

BOGARI VALUE

Investor Letter 19, Quarter 3 2011 – Conviction

Bogari Value FIA is an investment vehicle focused on equity investments in Brazilian public companies. The fund's objective is to provide its clients with long-term capital appreciation by investing in companies whose stocks are trading at a substantial discount to intrinsic value.

Our Performance

As of October 2011, Bogari Value's performance was -2.7%, against Ibovespa's -15.8%.

Since inception¹, our total return was +905%, compared to +46% for Ibovespa. During this period, our NAV per share appreciated to BRL 1,005 from BRL 100.

Annual Performance			
Year	Bogari	Ibovespa	Outperformance(%)
2011	-2.7%	-15.8%	+13.1
2010	29.5%	1.0%	+28.5
2009	122.0%	82.7%	+39.3
2008⁽¹⁾	-20.1%	-41.2%	+21.1
2007⁽¹⁾	278.8%	43.7%	+235.2
2006⁽¹⁾	18.7%	11.4%	+7.3

Accumulated Since Inception			
Year	Bogari	Ibovespa	Outperformance(%)
2011	905.0%	46.1%	+858.9
2010	933.3%	73.6%	+859.7
2009	697.8%	71.8%	+626.0
2008⁽¹⁾	259.3%	-6.0%	+265.3
2007⁽¹⁾	349.6%	60.0%	+289.6
2006⁽¹⁾	18.7%	11.4%	+7.3

The markets have continued to be volatile over the recent months, and will probably remain so for some time. Every so often, we continue to acquire some assets with some that are worthwhile.

In general, our investor letters are organized by sections, the first section being dedicated to update our performance, followed by a brief update on the portfolio, and lastly a section dedicated to general topics, related to companies or the general economy, which we believe to be worth sharing with our investors. In this issue, we will discuss "conviction" in the stock markets.

Portfolio Commentary

Our portfolio has been gradually changed throughout the year, but the fund's main positions have not altered in recent months. We seek to take advantage of the market swings to buy assets when there is an exaggerated drop and sell when there is an unjustified discharge.

In the last month, the results of the companies for the third quarter of 2011 were announced. The numbers of our main investments came without great surprises, confirming the trends that we had already mentioned in our last letters.

Itaú presented solid results, without major surprises. Delinquency is at controlled levels and the loan portfolio continues to grow at healthy levels. We expect the expenses to begin to show lower growth, showing next year an improvement in the bank's efficiency, as the company has promised.

Grendene confirmed the slowdown shown in the second quarter of the retail sector and more specifically the footwear sector in which the company operates. Revenue fell due to lower sales volume and lower average prices, pointing to a challenging year-end for the company.

However, the stock continues at an interesting price, pricing a very low growth. In the coming years, the government's measures of salary relief, announced in the Plano Brasil Maior, should generate a benefit of around R \$ 50 million per year for the company. This benefit will expand the generation and distribution to shareholders of your cashier.

Helbor made few launches in the quarter, again due to the difficulty of approvals in the projects, especially in São Paulo. There are a relatively large number of dammed projects that should be launched by the end of the year. The sector's demand has been resilient, supported by the high level of employment in the economy, so this delay does not cause great concern.

It is interesting to observe how the real estate development industry has evolved in recent years. Today, most companies have managed to adapt operationally to new levels of sales and launches. However, one of the new bottlenecks in the sector is the approval of projects with municipalities. While the private sector can rapidly grow its structure, so does the public sector. In this way, we believe that since the beginning of 2011 we are living a new phase,

¹ The vehicle was founded on 1 Nov 2006 as a private investment vehicle. On July 8, 2008 it was transformed into Bogari Value FIA.

the share of approvals. Whoever approves more launches and sells more. The logic, therefore, is to have more land in the land bank, more projects being developed and in the approval phase, to enable more sales in the future. Alternatively, one can go to cities where the volume of launches has been more modest in recent years.

We rest assured knowing the discipline of the company, which has the history of only launching projects that have real market demand. We are already in a phase of the industry cycle where demand may stagnate, so launching a project just to meet targets can be quite risky.

Tempo again showed weak results in the third quarter, confirming that the year 2011 has been quite difficult for the company. However, the prospects for 2012 appear to be different. With the hiring of experienced market people, including the new CEO, the various segments have moved from the internal adjustment phase to the growth focus phase. The CEF contract is expected to start operations in the agencies more effectively and new contracts have been closed with other companies, projecting a relevant growth for the time in the next year.

Redecard showed a small decrease in the margins charged in credit and debit (MDR) operations, corroborating our thesis of a softer competitive environment. This was the first quarter after "opening" of the market in which there was growth of the company's profit (in the annual comparison). The volume growth was very significant, of the order of 29%, compensating for the decrease of margins occurred in the last quarters.

With this, we believe that we are passing through an inflection point, where we must return to see sustainable growth of profit after a phase of adjustments due to the "opening" of the market. New entrants, especially Getnet, should start to make themselves more present in the market, but we believe it is difficult to reach relevant volumes in the short and medium term.

As we like to emphasize in our letters, we like to keep our portfolio adequately diversified. Our largest position is currently 10% of AUM and top 5 combined are around 35% of AUM. Our liquidity level is relatively high, holding a 19% cash-position and being able to sell 90%+ of our holdings in 10 days.

We continue to hold good assets in our portfolio, at compelling valuations and interesting perspectives for the next few years. Additionally, we are positioned to take advantage of a potential market devaluation.

On Conviction

Meaning and Semantics

The Oxford dictionary defines conviction as "a firmly held belief or opinion" while the Cambridge dictionary defines it as "a strong belief that is not likely to change, or the strong feeling that your beliefs are right". Meanwhile, the Merriam-Webster has a wider definition for the word: "the act of

convincing a person of error or of compelling the admission of a truth".

Conviction therefore, leads to accepting something to be a certainty. In numerical terms, the usage of the word leads us to an event with 100% chance of occurring.

The appeal of commenting on conviction stems from its usage in the asset management industry. On occasion, it is seen as a justification or defense of an investment case in some company.

The issue for us is that the process of investing in stocks, by definition lacks certainty in its possible outcomes. If it was not that way, it wouldn't be called "variable income" in Portuguese.

The act of investing in a stock, has outcomes that are unknown, but with estimated distributions in probability. Investing in stocks is not a precise science. Usage of the word conviction, strictly speaking, is removed from the basic concept of investing.

As we see it, the usage of the word "conviction" by investors may be split in two different ways. The first occurs when talented investors employ the word in order to emphasize that, according to the best of their knowledge, there is a high probability of success in a certain investment. In our understanding, these investors are aware that the investment can go sour and are not using the word in its strict sense, but rather as a way to emphasize an extensive research process which is reflected in their assurance with the investment.

The second case is when those using the term truly believe in the end result of the investment. They use the word to generate a sense of security which does not really exist when selling their investment case to others. Quite probably, they are projecting their personal hopes on a single outcome. At this stage, the risks increase.

In our case, we do not like to use the word "conviction", as we understand that its strict sense may convey a false sense of security, and therefore we do not condone it.

Conviction in Theory

Regardless of who uses the term, and in what situation, we must be careful with what we really think.

Studies show that, among the many biases in our brain, we tend to increase our sense of security as we become more familiarized with something. However, the rate at which we make correct choices does not increase as we enhance our understanding of a particular subject.

Mauboussin, in his excellent book *More Than You Know*, presents an experiment with punters on horse races. Initially, some information on the horses was given to them, and they were asked to assign the odds of each horse to win. As the quantity of information given to them was gradually increased, it was observed that the degree of confidence in their prognoses increased, while their accuracy did not.

Being more comfortable with a situation does not increase one's chances of success. It is not simply the amount of information that matters, but also how effectively it is processed. Human beings, often involuntarily, look for more information in order to confirm their hypotheses, not to refute them.

Conviction in Practice

Throughout the years, we have had many opportunities to affirm that there is a non-negligible divergence between the reality of a company and how it is interpreted by the markets.

We have stated sometimes that the market's degree of confidence in some aspects of companies' businesses does not reflect what happens day to day. Moreover, we maintain that often the executives or the controlling shareholders themselves do not have a full grasp on what is happening inside their companies – often not by incompetence, but due to the sheer complexity of their businesses. Our past experience in the controlling group of some companies has taught us this reality.

This is one of the reasons why we do not concentrate excessively the holdings in our portfolio. We believe that no matter how well we know a company, something unexpected can always happen. Lest we forget Aracruz or Sadia².

Specifically on banks, we have published in our Letter 13 in Q3 2010 a section titled "On Panamericano and the Act of Faith of Investing in a Bank", just two days after the announcement of the bank being in trouble. In this text, we put it that "Banks, in particular, are institutions of difficult evaluation. Some analysts say that investing in financial institutions is an act of faith, since it must be accepted as a truth that assets exist, are good and the institution is in good financial standing". In addition, "We believe that even controllers in many cases do not know with adequate depth what happens inside companies. This is often because they are too far removed, sometimes because their executives end up limiting and filtering information about certain topics, and sometimes simply because they do not fully understand the intricacies of their own businesses. As unbelievable as this statement may be, it is not too far from reality. Therefore, the only way to avoid excessive risk is to buy simpler businesses, with a good discount over their fair value and to have a good degree of diversification in your investment portfolio".

We were surprised to read an interview in Brazil' financial daily Valor Econômico published on 11/24/2011 with the president of the Credit Guarantee Fund (FGC) [the government fund aimed at guaranteeing deposits in case a financial institution collapses], Antonio Carlos Bueno. He tells what are the dynamics between the FGC's and banks, in normal times and at the time of a bank crisis, and the relationship of the fund with the Central Bank.

The frankness of Bueno allows us to corroborate the limited level of knowledge that many controllers have of their companies, as can be seen in the sections below:

"Valor: Does the FGC enter the bank and do a broader analysis?"

Bueno: Yes, we analyze if, with this kind of recapitalization, the bank can continue its business normally and have results which will allow it to pay us as well. We check if the banker is telling the whole truth. Or even if he knows the whole truth. Sometimes he does not know. (...)

Value: When does the Central Bank activate the FGC and vice versa?"

(...) Sometimes the controller comes here and does not tell that he has a commitment term with the BC. In general, they tell 50% of what they know, and they only know 50% of what is going on. When we close an operation, we hire an experienced audit and then show the result to controller, who is often scared. There are contingencies and tax liabilities that the controller often does not know. "

The surprise of the interview comes precisely from the fact that a person present in the dynamics of everyday life tells the reality behind the scenes.

At the end of the day, we know that the real life of companies is complex, which makes the investment activity not binary, so our position is usually cautious. We know that it is unpleasant for our client to hear this reality, it is always much easier to sell a non-existent certainty. However, we suffer from the problem of being overly frank. What we do is study a lot and closely monitor the companies and with that we expect to have fewer surprises, but we know that they will happen, as they are inevitable. Therefore, we believe that the decision to limit concentration will make a difference in the long run, when we may avoid larger drawdowns.

Thank you for your trust.

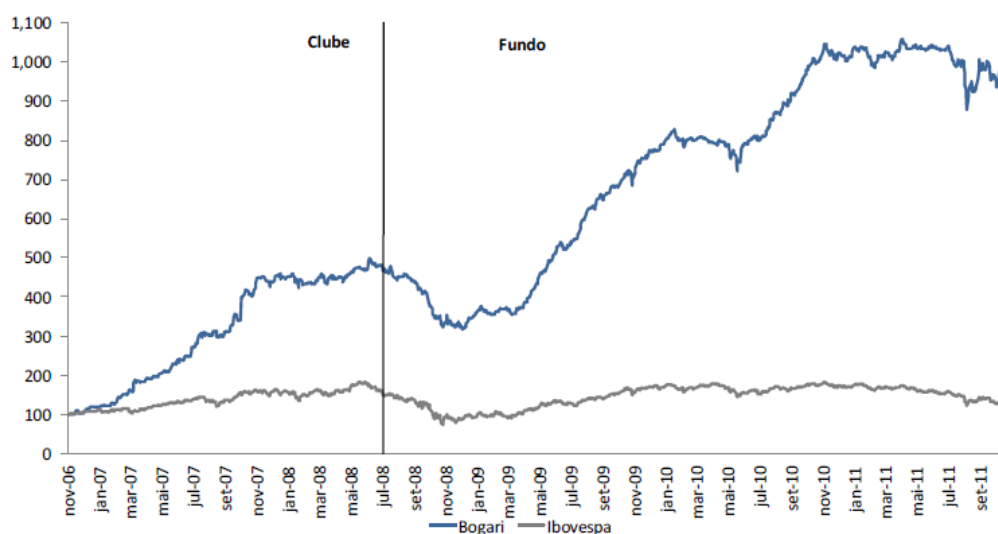
² Those companies' treasury departments were trading increasingly large positions in FX derivatives until a sudden devaluation of the BRL during the financial crisis in 2008

caused massive losses which nearly brought the collapse of those otherwise solid businesses and made them targets for takeovers.

Monthly Returns (BRL – Net of Fees)

		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2011	Bogari	-2.0%	0.7%	2.1%	0.3%	0.0%	-0.9%	-2.9%	-2.1%	-1.9%	4.2%			-2.7%
	Ibov	-3.9%	1.2%	1.8%	-3.6%	-2.3%	-3.4%	-5.7%	-4.0%	-7.4%	11.5%			-15.8%
2010	Bogari	0.0%	0.0%	-0.4%	-0.7%	-0.1%	1.2%	8.7%	4.4%	6.7%	4.8%	0.3%	1.7%	29.5%
	Ibov	-4.6%	1.7%	5.8%	-4.0%	-6.6%	-3.3%	10.8%	-3.5%	6.6%	1.8%	-4.2%	2.4%	1.0%
2009	Bogari	-1.2%	5.5%	-0.9%	21.3%	12.3%	5.1%	15.1%	7.3%	4.0%	3.0%	8.7%	4.2%	122.0%
	Ibov	4.7%	-2.8%	7.2%	15.6%	12.5%	-3.3%	6.4%	3.1%	8.9%	0.0%	8.9%	2.3%	82.7%
2008 ⁽¹⁾	Bogari	-3.6%	3.9%	-1.2%	3.1%	2.5%	2.2%	-7.3%	-0.8%	-12.9%	-13.0%	-0.6%	7.8%	-20.1%
	Ibov	-6.9%	6.7%	-4.0%	11.3%	7.0%	-10.4%	-8.5%	-6.4%	-11.0%	-24.8%	-1.8%	2.6%	-41.2%
2007 ⁽¹⁾	Bogari	9.4%	25.7%	14.4%	9.7%	16.3%	13.9%	11.3%	3.3%	8.8%	28.6%	0.6%	2.4%	278.8%
	Ibov	0.4%	-1.7%	4.4%	6.9%	6.8%	4.1%	-0.4%	0.8%	10.7%	8.0%	-3.5%	1.4%	43.7%
2006 ⁽¹⁾	Bogari											5.1%	12.9%	18.7%
	Ibov											5.0%	6.1%	11.4%

Valor da Cota Bogari⁽¹⁾ x Ibovespa
(Nov/2006 - Out/2011)



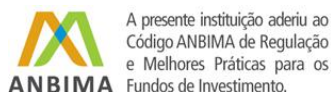
(1) Bogari Value was launched as a regulated private investment vehicle in November 1, 2006. In July 8, 2008, the vehicle was converted into Bogari Value FIA

Main Fund Characteristics (Brazilian Onshore Vehicle)

Administrator	BNY Mellon Serviços Financeiros DTVM S/A	Subscription	T+1
Manager	Bogari Gestão de Investimentos Ltda.	Redemption	T+30
Distributor	BNY Mellon Serviços Financeiros DTVM S/A	Settlement	T+33
Custodian	Banco Bradesco S.A.	Management Fee	2.175%
Auditor	KPMG Auditores Independentes	Performance Fee	20% over Ibovespa (w/ high watermark)
Minimum Investment	R\$ 50,000.00	Anbima Identifier	212962
Minimum Balance	R\$ 50,000.00	Classification	Equities Ibovespa
Minimum Transaction	R\$ 10,000.00	NAV	Close of Business Day

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In order to comply with applicable law, all investors must provide to the administrator copies of their identification documents prior to investing in the fund.



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