" A man should look for what is, and not for what he thinks should be."
(Albert Einstein)

Dear Investors,

HIX Capital is an independent asset management firm focused on investing in Brazilian equities. We manage local (BRL) and offshore (USD) funds whose goal is maximizing return on invested capital through a concentrated portfolio of high quality companies. In other words, we look to invest in companies that: (a) have simple business models; (b) are well managed; and (c) offer compelling potential returns. We strive to achieve the deepest possible knowledge about the companies and sectors we invest in.

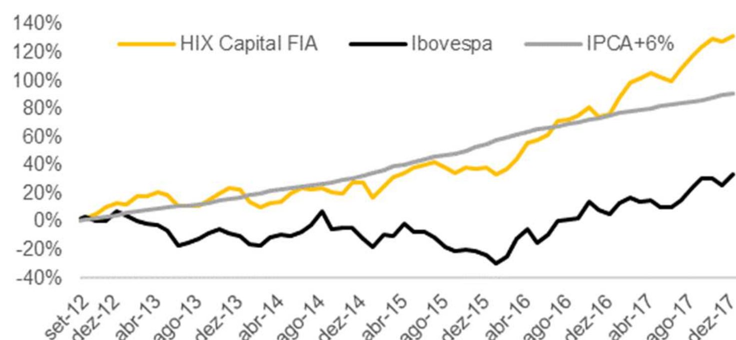
During the second semester of 2017 HIX Equities 1 SP (USD denominated offshore fund) gained 10.8%, whilst the Ibovespa index gained 2.5%. Whilst the offshore fund only completed its first full year of life in September 2017, the local fund of which is a mirror (HIX Capital FIA) has accrued gains of 99.7% compared to a 10.2% rise of the Ibovespa index back to the funds launch in September 2012. Please note that the performance numbers included in this letter from this point on refer to the local fund (in BRL).

Consolidated Results *:

Year	HIX FIA	Ibovespa		HIX EQUITIES 1*	Ibovespa (USD)
2012	13.09%	6.82%			
2013	8.78%	-15.50%			
2014	3.86%	-2.91%			
2015	8.28%	-13.31%			
2016	27.29%	38.94%		-1.53%	5.68%
2017	31.48%	26.86%		30.85%	24.47%
Since Inception	131.54%	33.90%		28.85%	31.54%

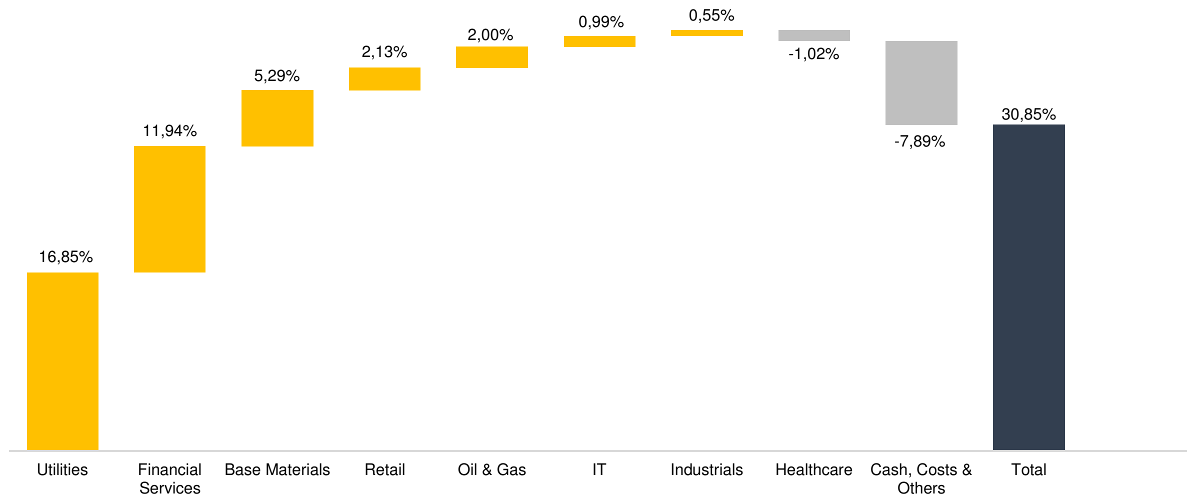
* HIX Equities 1 SP Inception Date: September 15, 2016. Performance Net of Fees in USD

HIX Capital FIA vs. Market Indexes



The main performance contributors towards the funds' performance in 2017 were the investments in Eneva, Jereissati Participações, Energisa and Equatorial, whilst the investments in Alliar and Biotoscana, two new investment positions, were the fund's main detractors. Please find below the fund's performance attribution by sector:

Performance Attribution 2017: HIX Equities 1 SP



Source: HIX Capital

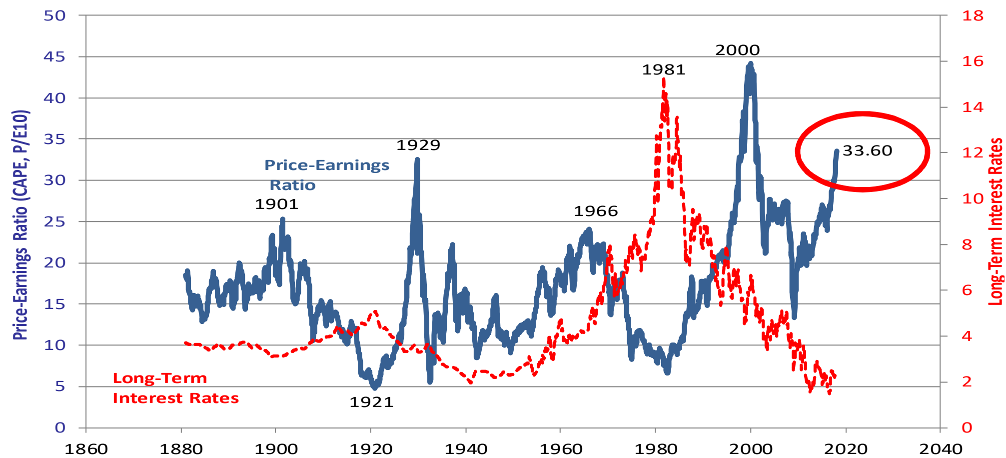
MARKET & PORTFOLIO UPDATE:

The current market scenario is quite interesting from a Brazilian Investor's point of view. On the one hand, developed country stock exchanges (especially the S&P) are consistently testing their historical high's. On the other hand, the Brazilian stock market, despite having undergone significant appreciation in the last two years, seems to still be at the beginning of its recovery process.

The current Shiller PE Ratio multiple[1], adjusted by the cyclicality of the US market, is at a level that, in the opinion of several successful investors, is likely to precede a bursting of the bubble[2]. At the same time, US interest rates remain at record low levels, encouraging investors to continue buying stocks, even at high valuation levels. The chart below depicts a long history of P/E relative to the US interest rate and shows clearly how this ratio is at one of the highest levels ever seen.

[1] Calculated by Novel prize winner Robert Shiller
[2] GMO's Jeremey Grantham recently wrote a letter on this subject (https://www.gmo.com/docs/default-source/research-and-commentary/strategies/asset-allocation/viewpoints---bracing-yourself-for-a-possible-near-term-melt-up.pdf?sfvrsn=4

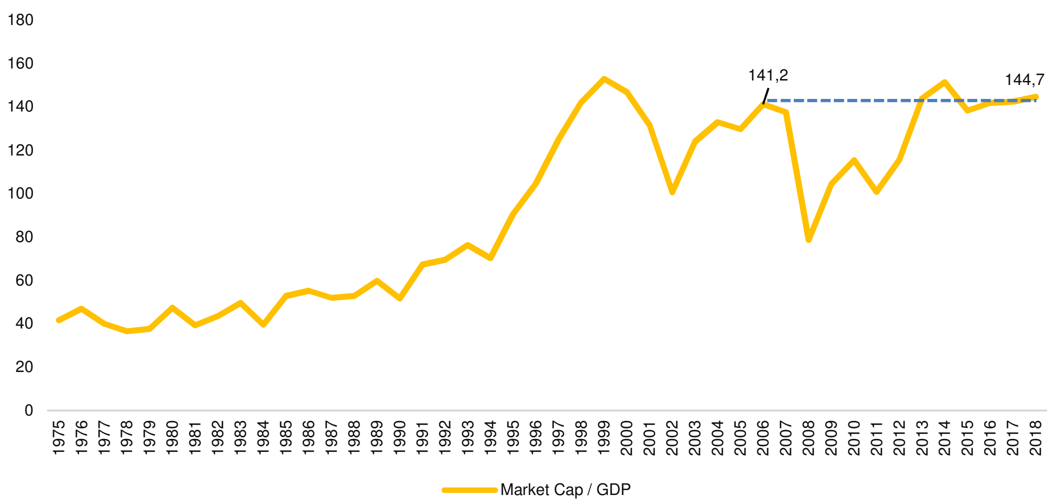
P/E vs. Long Term Interest Rates (USA):



Source: http://www.econ.yale.edu/~shiller/data.htm

Another way to look at valuation levels of the American stock market is by comparing the market value of listed companies against US GDP, and indicator suggested by Warren Buffett as the best thermometer for capital markets. This indicator has already surpassed the level of the subprime bubble and is close to the level reached during the internet bubble, as shown below:

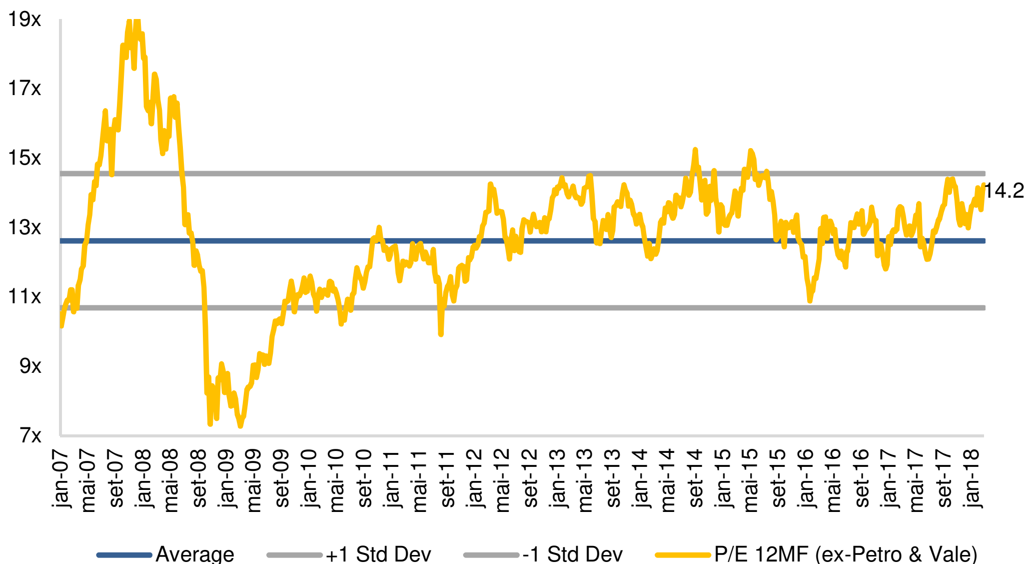
US Market Cap Growth x GDP:



Source: https://www.gurufocus.com/stock-market-valuations.php

Evolution of the Brazilian Stock Exchange's P/E Multiple

In Brazil, the situation is a bit different. Despite the recent rally, the stock exchange still does not appear to be expensive, as rising prices were sustained by the growth of listed companies' profits, which rose by an average of 25% in 2017 (excluding Petro and Vale), in line with the 26.9% appreciation of the Ibovespa in 2017.

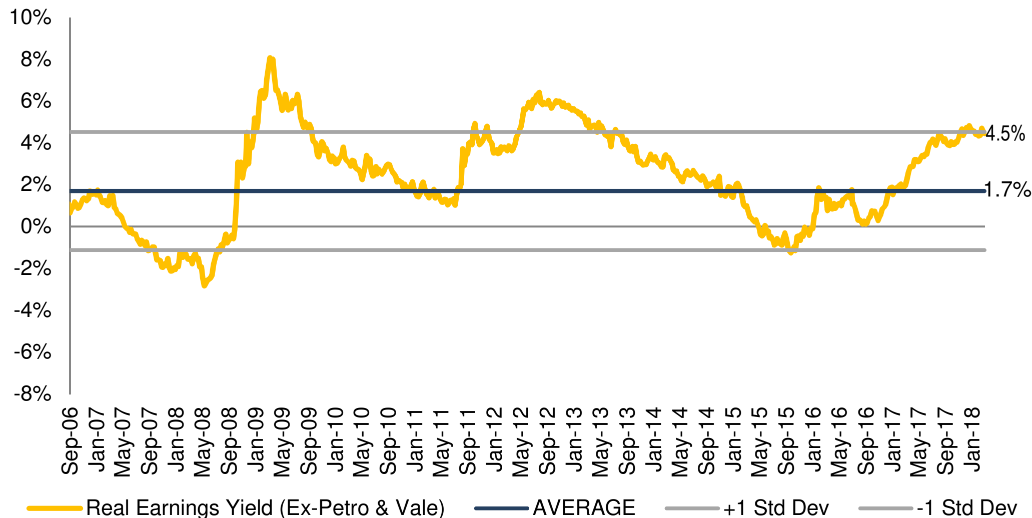


Source: BTG Pactual

In our view, setting aside possible pessimism in relation to the presidential election in Brazil, at this time it would be reasonable for the stock exchange to trade at a P/E above historical averages considering two main factors: (i) high probability of profit growth for the coming years and (ii) the lowest interest rate in the country's economic history.

As multiple levels have not yet risen, the equity risk premium for holding Brazilian stocks is at one if its highest levels in the last 10 years:

Brazilian Equity Risk Premium Evolution



Source: BTG Pactual

From the point of view of recent events, the second semester was very positive for Brazilian risk assets. Despite the present electoral uncertainties and the uncertainty surrounding the widely discussed pension reform bill, the market preferred to focus on positive aspects such as: GDP growth, improvement of corporate results, interest rate drop and controlled inflation, leading the Ibovespa to reach 76 thousand points in December. It should be noted, however, that foreign investors (despite having a relevant role in the recent rally, with a positive flow of R$ 9.7 billion during the second half of the year), Brazilian institutional investors and individuals continue to hold historically low exposure levels to shares of Brazilian companies. A reversal of this scenario could sustain a long period of stock market growth and the emergence of further new IPO's and follow-ons.

For the time being HIX believes that the political environment will dominate market headlines during 2018, significantly increasing volatility. The positive side of this effect is that asset volatility over time is the raw material for stock pickers. During these moments, it is not uncommon for asset prices to disperse from underlying fundamentals, generating investment opportunities. With proper diligence, we believe it is possible to find companies with attractive characteristics that can be excellent investments.

Our portfolios main driver will always be corporate profit growth. We believe that the ongoing economic recovery should go on for some time and allow the profits of listed companies to continue improving. In relation to the weighted result of our overall portfolio (affectionately nicknamed HIX Holding), the expected result growth looks very promising. After good consolidated growth results during 2017, we are confident that 2018 will not be different.

We believe that the weighted average profit of HIX's portfolio companies is expected to grow 41% in 2018. As this number is quite high, we decided to do a thorough analysis on the subject. Revenue is expected to grow 7%, which should allow for relevant operational leverage, and consequently a

2.4 pp improvement in operating margins, with EBIT growing by around 17%. The strong decrease in Selic (Brazilian interest rate) and further evolution of credit markets should generate a significant reduction of approximately 24% in financial expenses, which also contributes to the profit increase, as shown below:

Portfolio Growth (base 100)	2016	2017	2018	2017 x 2018
Revenue	**100**	**109**	**117**	**6.9%**
EBIT	**24**	**28**	**33**	**16.9%**
EBIT Margin	24%	26%	28%	2.4%
Financial Results	**-11**	**-9**	**-7**	**-23.5%**
Cost of Debt (% Net. Op Result)	-11%	-8%	-6%	2.3%
Tax	**-5**	**-5**	**-6**	**23.1%**
Tax Cost (% Net Op. result)	-5%	-5%	-5%	-0.7%
Net Profit	**8**	**14**	**20**	**40.5%**
Net Margin (%)	8%	13%	17%	4.1%

It should be noted that despite a conservative and diversified portfolio profile, the 2018 PE multiple is at one of its lowest levels, with projected result growth at its highest.

Earnings Performance (HIX FIA Holding Simulation)

	2014A	2015A	2016A	2017 E	2018 E
Net Revenue Growth %	17,8%	12,4%	8,9%	9,3%	6,9%
Net Profit Growth %	17,8%	23,7%	25,1%	16,6%	40,5%
P/E Fwd.	**11,7X**	**13,4X**	**13,6X**	**12,8X**	**12,0X**

Source: HIX Capital – Weighted results based on positions, semester-end

The Manager's Dilemma: Romantic or Philosophical Version? The light and heavy side of following or breaking past cycles

In his novel "The Unbearable Lightness of Being", Milan Kundera questions Friedrich Nietzsche's Eternal Return philosophy. Nietzsche proposes that all the universe's events will repeat themselves *ad infinitum*, along the eternity of time and finite life. Kundera, whilst not disagreeing with this concept, rebels against it, taxing it as being too heavy. He argues that it would be better to take life in a lighter way, assuming that what happens in this life will never repeat itself.

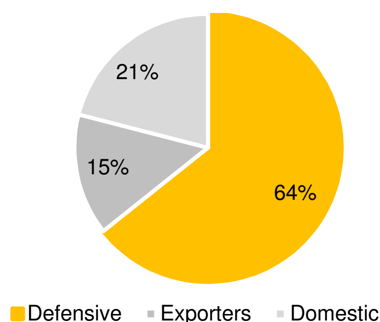
Even though we do not believe strictly in the concept borrowed from Nietzche's philosophy, the necessity of choosing between light and weight is imposed before a fund manager by the synthesis of directional movements for the new and returns to the past, propelling itself cyclically forward. The advances of humanity are undeniable and have been demonstrated by more productivity, culture, technology, medicine, food, etc. Hence, we could sustain that humanity's history is, in a way, light, being more prosperous as time goes by. On the other hand, however our global

economic history is permeated by cycles of euphoria and depression, ups and down, over and under supply, downward interest / upward prices and upward interest / downward prices that recur successively. Do we want to believe in the lighter side, as if what has happened will never take place again (today we live in a different situation, as there are long-term fundamentals for a sustainable jump into prosperity), or in the weightier side, as if everything that happens from hereon will inevitably lead back to the same starting point (even more political incompetence and a new economic crisis)?

The investment analyst is faced daily with choosing between the light and the weight. When a CEO takes on a new company promising the lightness of interrupting a series of bad results, the investor must decide whether to believe he can succeed or if the weight of the industry will shoot down another dreamer with promises he can't deliver. Brazil, at the same time, could also be framed in this dichotomy. Today we are facing a unique opportunity where fundamental issues such as the Pension Reform and the size of the State are being debated by the political class and questioned by society. It will be up to us to decide whether we are ready for the lightness of breaking with past history or where we will succumb to the weight of being the eternally dubbed "Country of the Future".

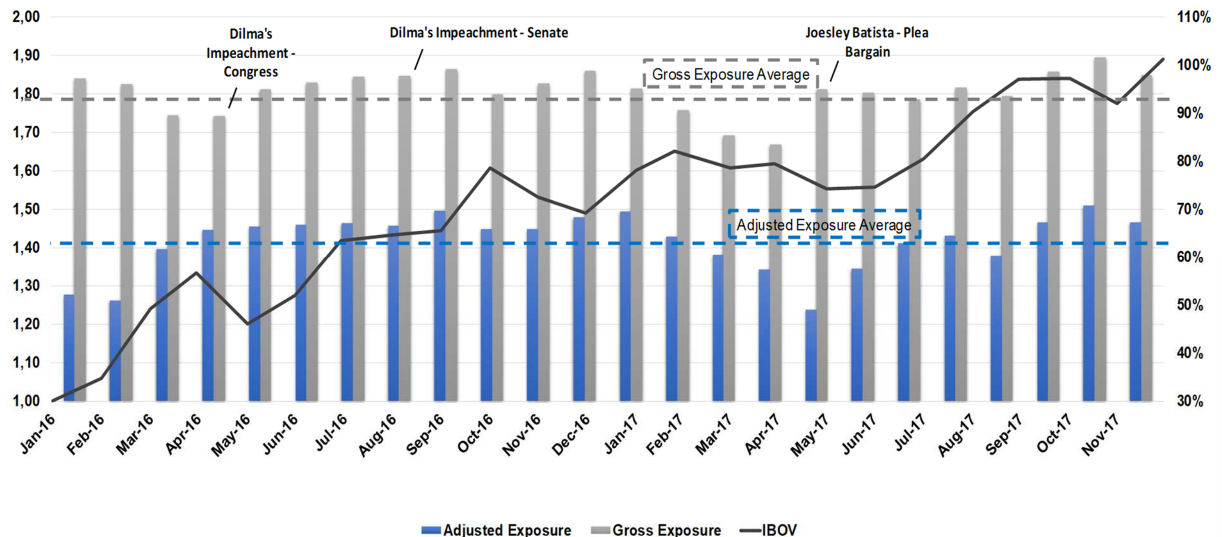
A lesson we learnt from a renowned Brazilian investor is that the role of an asset manager is not knowing what is going to happen, but rather what is reflected on asset prices. Thus, he can position himself cynically, taking advantage of interesting asymmetries. Currently, as we believe that an economic recovery is partially priced, our fund's portfolio is positioned believing in the potential evolution of the country, but prepared to deal with the burden of meeting ghosts of the past.

Currently 64% of our portfolio exposure comes from companies which are in sectors that can be considered defensive. Examples of these are: Utilities, Health, Sanitation and IT. With this, a large portion of the fund has the characteristic of being uncorrelated to annual GDP and therefore will probably navigate well the coming years in any type of scenario. On the other hand, 21% of the portfolio would benefit significantly from strong and sustainable GDP growth. Last but not least, approximately 15% are exporting companies that would experience margin expansion if the dollar gained strength against the Brazilian Real (in scenario where expectations worsen for brazil); in the other hand, in some cases they will also benefit from domestic market growth, bringing better margins, as well as opportunities for relevant internal improvements:



Another interesting way of analyzing the way HIX's portfolio is positioned is looking at the evolution of the absolute and adjusted exposure of our portfolio. To explain these two points, with absolute exposure, all assets excluding cash counts as exposure, whilst in the adjusted exposure calculation, we consider companies that have dollar denominated revenues as hedge, reducing

portfolio exposure. At the same time we adjust each company to its correlation with the evolution of the Brazilian GDP. The graph below shows this evolution:



At this very moment, 98% of the fund is long from an absolute exposure point of view, which can be considered high (as a matter of fact, the highest it's been in the last two years). However, looking at our weighted exposure, we believe HIX is roughly 65% directly correlated to the domestic GDP (also at historical highs, but not so high from an absolute point of view). This means HIX is optimistic about the future (we believe in the lightness story), but we are prepared and positioned for the weight of a more difficult scenario.

INVESTMENT THESIS UPDATE:

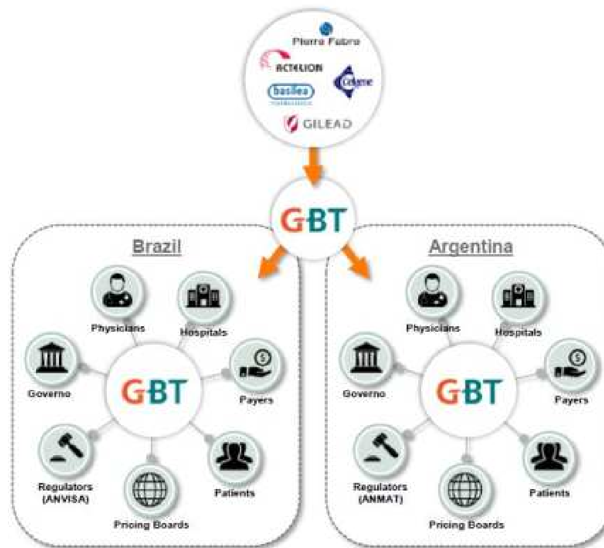
Biotoscana

We began building up our position in Grupo Biotoscana in 2017, a few months after its IPO. Biotoscana is a pharmaceutical company focused on the licensing of rare disease,high complexity medicine. What drew our attention to the company was the fact that: (i) it is inserted in a sector with a secular tendency of strong growth (growth expectations for the pharmaceutical sector in Latin is roughly 7% p.a. in USD between 2017 and 2021) and (ii) historically, large companies in this sector were strong cash generators, with very high margins.

The Group's growth and consolidation project began in 2011, when Advent[3] acquired Biotoscana in Colombia. Subsequently, some more acquisitions were made, of which the more relevant being United Medical in Brazil (2014) and LKM in Argentina (2016). Currently the company has operations in 10 countries in Latin America and its main partners are focused in research and development (R&D) of new drugs such as Gilead, Celgene, Eisai and Basel.

[3] Advent International Private Equity Group

The company's business model involves building licensing partnerships with global R&D companies (biotech's and start-ups) to distribute its products in Latin America. The target segments are specialty drugs, with greater focus on: Oncological, Anti-infectious, Respiratory, Central Nervous System and rare diseases. The company handles the regulatory process for securing new approvals of a given drug, to the importation of the medicine, training and marketing of doctors and hospitals, to the sale and distribution of related drugs. The following chart helps clarify Biotoscana's main activities:

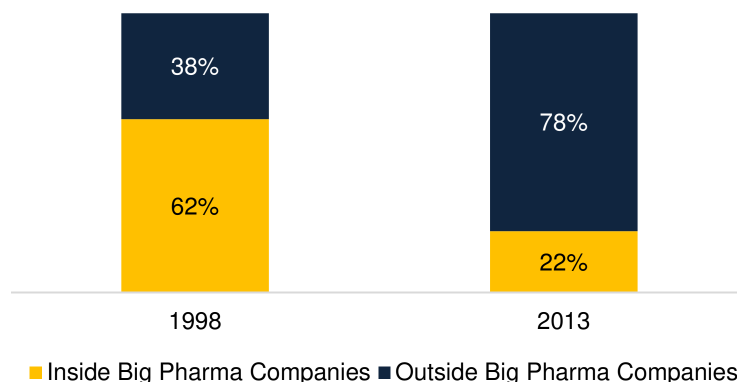


Source: Biotoscana

The opportunity to grow via this licensing model is significant due to some market trends and characteristics:

(i) The R&D market for drugs is increasingly concentrated in the hands of academic and university researchers and / or certain biotech firms and start-ups. In 1998, 62% of the development of new molecules came from large pharmaceutical companies, by 2013, this figure had dropped to 22%:

Developed Molecules



Source: Evaluate Pharma

(ii) Unlike large pharmaceutical companies with global presence and distribution, biotech's operate a business model which is focused on R&D rather than on drug sales and distribution. Even the largest companies, which have a distribution structure, focus their efforts in the US, Europe and Japan (which are the largest global markets). The Latin American market represents only ~7% of the global market for specialty drugs, and this is further divided into more than 10 regional countries. Because of this, the complexity of understanding and managing each market and country with completely different regulatory environments and sales and marketing models makes it difficult for smaller players to act directly, hence preferring the licensing model with a local partner.

(iii) There are few players that act as broadly as Biotoscana in Latin America, with a few competitors acting individually in specific countries. Regional presence is a relevant advantage for biotech's, who prefer to launch their products in Latin America with a single partner, avoiding the risk of managing numerous relationships. An example of this process is the relationship with giants like Gilead and Eisai (which recently decided to hand over a good part of its portfolio to Biotoscana).

To give a sense of the dimension of the potential new drug formula market, it is worth noting that only 50%[4] of drugs sold in the American market are present in Latin America, evidencing the market size and growth opportunity for Biotoscana.

Our investment rationale is based on the following pillars:

1) Growth potential thanks to a pipeline of already contracted molecules: Biotoscana has signed contracts and partnerships for 16 new drugs that will be launched in the near future, which we believe has the potential to double the size of the company in the next 5 years.

2) Preferential platform for Laboratories: The company has a strong competitive advantage and will become the most robust platform for biotech's wanting to sell their products in Latin America due to the following factors:
    a. Strong regional footprint, with strong regulatory, sales and marketing expertise in the region's main countries (especially in Brazil, Argentina, Columbia and growing in Mexico).
    b. Consolidated sales track record, which has allowed Biotoscana to renew partnerships with large companies such as Gilead and Celgene, even in the case of drugs which have already consolidated themselves over the last 10 years.
    c. Strong partner portfolio helps create new partnerships (Basel, Eisai, Pierre Fabre and Dipharma).
    d. Player with strong compliance and pharmacovigilance processes proven by their long-term partnerships (20 years with Gilead).
3) Asset Light business with high ROIC and growth opportunities:
    a. The licensing business is asset light and has great growth potential to be exploited due to new drug molecules arriving in Latin America.
    b. Additionally, the business of similar drugs brings and important complementary factors to the company, adding very interesting defensive positioning to the company's platform value without compromising ROIC and cash generation.
4) Quality management, with extensive experience in the pharmaceutical industry, aligned with the company's long-term strategy and clear growth plans.

We expect a 30% IRR for the next 5 years, with a MOIC of 3x.

[4] IMS Health

VALE

We began analyzing Vale in early 2017, when the its controllers announced a plan to transform the company into a Corporation, and a new CEO took control of the company. At that time, we saw the opportunity for Vale to undergo a relevant transformation in relation to its capital allocation strategy, as well as the quality of execution of projects and operations, and improving operating margins and corporate governance. Potential improvements would come from a significant evolution of EBITDA conversion into shareholder cash flow, coupled with multiple (EV/EBITDA) convergence to levels closer to its Australian peers.

Vale was founded by the Brazilian Government in 1942 to explore iron ore from the Itabira mines. The company's privatization process was initiated in 1997 and in 2002 a follow-on was carried out, where the Federal Government and BNDES (Brazilian Development Bank) sold a part of their stake in Vale.

During the period from 2002 to 2011, Vale took advantage of the so-called commodity "super-cycle" and, consequently, increased its operations, revenues and results. Currently, Vale is the world's largest producer of Iron Ore, Pellets and Nickel. It also produces Manganese Ore, Copper, Ferroalloys, Copper, Thermal and Metallurgical Coal, Cobalt, Platinum Group Metals, Gold and Silver. Vale operates large logistical systems in Brazil and other regions of the world, including railways, maritime terminals and ports, all integrated into its mining operations.

With the end of the "super cycle" in 2011, there was a scenario reversal. During the period of unbridled expansion, Vale had made poor investment decisions, which led to loss-making operations and investments with low (even negative) returns. The ultimate event that led Vale's results into a negative cycle, with a concomitantly complicated financial situation, was the fall in Iron Ore prices in 2014.

Evolution of Vale's Results

	2010	2011	2012	2013	2014	2015	2016	2017E
Net Revenues	45.293	58.990	45.395	48.050	37.539	23.385	29.363	33.625
EBITDA, adjusted	24.955	32.721	18.675	21.844	13.128	9.901	12.174	15.285
EBITDA Margin	55%	55%	41%	45%	35%	42%	41%	45%
Normalized Net Income	17.358	21.886	9.673	7.548	2.057	-6.398	6.654	6.337
Net Debt	15.185	19.548	24.396	31.303	31.311	30.139	31.151	16.137
Net Debt/EBITDA	0,61	0,60	1,31	1,43	2,39	4,84	2,63	1,06

In USD Bn. Source: Vale and HIX Estimates

VALE3 Performance

Source: Bloomberg

Business model and Operations Description

Vale's operations are divided into three main divisions: (i) Ferrous Minerals, (ii) Base Metals and (iii) Coal. The Ferrous Minerals division accounts for 74% of Net Revenues and ~87% of Adjusted EBITDA. Base Metals comprises the production of non-ferrous minerals, which includes nickel, copper and aluminum related investments. This represents 20% of Net revenues and ~12% of Adjusted EBITDA. The Coal division represents 5% of Net Revenues and ~2 of Adjusted EBITDA.

The Ferrous Minerals division, despite suffering from commodity price volatility, has always been a cash-generating operation. It is an efficient and differentiated worldwide operation from both a volume, and quality of Iron Ore produced point of view. This operation is the traditional cash cow.

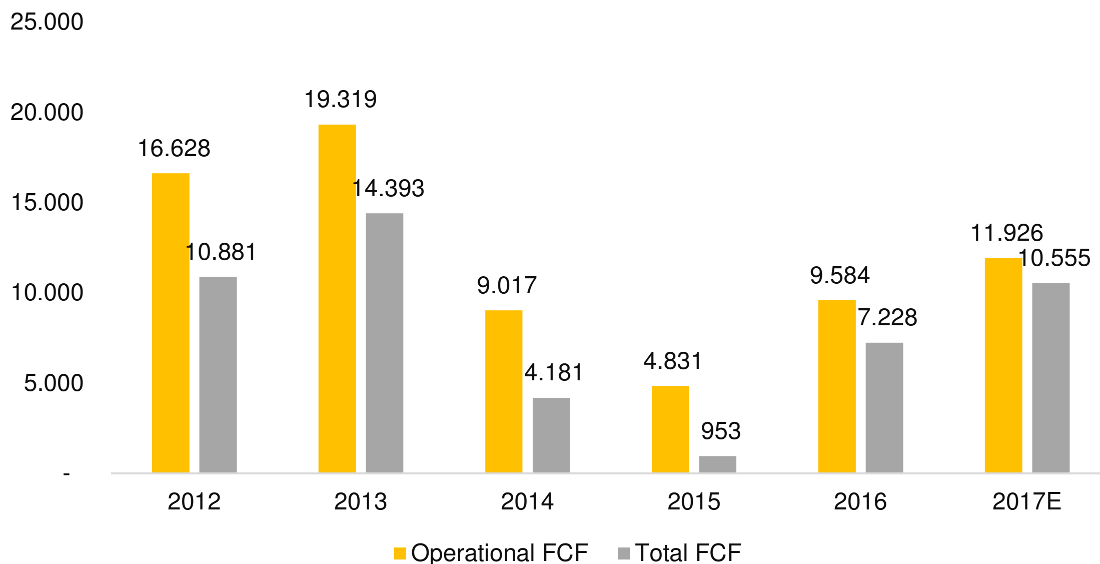
The supply of Iron Ore is dominated by 4 players: Vale, Rio Tinto, BHP and Fortescue, which represent around 76% of the global market, which brings to this market an oligopolistic trait. On the demand side, China represents the main market (70%), being the major driver China's steel production for its' construction industry.

Financial and Operational Indicators – Iron Ore Division

Ferrous Minerals	2012	2013	2014	2015	2016	2017E
Iron Ore - m tonnes	258	265	270	289	293	290
Pellets - m tonnes	45	41	44	46	48	51
Net Revenues	32.270	35.271	26.140	16.562	20.351	24.965
EBITDA, adjusted	19.333	21.543	11.321	5.899	10.476	13.348
EBITDA Margin	60%	61%	43%	36%	51%	53%
Project Investment	5.747	4.926	4.836	3.878	2.356	1.371
Project Maintenance	2.705	2.224	2.304	1.068	892	1.422
Total Investments	8.452	7.150	7.140	4.946	3.248	2.793
Operational FCF	16.628	19.319	9.017	4.831	9.584	11.926
Total FCF	10.881	14.393	4.181	953	7.228	10.555

In USD Bn. Source: Vale and HIX Estimates

Cash Generation – Iron Ore Division



In USD Bn. Source: Vale and HIX Estimates

Vale's main nickel mines and metal processing operations are located in Canada, although the company also operates a relevant mine in New Caledonia. The main use of nickel today is the production of stainless steel, but its importance for batteries has led to the expectation of a large increase in demand given the growing market for electric cars. The nickel segment was responsible for low and unattractive returns in the company's past results. Between the acquisition of Canadian Inco in 2006 and investments in new operations, Vale invested around USD 40 Billion, with a EBITDA of USD 780 million in 2017, which represents huge shareholder value destruction.

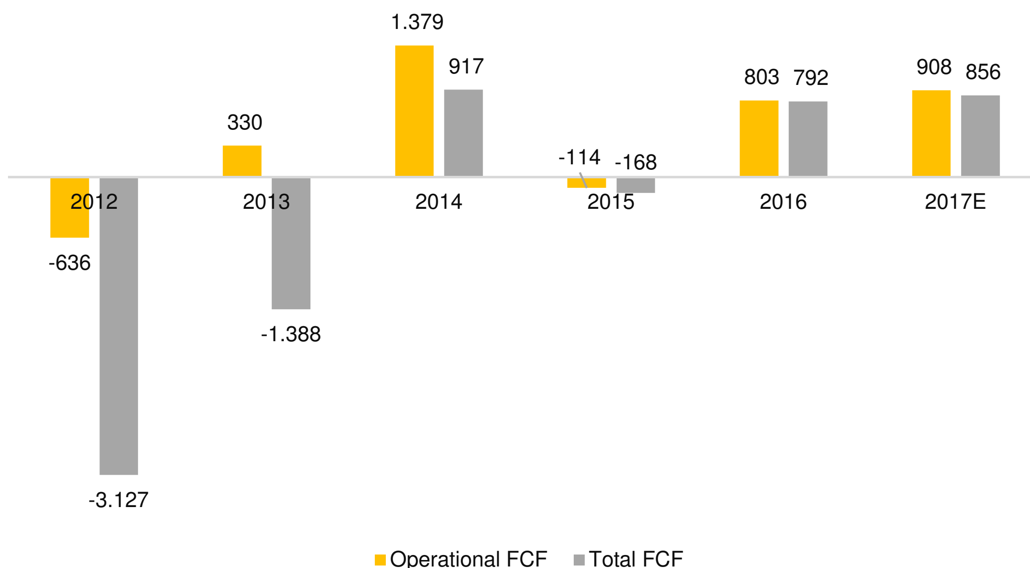
Vale's copper operations are profitable and are located in Brazil, Canada and Zambia. Copper has various uses, being used in the construction, automobile and solar energy industries.

Financial and Operational Indicators – Base Metals Division

Metais Básicos	2012	2013	2014	2015	2016	2017E
Nickel - k tonnes	232	259	272	291	311	294
Copper - k tonnes	282	351	352	397	430	424
Net Revenues	7.133	7.299	7.694	6.163	6.139	6.711
EBITDA, adjusted	1.052	1.639	2.521	1.388	1.848	1.897
EBITDA Margin	15%	22%	33%	23%	30%	28%
Project Investment	2.491	1.718	462	54	11	52
Project Maintenance	1.688	1.309	1.142	1.502	1.045	989
Total Investments	4.179	3.027	1.604	1.556	1.056	1.041
Operational FCF	- 636	330	1.379	- 114	803	908
Total FCF	- 3.127	- 1.388	917	- 168	792	856

In USD Bn. Source: Vale and HIX Estimates

Cash Generation – Base Metals Division



In USD Bn. Source: Vale and HIX Estimates

Vale operates its coal operations mainly in Mozambique. The company is also present in Australia and has a stake in two joint ventures in China.

Investment Thesis

We believe that the changes that are taking place at Vale should generate great value for shareholders and can be summarized by the following pillars:

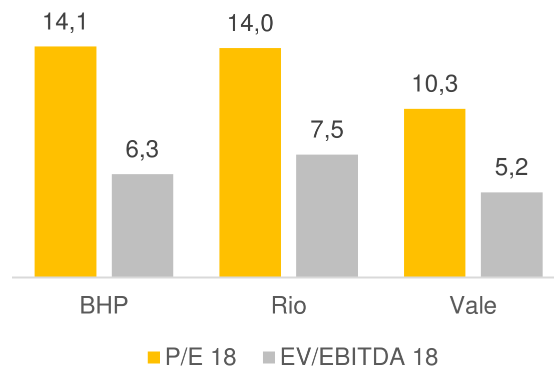
- **Rationalization in Capital Allocation**
  - Historically, large cash generation of the Ferrous Minerals segment financed a rampant expansion of the company's other businesses. This generated a series of

investments with negative returns. The new management team has already indicated that each operation of the company must prove profitable and sustainable by itself. The loss-making operations have to be turned profitable or they will be sold or discontinued (as last resort).
  - New investments will only be made if returns are proven to be attractive under conservative assumptions of future mineral price curves.
  - The company has disclosed investment guidance indicating a significant reduction in investments in capacity expansion. Thus, the new level of Capex should be in the USD 2.5 to 3.5 billion range, compared to a USD 16 billion budget in 2012.

- **Operating Cost Reduction:** Vale is working on several initiatives to reduce operating costs, which should reduce the company's cash cost by USD 3-5 per ton. These initiatives can bring an approximate gain of USD 1 to 2 billion in EBITDA annually. Among the projects are:
  - PIP Innovation / Automation Project – PIP in an international consulting firm with extensive expertise in the mining sector, having helped with improvements and changes in processes, bottlenecks and critical volume, as well as cost drivers for the main companies in the sector.
  - Structured Cost Management with Falconi – Vale hired Falconi Consulting Group with the objective of drawing up a cost reduction plan
  - S11D – Located in Carajás in southeastern region of Pará state, S11D is Vale's largest mining complex with a nominal capacity of 90 million tons per year. The project employs the most modern technology in the industry, which reduces the company's average cost of production (S11D's USD 7.7 / ton vs. USD 13 / ton average), and still has the highest quality ore on the market (65% Fe composition)
  - Integrated Operations Center – Vale has begun operating the Integrated Operations Center (IOC) in order to improve the real time analysis and monitoring of its entire production chain. This operation helps the integration of the operational and sales areas, favoring price and production productivity.

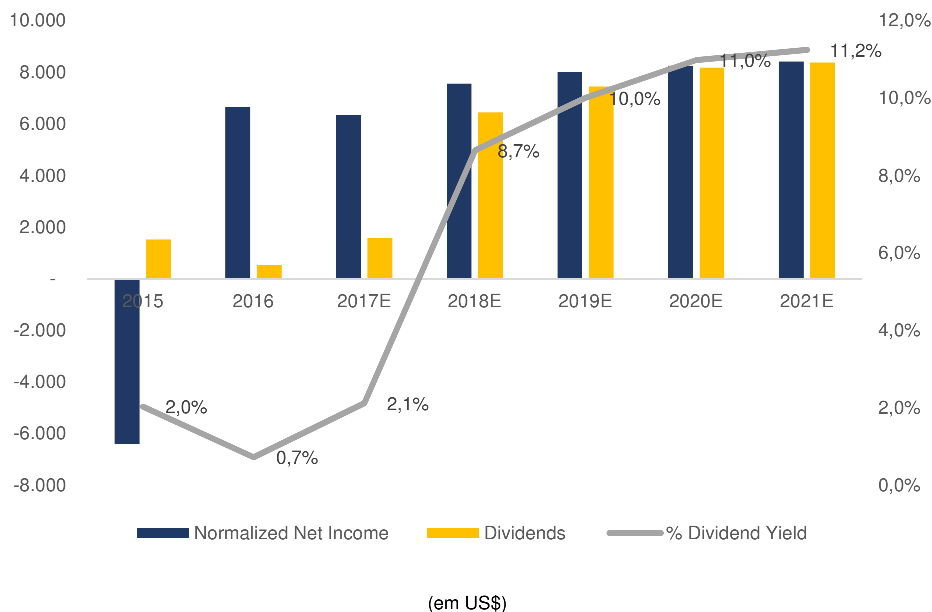
- **Leverage Reduction:** Improvement in cash generation has allowed Vale to reduce its leverage significantly. The board aimed to reach a new debt of less than USD 10 billion by the end of 2018. With this, the company's capital structure will ensure the necessary strength to better surf different economic cycles. We believe that these points alone would be enough to make the company more valuable to its shareholders. However, some other points are important in our investment thesis and deserve to be mentioned:

- **Improvement of Corporate Governance:** In 2017 Vale completed its migration to the "Novo Mercado" segment, Bovespa's highest level of Corporate Governance. Following this process, the company effectively became a Corporation with high governance standards and two independent board members appointed by minority shareholders (Isabella Saboya and Sandra Guerra). We believe that improving governance should help reduce the company's multiple discount against its peers:



Source: HIX Capital

- **Potential Dividend Increase:** Given the new cash generation and deleveraging scenario, Vale has the potential to become a strong dividend payer without affecting its results or debt levels (Considering the IODEX curve at 62% and USD 60 / Ton):

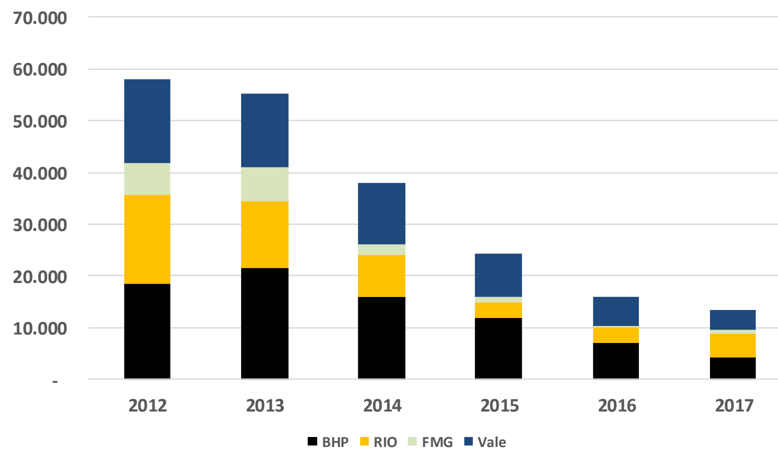


(em US$)

Source: Vale e HIX Estimates

- **Market Rationalization:** The dominant players in Iron Ore supply have become more rational in terms of production expansion investments. The volume of investments of the 4 major producers has dropped significantly in recent years, showing that they currently prefer to guarantee profitability over market share:

Investments – Main Players



Source: Vale, BHP, Rio Tinto e Fortescue

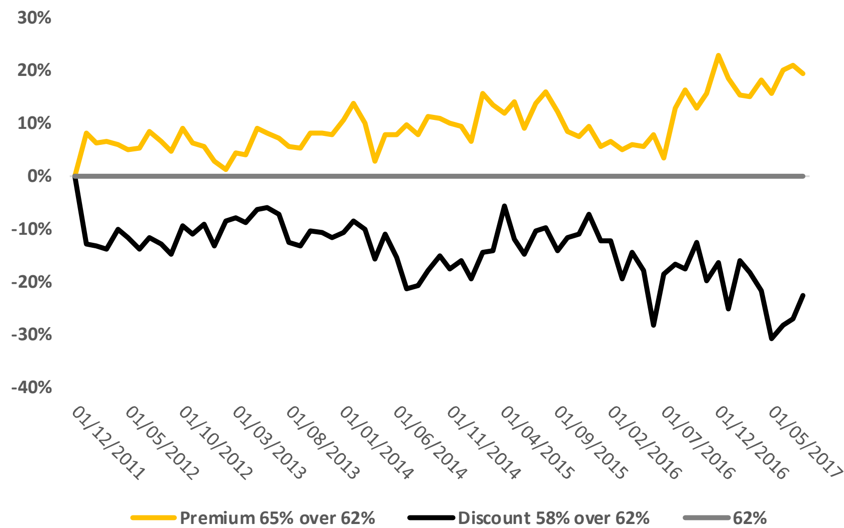
- **Support for Iron Ore prices**[5]

China has been implementing a Carbon Dioxide reduction agenda in recent years. This has led to the closure of over 250 million tons of steel from Chinese producers in the last 5 years. Consequently, the demand for higher quality Ore[6] has increased significantly. This led the premium of 65% Fe content Ore to USD 15.5 per ton, versus historical levels of around USD 7-8 per ton. The opposite occurs with low-grade Iron ore which, because of its high polluting characteristics, currently has lower demand and is thus being traded today at a high discount. Vale, as the company with the world's largest reserve of high quality ore has the opportunity to take advantage of these reserves to maximize its results.

Fortescue, the fourth largest Iron Ore miner, currently produces ~9% of global Ore, being a relevant player in the balance of supply and demand. At the average discount which 58% Fe Content Ore (the main product produced by Fortescue) is being traded at, the company's cash margin would be practically breakeven with IODEX 62[7] at 55 USD / Ton. Therefore, amongst other reasons, we believe that this level should be a type of theoretical minimum where supply and demand would balance even in a remote scenario where we see a 20% drop in China's purchasing volume.

[5] A caveat that any projection or analysis we make in a commodity Market like Iron Ore is probably wrong. Still, we believe that it is Worth noting some trends.
[6] The higher the Fe content in Iron Ore, the lower the coal consumption to produce steel.
[7] Price Index of Iron Ore with 62% Fe content.

Discount and Prize of High and Low Quality Ore on IODEX



Source: Bloomberg

In conclusion, we believe that the changes that are being carried out from the operational and corporate governance point of views will make Vale an interesting investment. Concurrently, although the main investment thesis risk is the price of Ore, we believe that this risk is low due to the market-priced scenario already being conservative – considering part of the efficiency gains and capital allocation – at an Ore price level of 55 USD / Ton.

In a conservative scenario we believe in a IRR of 17.5% in USD.

HIX COMPANY UPDATE:

After spending over 5 years working hard to build HIX into a great asset manager, the results obtained so far lead us to believe that we are on the right track. We started the company with R$ 20 million (USD 10 million) and ended 2017 with around R$ 640 million (USD 192 million) under management, having delivered a net IRR of 16.8% (local vehicle) against 5.5% of the Ibovespa. Without a doubt, when looking back on our trajectory, we feel proud in relation to what has been built so far.

However, we are soon reminded that we are no different today than yesterday, and the reason we have achieved any of the results to date has much to do with our consistent dissatisfaction with the status quo, entrepreneurial drive, pursuit of growth and continuous improvement. Additionally, in our line of business, every January 1st is a new year and everything we did the previous 12 months doesn't matter anymore. A new part of the race begins. The provocation we constantly impose on ourselves is to treat every day as if they were, according to Jeff Bezzos, "Day One". Every day we should rethink processes, incentives, tools, investments and so on. This culture has been disseminated over the last few years at HIX, so that our entire team is increasingly more mature and adherent to our culture, which is based on humility and hard work. With each passing day we grow more excited, because we have the advantage of starting without the effort of breaking the initial inertia of creating everything from scratch, benefitting from lessons (and mistakes) of the past.

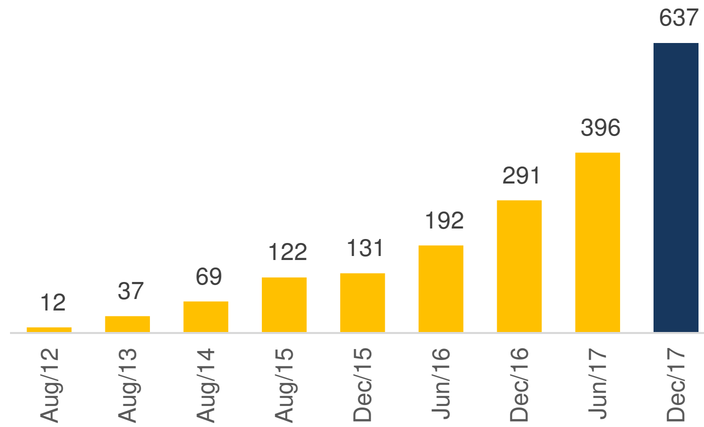
With regards to team and culture, we are pleased to announce that three members of the HIX team were invited to join the HIX partnership program in early 2018. In addition to this, 2017 was a year where we strengthened our team by hiring two more analysts for the investment team, as well as an additional analyst for the back office team. Currently, HIX team comprises of 12 members, 8 of whom are partners and 7 people dedicated exclusively to investment analysis.

Over the past few years, we have improved our investment analysis processes, better organizing our idea generation pipeline, evolved our investment case monitoring process, and made the portfolio adjustment procedure more efficient and dynamic.

In our Operational and Back Office areas, we have made significant improvements due to new systems implementations and continuous process improvement. We have a strong project pipeline to further robust and support the management and risk & compliance teams.

2017 was a successful year in terms of fund raising. Currently 70% of HIX capital's AUM is in our portfolio funds under one strategy: HIX Capital FIA, HIX Institucional FIA and HIX Equities Fund.

HIX Capital: AUM Evolution (R$ million)



We are excited about the growth prospects and challenges for 2018, and are committed to our mission of delivering attractive returns to our investors.

We appreciate your trust,

HIX Capital Team