mar asset management

Our first 12 months

Letter: February, 2020

HOW WE DEFINE OURSELVES

Despite no precise definition, a *hedge fund* undoubtedly holds three features. The first is its regulatory flexibility, allowing investment allocations across different asset classes, increasing the scope of investment opportunities it can take advantage of. The second is related to its compensation model, mainly through performance fees. A last but no less important feature is the possibility of combining long and short positions, which allows better control of market risks and greater portfolio leverage.

Still, in order to consistently get above market returns, a Hedge Fund needs something more. It needs to find an edge.

And where does **our** edge come from?

It comes from a powerful combination of macro investments and stock picking centered on a single book. That is encoded in our DNA.

In our first year, the synergies between those two strategies (macro and equity) proved to be our main edge. This could hardly be replicated by running two different funds. We hold the strategies as part of one another, we debate them all along. That may be the best way to define our investment model: a constant search for investment asymmetries in different asset classes, allowing an optimization of the risk return ratio in our portfolio.

This is what we are. A hedge fund and an edge fund. We are constantly looking for an edge, with focus on capital preservation and absolute returns. To do so, our partnership model values intellectual honesty as a steady exercise. It is a model that acknowledges the limits of our individual skillsets. Moreover, it values the true alignment of the best interests between the team and shareholders.

We are **MAR Asset.**

PERFORMANCE REVIEW 2019

MAR Absoluto celebrated its first anniversary at the end of January 2020. From an entrepreneurial perspective, it was a year full of learning, challenges, mistakes, and successes.

Throughout this period, we sure had a bit of luck since markets were such generous providers of opportunities (as they usually are). Nonetheless, results demonstrate our consistency - the synergies between the strategies are real - and a natural compatibility with consensual decision management, where no separations of risk limits are made between different asset classes.

We would like to especially thank the Founders' Round investors, those who believed in us when we were still an idea in a piece of paper. Should be noteworthy now that those words written on that paper were followed strictly throughout the year, as we built our portfolio.

In practice, these first 12 months went as following:

/ Expressive above CDI +10% return (our long-term goal), with an average stress risk level of 20%;

/ Positive contribution of macro strategies (long on short term yields);

/ Relevant contribution from stock pickings (our *BTG Pactual* stock thesis is a highlight);

/ Some theses went wrong too (long Argentine Peso and Brazilian Real against US Dollar)

The fund's average volatility was 9.7%. The highest drawdown was 6% in August. Our Sharpe was at 2.2.

Once again, we cannot stress enough how determinant our portfolio management model was, as well as our liability (shareholders) profile that allowed us to navigate smoothly through market volatilities.

What 2019 was all about?

At the beginning, we found 2019 to be a year of great opportunities and noticeably clear risks to look at. The dynamics between a newly appointed Bolsonaro government and the National Congress were key to watch, first and foremost in regards of the Pension Reform agenda. For this reason, most of our portfolio risk was invested in short term yields during the first half of the year. By the second half, as more favorable macroeconomic winds prevailed, we gave stocks way more space, as we grew our confidence in our specific thesis behind each of the invested companies.

What was on our minds for first year half?

When the year first started, a sense of an extremely favorable environment for the country was predominant in the market. The so much needed liberal approach should be able to produce mid and long-term benefits, clearly. However, the short-term impact of those same liberal policies was extremely contractionary for economic activity, given its fiscal and parafiscal tightening spectrum.

As a result of such cases, the resumption of growth is naturally impaired in the short term, while the inflationary outlook and the country's debt dynamics are greatly improved.

In situations where productive capacity sits idle, it is usually the norm that a combination of inflation under control, fiscal stability, and low growth lead to a natural downward of interest rates.

We then realized that the Selic rate should find its balance well below where the market was pointing at. In this context, we saw a high potential for cuts by the Banco Central.

Which is why we then structured a relevant position in the short-term Jan20 rate right away when the fund was launched, in February 2019.

In stocks, we concentrated ourselves on a few theses. The most important one was the long position in *BTG Pactual*, which carried a remarkably interesting asymmetry that we found to be not much dependent on the macro scenario.

On the other hand, if we happened to be wrong about the contractionary fiscal effect or, in other words, if general confidence were sufficient to make the country grow, interest rate cuts would not come, while stock prices should move up significantly. Because of that, we also held a long position on stock indexes.

So, while in respect of the short-term growth factor we felt capable of performing well either way, regardless of the weather, an eventual rejection of the Pension Reform was still a relevant portfolio risk at play.

As a precaution, we were also long on implicit inflation at 3.9%. The instrument seemed to be the variable priced at the top of market's optimism, therefore holding the greatest asymmetry if the Pension Reform were not to be approved. If that sad hypothesis confirmed, the whole debate around the sustainability of national's debt/GDP ratio would turn on its volume even more, and long-term inflation should move towards double digits.

That was basically our full shopping cart: short-term DI yields; a few specific companies with a bit of stock index; long-term implicit inflation. Also, we set up a BRL option (against the usd) strategy, a low-cost position with high leverage and low implicit volatility, as we believed in BRL's appreciation.

When the Pension Reform was approved in the first voting round in July, two things became clear: a downward cycle of interest rates was around the corner; and stock prices should be revalued upwards. At the same time, a few more companies earned our confidence.

The second half

The second half of the year was fundamentally a time to watch our thesis to mature. We rarely switched positions during that period. Instead, our attention and time was allocated to further in-depth research.

The month of August is especially noteworthy, as we went through our biggest share value drawdown. Two specific events negatively affected our portfolio in that month: the federal issuance and execution of a search and seizure warrant at *BTG*'s offices; and the disclosure of primary election results in Argentina.

Macri's unlikely chance of reelection strike us as an enormous surprise. It hit our long Peso position, placed to surf the extremely high interest rates (70% year) during the electoral period. We never intended to bet on the reelection of Macri, but to take advantage of that period.

Since primaries came way worse than market's expectations, the result of the election - held in October- was pretty much anticipated (against Macri). Thus, our position lost its fundamentals and we left it, losing around 2.5% of our value.

The following months proved that our main theses were to mature, and the year was concluded with a 27.35% accumulated return.

STOCK PICKING

During these first twelve months, our stock picking strategy accounted for the highest stake of our returns: 16.2pp + CDI. Considering our level of exposure to stocks at 20% of the portfolio, that return was quite significant. Moving forward, although we always seek the highest risk/return ratios, we acknowledge how hard it is to replicate that.

Our highlights were *BTG Pactual*, *Centauro*, *Natura* and *Iguatemi* (in order of contribution), companies that still integrate our portfolio. Together, they added up 13.3pp above CDI. If on one hand we see an unique story behind each one of them, on the other hand they all share an identical recipe: exceptional teams running good solid businesses, in positions to extra benefit tremendously in face of mid and long-term potential externalities and behavioral disruptions.

In early 2019, *BTG Pactual* seemed like a very glaring opportunity. The stock still reflected a traumatic event (Andre Esteves's prison in 2015), trading at a discounted valuation (1.2x P/B; 8x P/E - 2019). However, the business itself was clearly breathing a different air. Results of their main customer franchises (Asset and Wealth Management) were about to touch their historical tops. Management focus was firm on the mission to make the bank more client oriented and less proprietary capital oriented. Confronting that to a growing participation of capital markets in the Brazilian economy, we felt confident the stock would rally up.

But there was more.

After a few years of experiments and pivots, *BTG Digital* started to build momentum. Brazilians were getting on track of going digital on their financial routines. Autonomous agents became popular service providers, after a long way paved by *XP Investimentos*. In parallel, *BTG* was already the 6th largest bank in Brazil, holding a large record on credit and no legacy systems. So, it seemed to us that their retail success was finally to come.

Despite a bit of turbulence in the month of August, the stock price is up 150% ever since we bought it.

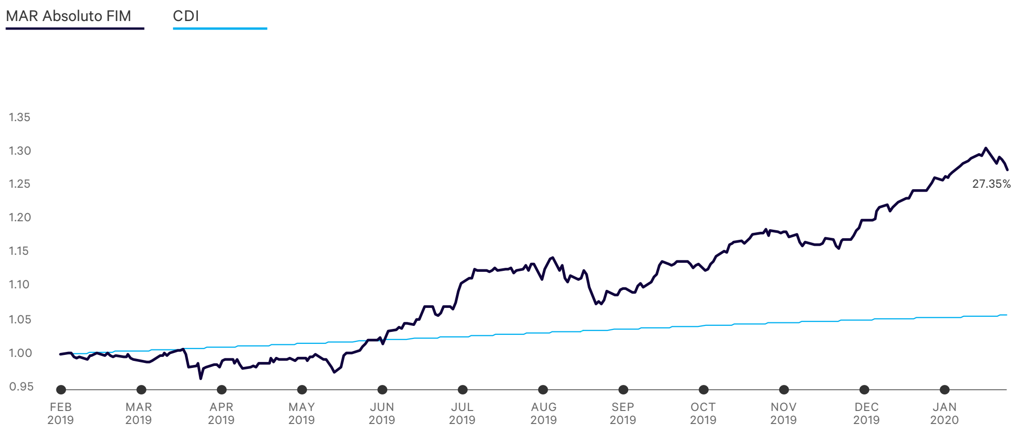
Between June and August, *Centauro*'s stock drew our attention. We saw a capitalized, organized company freed of years of financial restrictions. We saw a leader (5% market share) in an extremely fragmented market, beautifully executing its omnichannel new strategy. With new stores signed and old ones reforming, revenue growth was a sure thing, although the stock was still trading at 12x P/E (2020). For a company that can potentially deliver years of systematic and sustainable double-digit growth, we felt that to be cheap.

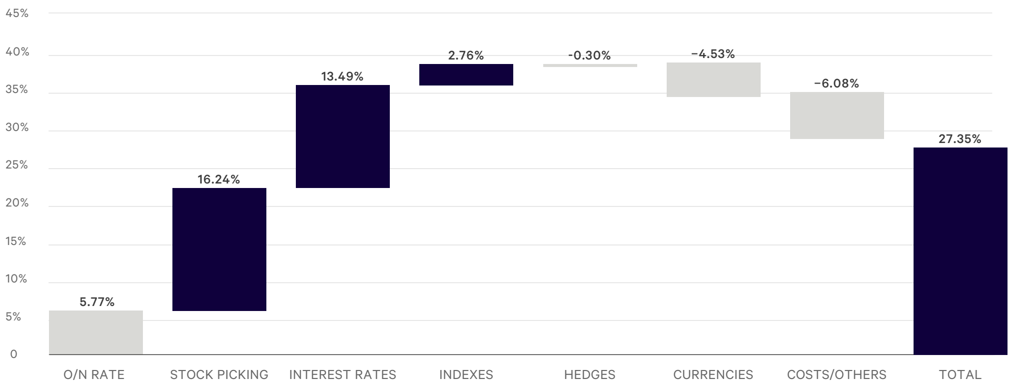
As sports and physical activities become more of a cultural *pilar*, *Centauro* might become a whole ecosystem, increasing customer loyalty and delivering even more value through its online marketplace. Leaded by Pedro Zemel, they sure have a strong management team and the tolls to execute this bold long-term vision. Meanwhile, the company is completely backed by their two biggest shareholders, founder Sebastião Bonfim and GP Investment's Fersen Lambranho (Board's Chairman and Vice Chairman, respectively).

Centauro's stock also appreciated over 100% ever since we bought in.

PERFORMANCE

2019, February 1st to 2020, January 31th





TEAM

The small team company aspect is in our DNA. For our partnership to be effective, our headcount shall be small. In 2019, we were a team of six people: three in investment and management and three in the operational part.

At the end of the year we brought in Leonardo Andrade. Besides his surf passion and love for the ocean, the 27 years old new member has a solid background in corporative analysis, focused on M&A and Private Equity. Welcome, Leo!

In 2020, we plan to bring three more people to the investment team.

AUM

The value of **MAR**'s total assets under management increased from R$ 40Milion to R$145Million. We stick to the plan of attracting the right clients in the right way, as oppose to pursuit more size. Our focus is on performance.

Once again, we appreciate your support and partnership.
We would love to hear what you think about markets, our portfolio or our values.
We are committed to deliver continuous performance, taking advantage of different classes of assets, as well as of noises around markets in general.
Have a good year and thank you for your continued support.

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