# Vista Equities

First Quarter of 2023

VISTA CAPITAL

<u>In the first quarter of 2023</u>, Vista FIA Fund return was -12.54% compared to the -7.16% of IBOV in the same period.

The Vista Long Biased Fund return was -9.78% compared to 3.25% of the CDI in the same period.

<u>Since its inception</u> on January 1st, 2015, the Vista FIA Fund return is 152.15%, compared to 103.73% of the IBOV in the same period.

Since October 26th, 2018, the Vista Long Biased Fund return is 23.61% compared to 33.31% of the CDI in the same period.

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Just like in our last letter, we will explore the main contributions to the funds' results in the first three months of 2023.

The first quarter of the year was marked by an escalation of the uncertainty level already high at the end of 2022. The outflows from equities and multimarket funds ate still very high with no signs of easing: this year alone, R$ 27 billion and R$ 45 billion have already been withdrawn from each of these fund types, respectively. After the *Americanas case,* the credit market was also impacted - with 130 bps widening in spreads already excluding outliers.

With real interest rates significantly high in all horizons, and with uncertainties still relevant about the new fiscal regime of the Brazilian economy, the investor's horizon has shortened a great deal, focusing disproportionately on short-term results. The release of fourth quarter sparked such discussions and, in many cases, frustrated expectations resulted in double-digit drops.

The divergence of ex-ante expectations with results caused in-depth discussions in order to reassess, once again, the premises that made us invest years ago. The burden proved to be harder than we expected and led us to adjust the size of some positions. Nevertheless, we remain confident in the market share gains, profitability improvements, and the consequent profit growth of companies in our portfolio.

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Our position in Hapvida was largely responsible for the negative performance in the first quarter. Since completion of the acquisition of NotreDame Intermédica Group, in early 2022, the company's EBITDA margin has hovered around 8%. Until then, the proforma combined company had a reasonably stable margin at a level that was double the current one.

The recovery of the group's margins would come mostly from the price readjustments of the plans. In short, for every 1% increase in revenues per beneficiary in excess of cost growth, there would be a 60 to 70 basis points decompression in the margin. Despite price adjustments over the year, there was a proportional increase in the level of claims – an effect that could be observed industry-wide. The consequence of the disappointment in the margin was the unanchoring of expectations for the results in 2023 and 2024.

Although the company does not present a margin displacement higher than the sectoral average, the leverage resulting from the acquisition of GNDI and an atypical consumption of working capital caused it to burn a relevant amount of cash. The lack of clarity about the inflection point of margins not only caused the share price to fall, but also caused the controlling family to seek ways to capitalize the company. The former GNDI leadership was almost entirely replaced by trusted individuals from Hapvida and market executives in March 2023, and the following chapter is a vote of confidence for the family and their executives.

Our interpretation is that the market reacted disproportionately to the foregoing. Today's price is not in line with the expectation of margin recovery, even if at levels significantly below historical levels. We will remain close to the company and its stakeholders with the purpose of increasing the position when prudent.

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In the case of Alpargatas, the second largest detractor of the quarter's results, there was a disappointment both in revenue and in the company's profitability and cash conversion. All of these are explained by the significant drop in sales volume in Brazil.

Alpargatas conducts 70% of their sales in Brazil by means of intermediaries, distributors, and wholesalers who in turn resell the products to small retailers. Sell-in is the sale by company to their customers, sell-out is the sale to the end consumer.

After a promising first half of the year in the sell-out and customer enthusiasm for the second half, intermediaries came in stocked for the year's end. Starting in September, with weaker sales as a result of the weather, the elections, and the World Cup – and high interest rates as an opportunity cost for stockpiling – there was a reversal of this trend.

The sell-out fell 4% in the fourth quarter of 2022, on an annual basis, in line with our expectations. However, the unexpected change in customer inventory levels caused a double-digit volume drop in sell-in which in turn has adverse effects of operational deleveraging, an increase in company inventory, and a consequent loss in gross margin.

After an increase in cost of more than 40% between the second half of 2021 and 2022, and consequential price transfer, we saw a downward trend in costs already in the second half of 2022. However, there must be inventory turnover for the new costs and prices to emerge in the result, and the drop in volumes delays this recovery.

Large mismatches between sell-in and sell-out are unsustainable, and strong destocking movements like the one in the fourth quarter of 2022 and early 2023 tend to last a maximum of two or three quarters historically. The year 2023 will focus on efficiency and expense and working capital productivity. To execute this task the company has brought in two new executives, André Natal as CFO, and Gabriel Aver as Director of Manufacturing.

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Finally, it is appropriate to issue a comment on BR Properties – the largest position in our equity funds since 2019. In early April, the company was subject to a stock acquisition through a public offer, where GP Investments acquired approximately 90% of the Company's capital. Before the capital closing auction, the company made effective the capital reduction announced in January of this year, distributing a relevant part of its market value in cash and BRPR Corporate Offices REIT shares: of the R$ 242 per share at the time of the bid, R$ 174 (72%) was paid in cash, and the rest in REIT shares.

The transaction reduced our exposure to the company from just under 20% to around 5%. Our current position is held through shares of the real estate fund managed by the same team and holding the same assets as the company in which we invested all this time. Today, this portfolio is concentrated in Passeio Corporate, a triple A corporate building in downtown Rio de Janeiro, almost entirely leased at prices in line with the market average, with long-term contracts, high penalties, and high-end tenants. This asset trades at a real yield[1] of over 13%, with monthly dividend payments starting as of the middle of this year.

We remain at your disposal.

**Vista Capital**

[1] The value of the dividends estimated for the year divided by the market value of the fund's shares, plus the assumption of inflation correction of the property value - as well as of the rents charged.

### Vista FIC FIA Historical Performance

| Year | Vista FIA | IBOV |
|---|---|---|
| 2015 | 3,2% | -13,3% |
| 2016 | 53,7% | 38,9% |
| 2017 | 26,7% | 26,9% |
| 2018 | 24,5% | 15,0% |
| 2019 | 46,2% | 31,6% |
| 2020 | 9,9% | 2,9% |
| 2021 | -20,8% | -11,9% |
| 2022 | -9,5% | 4,7% |
| 2023 | -12,5% | -7,2% |
| Jan | 4,3% | 3,4% |
| Feb | -7,6% | -7,5% |
| Mar | -9,2% | -2,9% |
| Since Inception | **152,1%** | **103,7%** |

### 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 | -6,0% | 12,4% |
| 2023 | -9,8% | 3,3% |
| Jan | 5,5% | 1,1% |
| Feb | -7,5% | 0,9% |
| Mar | -7,5% | 1,2% |
| Since Inception | **23,6%** | **33,3%** |