 12 Months; N12M - Next 12 Months; CARG L3Y - Compound Annual Rate of Growth 3 Years before IPO; CARG N3Y - Compound Annual Rate of Growth 3 Years after IPO; NM - "Novo Mercado" - Bovespa highest Corporate Governance Standarts.

pany that formally stated institutional reasons for going public in its prospectus, the official document sent to CVM[8].

To date, secondary shares sales, regardless of whether held by strategic shareholders, a family control group, or financial investors, seem to have played a vital role in the decision to seek a listing in the Bovespa. Our equity market has achieved successive historic price and volume records, liquidity has been abundant with the arrival of overseas resources, and increasing market-share of individuals investors. To assure liquidity to some shareholders aiming to maximize their portfolio diversification is an authentic motivation, and timing the offerings when markets pay the desired prices, frequently represents the merited closing of a successful entrepreneurial cycle. Nevertheless, there is no denying that this type of motivation lessens the attraction for investors such as Dynamo, particularly, in view of the fact that, in a number of these recent cases, the market has offered prices higher than those that strategic investors are prepared to pay. In theory, entrepreneurs and executives have a deeper specific knowledge about their businesses than market financial investors, with their broader portfolio view.

IPOs and Markets

There is much documented evidence of the phenomenon known as the 'hot issues markets' in IPO. In other words, initial public offerings tend to be cyclical, where entrepreneurs seek windows of market opportunities to sell their companies[9]. In line with behavioral researches, several studies associate IPO movement with periods of investor´s excess of confidence. This same type of survey further argues that companies follow in the footsteps of their predecessors in the same IPO cycle. This gives rise to a sector cluster phenomenon. In this ongoing cycle, it is interesting to observe the presence of no less than four real estates companies, with another three currently under CVM analysis. An exercise of mental curiosity is to imagine the profile of this IPO cycle had it had not been inaugurated by such premium quality companies as Natura, ALL, and Gol.

To date, in this cycle, IPO size and performance have advanced side by side (chart 2). What is not so apparent is the causal relationship here. Behavioral premise suggests that size variations of the new offerings derive from recent performance of companies just '*IPOed*'. The chart more shrewdly suggests an inverse relationship; one where volume growth tends to be swiftly followed by price increases, thereby evidencing a slightly greater correlation for the time lag of one month. One explanation for this phenomenon, known as first day *underpricing*, as we shall see in our next Letter, justifies this pattern of IPO appreciation immediately after shares begin to be traded. A good barometer for measuring the premise that IPO decision is conditional upon market price performance is the subsequent rash of postponements/cancellations of offerings at CVM, that tend to occur when the market shows signs of cooling down. But, no signs of that, to date.

Dynamo Cougar x IBX x Ibovespa
Performance up to december/2005 (in R$)

Period	Dynamo Cougar	IBX	Ibovespa
60 months	386,03%	288,34%	167,75%
36 months	244,19%	262,20%	235,20%
24 months	104,20%	101,47%	71,37%
12 months	44,31%	50,41%	42,31%
3 months	14,45%	13,77%	13,70%

NAV/Share on March 31th, 2006 = R$ 122,967570260

Breaking News: as this Letter was going to press, we heard that a bank notorious for its high IPO activity has decided to postpone its backlog operations.

There is nothing to criticize in this approach, one that is part and parcel of the healthy 'animal spirit' of entrepreneurial activities, where advantage must be taken of every market opportunity that presents itself. There is also no reason to claim that investors operate in a state of 'Rousseauesque' innocence. Players in our market must be mature enough to perceive cyclical movements as well as the intrinsic risk of buying companies with no trading history. If the efficient market assumption is merely a theoretical construct, it either makes no sense to admit the theory that companies are rational agents and investors a band of ambitious absentminded. On the other hand, vocation for public company requires more enduring commitments other than a mere opportunity to maximize family wealth or capital gains for foreign head offices[10]. And boundaries here are less clear. When the original intention is ephemeral and merely one of opportunity, the subsequent relationship between shareholders is transformed into an intolerable obligation. We have already seen this before, a hangover from an era when many companies joined *Bovespa* purely to take advantage of tax benefits.

The big difference today is the quality of the by-laws, duly adapted to the rules of *Novo Mercado* or to *Bovespa Level 2*[11]. This is a significant advance and deserv-

(8) *At their pre-marketing stage, both Localiza and ALL also stated that institutional reasons had weighed in their decision to go public, but they did not go so far as to formalize this in their prospectuses.*

(9) *For example, Ibbotson and Jaffe (1975), Pagano, Panetta and Zingales (1995), Ritter (1998), Lowry (2001), Lowry and Schwert (2002). Brau and Fawcett (2004), in their direct survey with CFOs, also uphold this theory.*

(10) *In this last case, the perception of an appreciated Brazilian exchange rate reinforces the opportunity to cash resources.*

(11) *These are the highest standards of Corporate Governance for companies listed in São Paulo Stock Exchange.*

ing of the credit for the success of this new cycle of issues. The thesis that we have upheld for some time that the combination of competent management, with good reputation, in a legal arrangement based upon fair rules for all shareholders, and complying with best corporate governance practices, should be able to access capital markets at competitive prices, is now an indisputable reality. However, we have also pointed out that good statutes do not fix bad business, do not sustain excessive evaluations, nor rectify tortuous intentions.

On the other hand, the good performance of the companies listed under *Novo Mercado* rules has begun to produce a positive demonstration-effect, that motivates and attracts other companies such as, for example, Perdigão and Embraer that have already disclosed their corporate restructuring plans, involving migration to a higher level of *Bovespa* corporate governance.

Despite the generally high quality of companies that are going public under a more reliable legal framework, investors should remain alert and selective. This is because some not so interesting assets and/or less principled intentions probably will infiltrate the cycle, on the back of their predecessors' partial success.

In our next Letter, we shall examine in more detail whether these recent Brazilian IPOs are aligned with the typical standards of other markets, and also analyze the internal mechanics of the deals. We shall then be in a position to form a broader understand about the subject and about Dynamo's role on these offerings.

Rio de Janeiro, June 6th, 2006

Dynamo Cougar x Ibovespa x FGV-100 (in US$ dollars)

Period	DYNAMO COUGAR*			FGV-100**			IBOVESPA***		
	Quarter	Year to Date	Since 01/09/93	Quarter	Year to Date	Since 01/09/93	Quarter	Year to Date	Since 01/09/93
1993	-	38.78	38.78	-	9.07	9.07	-	11.12	11.12
1994	-	245.55	379.54	-	165.25	189.30	-	58.59	76.22
1995	-	-3.62	362.20	-	-35.06	87.87	-	-13.48	52.47
1996	-	53.56	609.75	-	6.62	100.30	-	53.19	133.57
1997	-	-6.20	565.50	-	-4.10	92.00	-	34.40	213.80
1998	-	-19.14	438.13	-	-31.49	31.54	-	-38.4	93.27
1999	-	104.64	1,001.24	-	116.46	184.73	-	69.49	227.58
2000	-	3.02	1,034.53	-	-2.63	177.23	-	-18.08	168.33
2001	-	-6.36	962.40	-	-8.84	152.71	-	-23.98	103.99
1stQuar/02	13.05	13.05	1,101.05	3.89	3.89	162.55	-2.76	-2.76	98.35
2ndQuar/02	-19.15	-8.60	871.04	-22.45	-19.43	103.60	-31.62	-33.51	35.63
3rdQuar/02	-22.31	-28.99	654.37	-31.78	-45.04	38.90	-44.17	-62.88	-24.28
4thQuar/02	29.76	-7.86	878.90	38.00	-24.15	91.67	45.43	-46.01	10.12
1stQuar/03	4.47	4.47	922.65	4.63	4.63	100.55	5.39	5.39	16.06
2ndQuar/03	27.29	32.98	1,201.73	38.16	44.55	177.07	34.33	41.58	55.91
3rdQuar/03	19.37	58.73	1,453.83	24.72	80.29	245.56	22.34	73.20	90.74
4thQuar/03	22.18	93.94	1,798.51	35.98	145.16	369.91	39.17	141.04	165.44
1stQuar/04	4.67	4.67	1,887.16	2.35	2.35	380.16	-1.40	-1.40	161.72
2ndQuar/04	-4.89	-0.45	1,790.04	-8.66	-6.51	339.30	-11.31	-12.56	132.11
3rdQuar/04	35.12	34.52	2,453.91	23.73	15.67	443.56	21.13	5.92	181.16
4thQuar/04	22.17	64.35	3,020.19	25.32	44.96	581.16	21.00	28.16	240.19
1stQuar/05	-1.69	-1.69	2,967.41	-1.66	-1.66	569.87	1.06	1.06	243.80
2ndQuar/05	5.41	3.62	3,133.23	2.98	1.27	589.80	7.51	8.65	269.60
3rdQuar/05	32.32	37.12	4,178.29	25.21	26.80	763.71	31.63	43.01	386.50
4thQuar/05	2.97	41.19	4,305.49	3.13	30.77	790.73	0.75	44.09	390.17
1stQuar/06	23.32	23.32	5,332.90	18.89	18.89	958.98	22.51	22.51	500.48

Average Net Asset Value for Dynamo Cougar (Last 36 months): R$ 411.125.465,53

(*) 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 average.

Please visit our website if you would like to compare the performance of Dynamo funds to other indices: ***www.dynamo.com.br***

For any further information, visit our web site:
www.dynamo.com.br

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