

In 2022, the Vista FIA return was -12.1% compared to -6.0% of the Bovespa Index in the same period.

The Vista Long Biased return was -8.3%, compared to 5.4% of the CDI in the same period.

Since its inception on January 1, 2015, the Vista FIA return is +179.7%, compared to +97.1% of the Bovespa Index in the same period.

Since October 26th, 2018, the Vista Long Biased fund return is +33.7% compared to +21.1% of the CDI in the same period.

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In the previous letter, we addressed the issue of value generation through divestments, when a company releases human and financial capital for more efficient uses through the sale of assets. In this letter, we will comment on the main driver for generating value for the shareholder: capital allocation.

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When analyzing a company, the investor compares the present value of future cash generation with the current price of the business. Often, for the sake of simplification, the investor assumes in its projections that all cash generated will be returned to the shareholder. In real terms, most of this capital will be reinvested¹, and here lies an important part of the complexity of investing in stocks: in addition to understanding the cash generation capacity of existing

¹Just out of curiosity, a study published by Michael Mauboussin in 2015 on capital allocation showed that investments made by

assets, the investor needs to be aware of the ability of their managers to reinvest the cash generated.

Broadly, a company has three major destinations for capital:

- i. allocation to organic investments, whether in fixed assets, R&D, or increase in working capital;
- ii. allocation in mergers and acquisitions of other assets or companies (M&A);
- iii. return of capital to the shareholder, via repurchase of shares or payment of dividends.

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Right and wrong decisions have a ripple effect on the company's future. He who knows the best marginal alternative to the use of money ends up creating an important advantage: using the extraordinary returns of past decisions to finance the capital needs of future cycles, thus minimizing dependence on external sources of money.

To enable the constant search for value generation, it is essential that the effective owners of the business put in place correct incentives for managers and that they have a symbiotic relationship to guide them on this journey directly or through the board of directors. Inadequate incentives tend to favor the generation of value in the short term over the long term of the business. Goals linked only to the result without considering the amount of capital invested, for example,

American companies between the post-World War II and 2014 were 80% financed by the companies' own cash generation.

cause finite resources to be allocated without returns and opportunity costs analysis.

We believe that the most appropriate way to gain comfort with a company's ability to allocate is to thoroughly investigate the decision-making of the same managers in past investments.

*"Prediction is very difficult, especially about the future"*²

At this stage, we looked back at the path taken by the company so far, seeking to understand: what was the strategic rationale for investment decisions; how and by whom they were approved; the type of financing used; the minimum rate of return required for approval; and the risk additions or distractions that came with it.

To understand value generation in mergers and acquisitions, the investor needs to make sure that the premium³ paid by the acquirer does not exceed the benefits generated in the business combination. The benefits may be of an operational nature as in cases of sales synergies, improvements in expense productivity and tax; or also have a defensive profile, in which the buyer removes a competitor or risk factor from the market, which in turn could destroy value in the future.

Being positioned in the right industry - with growth and competitive discipline - is already a big advantage, but it is not enough. The company needs to have the skills and appetite to fill in these spaces efficiently in capital and risk.

²Niels Bohr, chemist

³What accounting cannot reclassify into fixed and intangible assets or working capital is recorded as goodwill in the buyer's balance sheet as a way to reflect the future expectation of cash generation from the acquisition.

We often come across managers who can create important competitive differentials over time, even in industries that *ex ante* did not seem to present obvious opportunities for value generation. They are companies that build advantages by gaining operational efficiency at each critical point of the business, building an entry barrier that is difficult to replicate because it is not present in a single factor. Therefore, we do not exclude from the portfolio investments in historically more competitive industries.

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Eneva

Eneva (originally MPX) started its activities in 2001, dedicated to the management of coal-fired thermoelectric plants. The predominance of gas as an energy source and the main current business model – the fully verticalized Reservoir to Wire (R2W)⁴ – emerged only in 2009, with the right to explore the blocks in the Parnaíba Basin.

Gas exploration in Parnaíba began through a joint venture with OGX, which was responsible for supplying MPX's thermoelectric plants, located on the same site. From 2013, the deterioration of the EBX group froze new exploratory investments and the absence of the discovery of new gas reserves started to threaten electricity generation. In the same period, MPX suffered from the payment of penalties for unscheduled

⁴Reservoir to Wire (R2W) is a type of thermoelectric generation where the gas used by the plant is produced in the vicinity of the project itself.

downtime in coal-fired power plants and delays in the completion of some projects.

The operational and financial deterioration rapidly accentuated and culminated in the judicial recovery initiated at the end of 2014. During the process, former creditors Cambuhy and BTG took over corporate control and hired a new team of managers with the mission of tidying up the house.

The verticalization of gas exploration and production, thermoelectric generation, and energy trading activities would create some of the company's competitive advantages – cheap access to gas molecules, reduced global price exposure, generation flexibility – which, after a troubled start, would allow a sequence of successful investments.

In the first year of the new management, the operating cost of the plants fell 16% and availability rose 68% to 96%, between the second half of 2016 and the second half of 2017. The operational inefficiencies correction and the profitability recovery in existing operations made it possible to resume growth.

The company, which at this point was known as Eneva, recognized the economic attractiveness of onshore gas compared to offshore gas, given the lower technological and monetary effort, and was well positioned during a transition in the Brazilian electro energetic matrix.

In the last decade, the accelerated adoption of wind and solar sources has introduced into the system new forms of non-controllable and intermittent generation, which already reach 12% of the country's generation capacity. In the same period, the environmental agenda

prevented the construction of new hydroelectric plants with storage reservoirs, which were historically used to neutralize the risk of generating sources whose availability is uncertain and not storable.

In the absence of reservoirs, the long-term planning of the electricity sector began to predict a greater penetration of thermoelectric generation in the system, bringing the necessary predictability for Eneva to develop its investment plan.

The company accelerated the exploration and development of the fields in Parnaíba, increasing proven reserves by more than 65%, which enabled thermoelectric projects with returns estimated at 20% in real terms without leverage.

In December 2017, the company obtained the right to explore the Azulão Field, which would prove to be one of its best investments. Located in the Amazon Basin, Azulão is one of the last prolific onshore gas frontiers in the country. The operation means the possibility of exploring the R2W model in a new location and preventing a competitor from establishing itself in the region. The project got even better when the isolated system of Roraima, which bought energy from Venezuela, faced difficulties to import energy and the government had to auction for the region's electric service. As the state is more than a thousand kilometers away from the Azulão field and presents logistical challenges intrinsic to the forest region, the use of Eneva's gas relied on a previously unprecedented solution in Brazil: transport the gas in liquefied form (LNG) in trailers from the Azulão field to Boa Vista. The company won the auction and made it possible to

allocate R\$2.0 billion to a projected return, in our analysis, of more than 20% in real terms.

The potential of the project of Azulão would not be exhausted in this auction. The new field and the new model made Eneva the largest LNG producer in Brazil, developing skills that would unlock the possibility of supplying LNG directly to industrial customers, as shown by the recent and unprecedented supply contract with Suzano and Vale. In addition, at first, the reserves of the field were only sufficient to honor the 130 MW contract of the Jagatirica plant, but after the successful development of the asset, Eneva will be able to enable about 1,000 MW in new thermoelectric projects to be enabled in future auctions.

A good capital allocator should also know how to back down from seemingly attractive opportunities when recognizing better uses for money. During 2021, there was a great expectation about Eneva's purchase of the Urucu⁵ oil and gas production pole. Buying the hub meant entering the last major onshore gas frontier in northern Brazil. During negotiation, Petrobras raised the price required for the asset due to the increase in oil prices and Eneva decided not to move forward with the acquisition.

Even with the great value generation observed in recent years, the future of Eneva still looks promising. Outside the electricity sector, the gas market is still taking its first steps. The Gas Law, a legal framework that organizes the sector and creates incentives for competition, is recent,

having been enacted only in 2021. Historically, every molecule of gas consumed in Brazil had to go through Petrobras, which has the monopoly in every part of the chain. After the law and the adoption of anti-trust commitments and divestments by the state-owned company, today we see a more mature market with independent participants managing their own infrastructures and their natural gas portfolios.

In its most recent movement, Eneva acquired CELSE, the largest thermal plant in Brazil located in the state of Sergipe. In the case of a low-risk asset acquisition, at first, the expected return is lower. However, we believe that the acquisition not only removes the possibility of a competitor settling in the region, but puts in the hands of Eneva one of the few private regasification terminals in the country, capable of supplying gas to the interconnected gas network. The investment allows Eneva to act as an important gas supplier for local distributors and customers of the still incipient gas free market in the future.

Searching diversification, Eneva acquired Focus. Before being acquired, Focus faced a serious solvency problem: after a large cost overrun in its project and without the possibility of adding leverage, the company did not have the resources to continue the project. Eneva took advantage of this market condition and quickly structured an operation where it injected resources into the company and took control of the business. The opportunistic reading granted entry into renewables at

⁵ Urucu is the largest onshore natural gas producing field with the largest proven reserves located in a remote region of the state of Amazonia.

an estimated real return around 16%, very high when compared to other similar transactions⁶.

In recent years, Eneva has negotiated with a premium in relation to its peers when we consider only projects already contracted. To date, this premium has been justified as the *company* has been able to identify new opportunities for capital allocation to high returns. We believe that the investments made by the current management in the construction of competitive advantages and the development of new growth platforms will allow the company to continue allocating a large volume of capital in the long term with returns substantially above its cost of capital.

Itaú

One of our investments is Itaú-Unibanco⁷, a name rightly derived from the merger that took place in 2008 between two competitors that created the largest private bank in the country. The history of both institutions is based on numerous acquisitions that consolidated the national banking sector, getting the conglomerate into adjacent businesses and creating a vertical company in various segments of the financial sector.

Although new entrants are attacking individual segments, by bringing value propositions to customers that are more appropriate to the present day, for

decades the verticalization resulting from the acquisition process has generated a great amount of return for the bank. From 1995 until the merger with Unibanco in 2008, Itaú made at least one relevant acquisition per year and the capital used in them represented 35% of the accumulated profit in the period⁸. During this period, the bank composed its equity⁹ at the rate of 28% per year.

After the merger with Unibanco, the Central Bank and CADE (Brazil's antitrust authority) became more restrictive with the acquisitions made by the company, in addition to imposing several microeconomic agendas to encourage competition. Still, since then the bank has managed to make up its capital at 19% a year.

Acquisitions in the banking sector have long had very clear levers of gains. An institution with greater scale and retail exposure had access to better funding, enabling the purchase of smaller institutions in order to gain competitiveness. Another important cost synergy came from the integration of backoffices and greater scale in processing. Banks also gained in capillarity and scale by adding branch networks and customer portfolios of those acquired, which increased price power in specific segments or regions. The acquisitions of state banks at the time of privatizations brought

⁶ With a low barrier and easy to operate, acquisitions in the renewable generation sector have typically low returns.

⁷ Itaú is a name that comes from an acquisition in 1963, 20 years after the founding of the Central Bank of Credit by Alfredo Egydio de Souza Aranha. And Unibanco literally comes from the Brazilian Union of Banks, a name adopted by Banco Moreira Salles after the purchase of Banco Agrícola Mercantil in 1967.

⁸ Another 25% of the accumulated profits in the period were paid in dividends to shareholders and 40% retained for organic growth.

⁹ Average ROE of the period. Approximately also the number verified in the growth rate of equity value per share with added dividends paid to shareholders.

acceleration in regional expansion¹⁰, as well as good customer bases.

Itaú also often used acquisitions to strengthen competencies and segments where it was not so dominant:

- i. High income segment: acquisition of Banco Francês Brasileiro in 1996, which brought the Personalité brand, and the retail portfolio of Citibank Brazil in 2016;
- ii. Wholesale and Private Banking segment: acquisition of BBA in 2002;
- iii. Vehicle market: acquisition of Banco Fiat also in 2002;
- iv. Life and pension plan: acquisition of the portfolio of AGF Brasil Seguros in 2003; and
- v. Cards: acquisition of Credicard in 2013.

The merger and acquisitions had also been part of the international expansion, with the acquisitions of the Bank Del Buen Ayre in 1998, BankBoston in 2006, and Corpbanca in 2014. Here, however, we believe that they were not good capital allocation decisions, because the bank was not able to achieve dominance positions in the main markets it entered, certainly thwarting risk diversification plans outside Brazil.

The bank has also been exceptionally skilled over time in keeping key people in its major acquisitions, using them to strengthen its staff. This ability to aggregate

different cultures is essential to succeed in a merger or acquisition. In its main acquisition, Itaú managed to reconcile different cultures and shareholders by joining with Unibanco, creating a joint board and even changing its own name to accommodate its new partners, even though it was almost twice the size of the new partner.

A good capital allocator also needs to be able to make bold moves in times of uncertainty. When the deal with Unibanco closed, the world was in the midst of the biggest global crisis since the great depression of 1929. In the turbulent period of the late 1990s and early 2000s, the bank made major acquisitions.

A recent and important acquisition was a stake in XP. In 2017, while seeking to open its capital on the stock exchange, the investment platform ended up accepting an offer from Itaú to buy 49.9% of its capital¹¹ for R\$6.3 billion and postpone its IPO. The original plan was to take control of XP and make it its investment platform, however BCB (Central Bank of Brazil) vetoed the transaction, creating the strange position of largest investor, non-controller and competitor. Although its plans were frustrated, when considering the return on initial investment only from the perspective of Itaú's investor, through the sale of 5% of its position in the follow-on in December 2020, until the division of the stake with distribution to its shareholders, the bank multiplied by 9x its capital in just over four years¹².

¹⁰ Between the 1997 and 2000 Itaú bought Banerj, Bemge, Banestado and BEG.

¹¹ The original plan was to acquire control of XP, but the BCB (Central Bank of Brazil) restricted this part of the deal.

¹² In May 2017 Itaú bought 49.9% of XP for R\$6.3 billion, in December 2020 Itaú sold 5% of XP for R\$5.6 billion, and in

October 2021 the bank distributed R\$50 billion in XP shares to its shareholders. In April 2022 the bank again bought 11.3% of the company for R\$7.9 billion, of which it has already sold 1.3% for R\$0.9 billion for complying with Basel regulatory framework. Together with Itaúsa, the group holds almost a quarter of XP's total shares.

In addition, Itaú took advantage of the closeness to XP to reformulate its investment area and seek M&As in the segment, which complement the banks capabilities. In addition to organic investments, Itaú bought large stakes in the brokers Ideal and Avenue. These investments bring technological improvement to the bank's brokerage firm, the ability to offer a white label platform for investment advisors offices, the possibility of offering investments in the US, as well as teams with experience in creating brokers dealers for retail.

Another important aspect of Itaú-Unibanco's capital allocation policy over time was to always pay close attention to shareholders cost of capital. They took this into consideration not only when determining the level of return requirement for organic or inorganic investments, but also to determine what will be the policy of dividend payout or share buyback. We believe it is a good practice, which allows flexibility for growth, as well as fulfilling its role of giving some predictability to the minority shareholders that the company will not accumulate capital inefficiently.

Finally, a final determining factor for Itaú-Unibanco to have remained a good capital allocator over the years is the performance of its controller through Itaúsa, a vehicle of the bank's founding families. Through this holding company, the family diversifies its investments in sectors other than the financial one, thus avoiding a conflict of interest with the bank's minorities by diversifying capital in other sectors.

Looking forward, we do not expect large mergers and acquisitions in relation to the size of the bank, both for regulatory reasons, as for the already advanced

consolidation of the Brazilian market and the international failure in the next few years, but we believe that the new CEO will pursue new acquisitions and associations with companies that could bring technological capabilities to the bank. The market moment seems especially appropriate to buy technology companies at good prices.

We remain at your service.

Vista Capital

Vista FIC FIA Historical Performance

Year	Vista FIA ¹	IBOV	IBX
2015	3.2%	-13.3%	-12.4%
2016	53.7%	38.9%	36.7%
2017	26.7%	26.9%	27.5%
2018	24.5%	15.0%	15.4%
2019	46.2%	31.6%	33.4%
2020	9.9%	2.9%	3.5%
2021	-20.8%	-11.9%	-11.2%
2022	-12.1%	-6.0%	-5.7%
Jan	3.7%	7.0%	6.9%
Feb	-1.0%	0.9%	1.5%
Mar	6.7%	6.1%	6.0%
Apr	-12.9%	-10.1%	-10.1%
May	1.4%	3.2%	3.2%
Jun	-9.2%	-11.5%	-11.6%
Since Inception	179.7%	97.1%	103.8%

Vista Long Biased FIC FIM Historical Performance

Year	Vista LB	CDI
2018	2.9%	1.1%
2019	36.4%	6.0%
2020	21.8%	2.8%
2021	-14.7%	4.4%
2022	-8.3%	5.4%
Jan	6.9%	0.7%
Feb	-1.1%	0.7%
Mar	5.0%	0.9%
Apr	-12.1%	0.8%
May	0.8%	1.0%
Jun	-6.8%	1.0%
Since Inception	33.7%	21.1%

¹The benchmark of the Vista FIC FIA fund was altered from Brazil Index - IBX to Ibovespa - IBOV on 06/11/2021.

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