

IS IT WORTH INVESTING IN IPOs?

February, 2021

Dear investors,

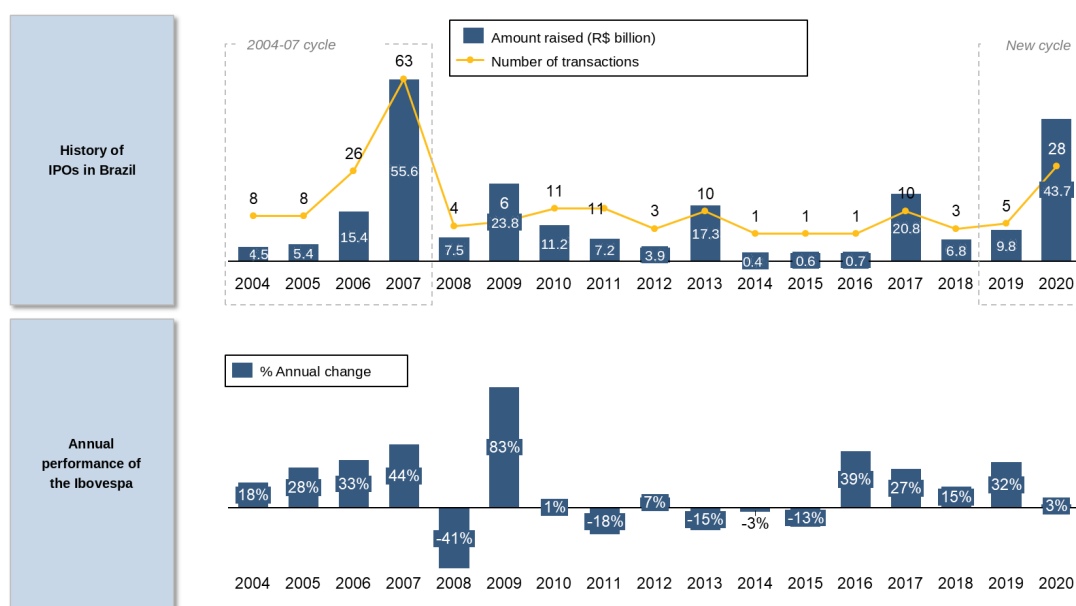
The Brazilian capital market is going through a new cycle of IPOs. Between 2019 and 2020, 33 companies debuted on the stock exchange, raising a total of R\$54 billion. In 2021, there have already been 9 IPOs, and more than 30 offerings are under review by the CVM. To put this in perspective, between 2014 and 2016 there were only 3 IPOs!¹²

This cycle is comparable only to the period from 2004 to 2007, when there were a total of 105 IPOs, raising a total of R\$81 billion.

Given the similarity between the two periods, we have analyzed the historical performance of the IPOs of the 2004-2007 cycle in an attempt to answer the following question: is it worth investing in IPOs?

The chart below shows the history of IPOs in Brazil between 2004 and 2020 and illustrates the figures mentioned in the introduction to this letter.

Chart 1 - History of IPOs in Brazil and annual performance of the Ibovespa



¹ IPO ("initial public offering", or "oferta pública inicial" in Portuguese) represents the first time a company's shares are offered to the market. After the IPO process, it becomes a company whose shares are traded on the stock exchange

² Through Feb/11/2021

The fact that more companies are managing to go public is excellent for the Brazilian capital market, as it means that business owners are able to raise funds to finance expansion plans, which, in turn, create new jobs and benefit the economy.

From our perspective as investors, IPOs broaden the range of investment opportunities. In a country with few listed companies, newcomers to the stock exchange are very welcome.

As we mentioned in our November 2011 letter, Brazil had, up to that point, 316 listed companies, a very low number compared with countries whose economies are of a similar size to ours, such as India, Canada and Australia, with 5,541, 3,948 and 1,967 listed companies, respectively.³

Despite these benefits, investors need to be selective in choosing assets. It is no coincidence that the periods with the highest volume of IPOs are precisely those in which stock markets are rising (see Chart 1 above), as this is when business owners believe they will be able to sell their shares at attractive *valuations*.

This is an important point: if business owners, who know much more about their own company than any investor, believe it is a good time to sell, caution is needed in selecting what may actually be a good investment.

To illustrate this point, we have analyzed the returns of the stock market newcomers of the 2004-2007 cycle. At the time, the situation was very similar to today's: investors competing to take part in IPOs and huge share price gains on debut days.

Almost 15 years after this period, of the total of 105 companies listed, only 65 remain public. Of the 40 that are no longer listed, 22 were acquired or went through an M&A process, 15 went private through a tender offer and 3 went bankrupt.

Of the 65 companies that remain listed, the average performance is not very positive. Only 26 companies outperformed the Ibovespa over the period.

A more alarming figure is that 28 companies (43% of those that remain public) delivered negative returns. These include homebuilders such as PDG, Gafisa, Viver and CR2; banks such as Indusval and Pine; and the mining company MMX (OGX, the best-known company of the X group, went public in 2008). In all of these companies there was a significant loss of capital, in some cases of up to 99%.

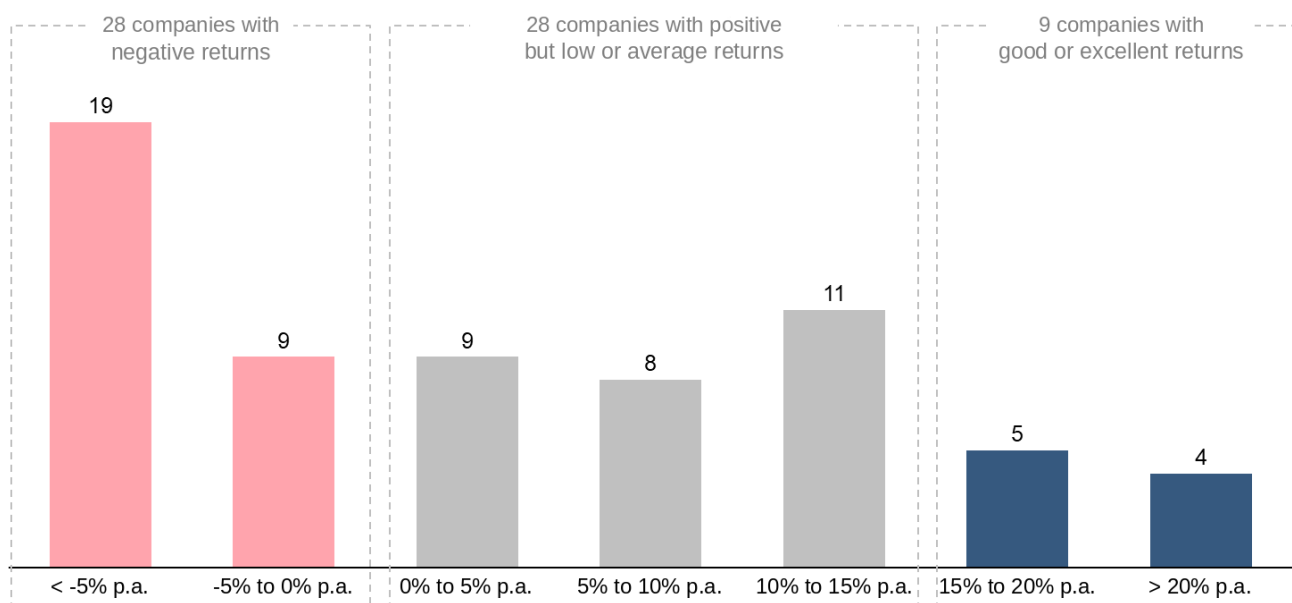
Of the rest, 28 delivered low or average returns (between 0 and 15% per year), and only 9 delivered good or excellent returns (above 15% per year). The chart below illustrates these data:

³ In 2017

Chart 2 – Dispersion of returns of companies listed between 2004 and 2007

Performance of companies listed on B3 in the 2004-07 cycle

Number of companies by annualized return range, returns calculated from IPO through Dec/20



Source: Economática, Ártica analysis

Despite the poor average results, the 2004-2007 window brought excellent companies to the stock exchange, which were able to generate significant value for their shareholders. Highlights among them include Localiza, Natura, Equatorial, Totvs and Porto Seguro, all of which multiplied the capital invested by at least 15x.

Chart 3 – Most successful IPOs of the 2004-07 cycle

Company	Ticker	IPO date	Annual return (through Dec/20)	Capital multiple (through Dec/20)
 Localiza	RENT3	May/05	33%	85x
 natura	NATU3 / NTCO3	Nov/04	21%	23x
 GRUPO equatorial ENERGIA	EQTL3	Apr/06	23%	22x
 TOTVS	TOTS3	Mar/06	21%	17x
 PORTO SEGURO	PSSA3	Nov/04	18%	15x

Source: CapitalIQ, Ártica analysis

If history repeats itself, which seems likely to us, the IPO cycle we are now experiencing should bring companies with an enormous dispersion of performance. Discipline in selecting the best opportunities, investing in good companies trading at fair prices, is what makes the difference in the long run.

Fund characteristics

ARCADIA FUNDO DE INVESTIMENTO DE AÇÕES (the "Fund"), managed by Arcádia Participações e Gestão de Recursos Ltda., is an equity investment fund regulated by CVM Instruction 555/2014.

Target audience

The Fund is intended exclusively for qualified investors (under CVM Instruction 554/2015) seeking long-term-focused returns.

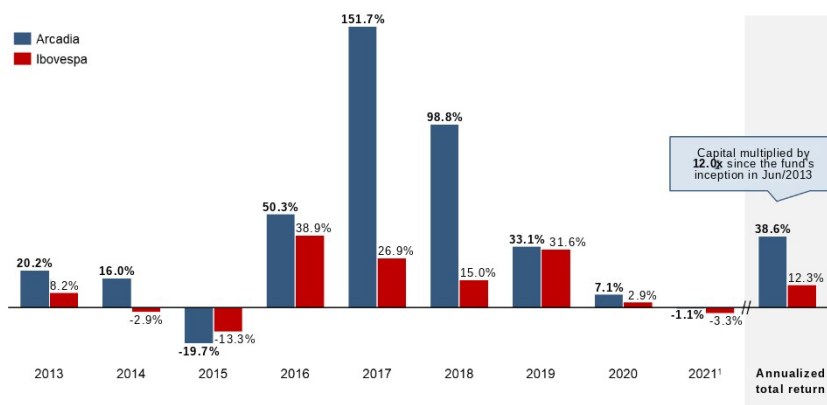
Fund objective

The Fund's objective is to provide its unitholders, over the medium and long term, with capital gains by investing its resources primarily in the stock market, without pursuing a high correlation with any specific equity index available.

Current net assets	R\$105.3 million
12-month average net assets	R\$85.2 million
Cumulative return	1,089.0%
12-month return	3.3%
36-month return	129.8%
Fund assets held by partners	56.4%

ANBIMA classification	Equities (Free)
Manager	Arcádia Participações e Gestão de Recursos Ltda.
Administrator / custodian	BTG Pactual Serviços Financeiros S.A. DTVM
Minimum investment	R\$20.0 thousand
Additional investment	R\$1.0 thousand
Minimum balance	R\$10.0 thousand
Management fee	2% p.a.
Performance fee	20% of excess return over the Ibovespa (high-water mark)
Subscription conversion	D + 1 (business day)
Redemption conversion	D + 89 (calendar days)
Settlement	D + 1 (after conversion)
Taxation (income tax)	15% of gains upon redemption (no come-cotas)

Annual return



Monthly return

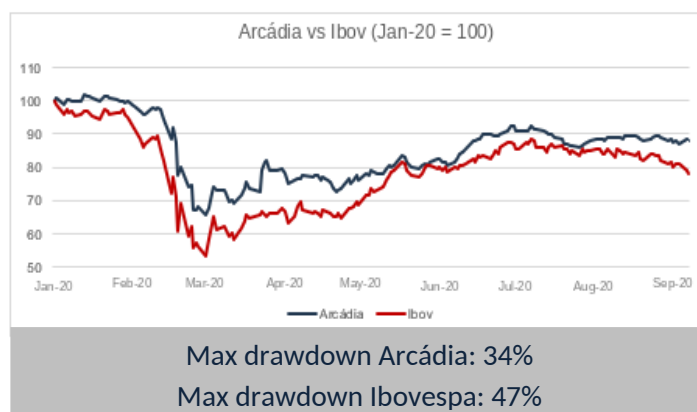
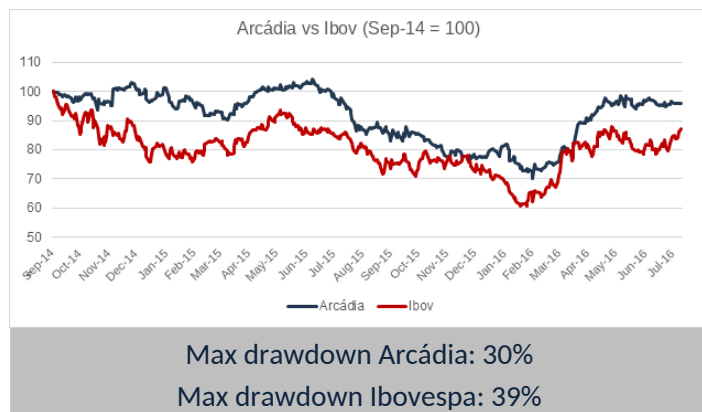
		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year	Cumulative
2013	Arcádia	-	-	-	-	-	2.2%	6.7%	(5.2%)	8.8%	8.3%	(1.0%)	(0.3%)	20.2%	20.2%
	Ibovespa	-	-	-	-	-	(11.3%)	1.6%	3.7%	4.7%	3.7%	(3.3%)	(1.9%)	8.2%	8.2%
2014	Arcádia	(4.5%)	2.9%	2.2%	(0.9%)	4.2%	7.7%	1.2%	0.9%	(1.2%)	(1.2%)	6.2%	(1.7%)	16.0%	39.4%
	Ibovespa	(7.5%)	(1.1%)	7.1%	2.4%	(0.8%)	3.8%	5.0%	9.8%	(11.7%)	1.0%	0.2%	(8.6%)	(2.9%)	5.0%
2015	Arcádia	(4.4%)	(3.6%)	3.4%	5.1%	1.3%	(4.2%)	(10.6%)	(2.9%)	0.2%	(8.7%)	0.5%	3.5%	(19.7%)	12.0%
	Ibovespa	(6.2%)	10.0%	(0.8%)	9.9%	(6.2%)	0.6%	(4.2%)	(8.3%)	(3.4%)	1.8%	(1.6%)	(3.9%)	(13.3%)	(8.9%)
2016	Arcádia	(9.7%)	2.8%	20.9%	4.7%	1.8%	(0.7%)	16.1%	7.8%	(0.3%)	(1.0%)	1.6%	0.6%	50.3%	68.3%
	Ibovespa	(6.8%)	5.9%	17.0%	7.7%	(10.1%)	6.3%	11.2%	1.0%	0.8%	11.2%	(4.7%)	(2.7%)	38.9%	26.5%
2017	Arcádia	2.0%	3.7%	1.4%	2.6%	20.4%	1.7%	27.9%	9.4%	8.7%	8.9%	14.1%	(1.2%)	151.7%	323.7%
	Ibovespa	7.4%	3.1%	(2.5%)	0.7%	(4.1%)	0.3%	4.8%	7.5%	4.9%	0.0%	(3.2%)	6.2%	26.9%	60.5%
2018	Arcádia	22.1%	23.9%	0.8%	2.4%	29.7%	(8.4%)	7.9%	5.1%	(7.8%)	6.5%	(4.7%)	0.9%	98.8%	742.3%
	Ibovespa	11.1%	0.5%	0.0%	0.9%	(10.9%)	(5.2%)	8.9%	(3.2%)	3.5%	10.2%	2.4%	(1.8%)	15.0%	84.6%
2019	Arcádia	10.7%	(1.7%)	(3.4%)	(1.2%)	(5.7%)	(1.5%)	3.6%	1.0%	(7.8%)	14.0%	0.5%	25.0%	33.1%	1021.5%
	Ibovespa	10.8%	(1.9%)	(0.2%)	1.0%	0.7%	4.1%	0.8%	(0.7%)	3.6%	2.4%	1.0%	6.9%	31.6%	142.9%
2020	Arcádia	2.7%	(4.2%)	(24.8%)	8.0%	0.2%	6.7%	9.9%	(2.9%)	(0.2%)	0.1%	12.2%	4.6%	7.1%	1,101.6%
	Ibovespa	(1.6%)	(8.4%)	(29.9%)	10.3%	8.6%	8.8%	8.3%	(3.4%)	(4.8%)	(0.7%)	15.9%	9.3%	2.9%	150.0%
2021	Arcádia	(1.1%)	-	-	-	-	-	-	-	-	-	-	-	-1.1%	1,089.0%
	Ibovespa	(3.3%)	-	-	-	-	-	-	-	-	-	-	-	-3.3%	141.7%

* Arcádia began on June 27, 2013 as an "investment club" and, on September 27, 2019, it was converted into an "equity investment fund." Returns shown from inception on June 27, 2013 through January 31, 2021



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Additional analysis



	Arcádia	Ibovespa
Volatility – since inception	24.5%	26.3%
Sharpe – since inception	1.27	0.26
Correlation (Arcádia vs Ibov) – since inception	0.36	-
Volatility – 12 months	29.1%	44.5%
Sharpe – 12 months	0.18	0.20
Correlation (Arcádia vs Ibov) – since inception	0.78	-

