(A free translation of the original in Portuguese)

JBI JARDIM BOTÂNICO INVESTIMENTOS

TRIANNUAL LETTER

August 2009

First Letter

INDEX

INTRODUCTION

As mentioned last June, we decided to send a shorter monthly fact sheet, including only data showing the evolution of the Fund's risk/return ratio, as well as a one-page analysis of the portfolio's composition. This decision is based on the fact that the disciplined application of the value-oriented philosophy does not produce significant changes in the portfolio in a short timeframe.

We believe that issuing a more elaborate four-monthly newsletter is a better way to present pertinent information about the thinking of the management team and its investment decision process.

The format of this first four-monthly letter will be maintained in the subsequent issues. The plan is always to have two well defined sections: the first containing a general discussion of themes that interest the team and that we believe to be relevant to our investment decisions, and the second dealing with the evolution of the fund's risk/return ratio based on the analysis of the portfolio.

SECTION I GENERAL DISCUSSIONS

I. JBI'S VALUES

In June of this year, we received important reinforcements to our investment team. With the recent addition of Isabella Saboya and Marcio Brito, we now have a team of six investment professionals with an average of 15 years' experience.

Today, JBI has a characteristic that we consider very advantageous and hard to replicate in the market: partners with a long history of 17 years working together and who, for this very reason, share the same professional objectives that underpin the orientation of the firm's values:

- To fulfill our fiduciary duties as asset managers by seeking high returns in the long term, adjusted to the risk incurred.
- To be recognized as one of the leading exponents of the value investing philosophy in Brazil.
- To become a reference for corporate governance in the Brazilian asset management industry.
- To be fully aligned with our investors through our remuneration structure, which is predominantly based on performance, and through a substantial investment of our partners' own resources in the funds that we manage.

A more critical observer may infer that our objectives seem too heavily weighted on mainly qualitative factors, in an industry that is traditionally known for its focus on quantitative targets and used to judging the quality of managers by their results relative to these goals.

At the risk of losing credibility, we argue that performance is relevant, but it is not everything. It should not even be the basis for selecting managers. We would rank the following criteria as absolutely critical when making our personal investment decisions:

a) To establish clear objectives

As everyone knows, the relationship between risk andreturn is inversely proportional and the maximization of this equation is not easily measurable. If the objective is to obtain the maximum relative return, this can only be achieved with a lower aversion to risk, and vice-versa. We seek a return premium in relation to the opportunity cost that does not represent a much higher risk than that implied in the opportunity cost itself. The key concept here is capital preservation, in other words, to make investments to minimize losses and not necessarily to maximize gains. Experience shows us that the magic of compounding rates causes investments of this type, which are less negatively impacted in crises and only <u>partially</u> accompany the rallies, to produce higher returns than the other available alternatives in the long term,.

We have nothing against decisions which are strictly geared to either maximize returns or minimize risk (note the "either" "or"), but establishing objectives beforehand and communicating them clearly avoids often difficult explanations later.

b) Strict analysis and discipline in applying the chosen investment philosophy

Financial literature is full of examples where incentives that are short-term in nature and/or restricted to quantitative/financial targets have caused strategy changes that resulted in a spiral of unrecoverable losses.

The most successful investors in history are invariably those who never stray from their chosen investment philosophy. They are those who, when questioned about the present or what has changed in their way of investing, are almost boring in their repetitive answers.

Although the discipline that is required to strictly follow an investment philosophy may seem trivial at first, it is incredibly difficult in practice. Peter Lynch used to advise people not to read week-end newspapers or special supplements, because human nature could always lead you to sell GAP shares on Monday because you were unconsciously impacted by an article on global warming and this convinced you that there would be no more youngsters with purchasing power to buy GAP clothes (all right, GAP is a bit antiquated – but replace it with Abercrombie and the rationale is the same).

Still along these lines, back in the nineties when a number of the partners of JBI worked at Banco Icatu, there were two investors headquartered in Australia who called attention by the way they successfully traded in the Brazilian market. It seemed to us that their success relative to other investors was in great part attributable to the fact that they kept away from the hubbub of the market due to the great difference in time zones. They were clearly less influenced by the great quantity of "noise" that is generated daily.

The point is that, in practice, an investment team is exposed every day to strong external influences that can compromise their strict adherence to the investment philosophy if they do not have the required discipline.

At JBI, we believe that an efficient way to maintain discipline is to implement more formal processes for analysis and decision taking. In a recent article in CFA Magazine[1], the author says: "The more one understands and believes in what one is doing at each stage of the decision process, the more one is able to manage the stress – and as one learns to control the stress, the more the decisions regarding one's portfolio will reflect one's strategy and analytical thought, instead of rules of thumb hidden in one's subconscious". This article argues that programming and maintaining processes helps one to make rational decisions and to avoid decisions based on gut feeling.

In short, it does not seem a coincidence to us that successful investors have displayed strict adherence to their chosen investment philosophy, even when it was completely discredited and out of fashion (Warren Buffett during the internet fever at the beginning of the decade – he was even called senile). What is really important is not to change one's strategy in order to,

[1] *Article by Nancy Opiela, page 18 of CFA Magazine, July-August 2009*

for example, come top of the annual performance league tables. For one thing, because the curse of "the first will be the last" is implacable in the financial market.

c) Strict evaluation of the manager`s ethical standards

This item is self-explanatory. It may be difficult to gauge, but as time goes by, the biography of the professional in question speaks for itself.

It is ethics that speaks louder in the numerous uncommon moments in our market. Ethics can prevent the mistakes that produced the great scandals of the corporate and financial world. In the absence of adequate control mechanisms (checks and balances), ethics can safeguard institutions and minimize the occurrence of irreparable situations. And it continues to be essential even in the face of the best control mechanism ever invented. After all, behind such mechanisms there are people and, inevitably, their human nature.

Going back to the issue that our objectives may sound excessively subjective and limited to qualitative factors, we would like to comment on a working paper that greatly called our attention to the theme of establishing objectives. The text reference is HBS 09-083[2].

In this interesting work, the authors call our attention to a series of possible consequences related to the way in which objectives are set. In this respect, they mention studies that show problems when one has multiple objectives, especially mixing those of a quantitative and qualitative nature. In a stock selection exercise, the researchers provided participants with the two types of objectives. The results showed that when both types of objectives were difficult to attain, the participants sacrificed those of a qualitative nature in favor of the quantitative ones – human nature moves towards that which is more easily measured.

Another interesting study showed a direct link between establishing targets and manipulating results. That is, participants are more inclined to fake their level of performance when they have objective and challenging targets than when they do not (of course, faking occurs especially when actual performance falls below the target).

The authors' conclusion is that the use of goals such as that of "managing by objectives", creates a focus on the end in detriment of the means to achieve this end. But it is clear that the authors are not in favor of a laissez-faire world, unorganized, unstructured, without goals. Neither are we. The text calls attention to the care to be taken when establishing objectives. In the authors' words, just as doctors prescribe drugs knowing about their side and adverse effects, managers/administrators should also establish their goals with care. There is even a warning label saying: "Caution! Goals may cause systematic problems in organizations due to narrowed focus, unethical behavior, increased risk taking, reduced cooperation and lower intrinsic motivation. Use care when applying goals in your organization."

In the same section, they recommend that goals be sufficiently broad to include elements that are critical to the firm's success. Once again, they point out the importance of goals that will

[2] *Goals Gone Wild: The Systematic Side Effects of Over-Prescribing Goal Setting, Working Paper 09-083, Harvard Business School, Copyright 2009 by Lisa D. Ordónez, Maurice E. Schweitzer, Adam D. Galinsky and Max H. Bazerman.*

encourage an appropriate level of risk tolerance, and prescribe establishing safeguards to ensure ethical behavior throughout the process of achieving goals (they illustrate it with the ethical behavior of the organization's leaders and methods that make the costs of manipulation greater than the benefits).

We recommend reading this working paper, which only reinforces our decision to establish feasible, prudent goals, and not exclusively quantitative ones, in defining JBI's values.

As many people already know, JBI adopts a value-oriented investment philosophy. We have listed our 10 fundamental principles on two occasions: in our letters of March 2006 and December 2008.

We have also won recognition for our emphasis on corporate governance; and the use of a a governance filter to define our universe of investable companies, continues to differentiate ourselves from other so-called governance investors. We believe that the adoption of adequate corporate governance practices is a tool for value creation in the long term. Our view is that equivalent companies, which have attractive businesses and competent managers, will be differentiated according to the quality and adequacy of their governance practices. It is important to clarify that governance measures, no matter how superior they may be, will not turn a company with weak economic fundamentals into a strong value generator. However, we do believe that between two companies that are equivalent in terms of the nature of their businesses and their management, the one that adopts more adequate governance practices will tend to perform better in the long term and consequently to generate a greater return for its shareholders.

At present, these two themes – value investing and corporate governance – seem to be in fashion and to attract many investors. We see some confusion in the use of these two concepts in the market. In the next letter, we will discuss our investment philosophy in greater detail, addressing the common confusions that we see in the market in relation to these two themes that are central to JBI's investment philosophy.

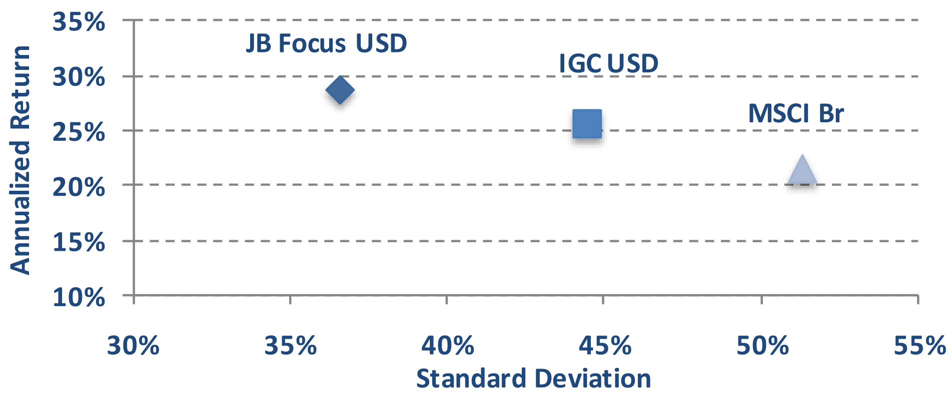
SECTION II THE PORTFOLIO'S RISK/RETURN RATIO

I. FLAGSHIP FUND: JB FOCUS FIA in USD

Since inception on September 16, 2005 the fund has accumulated a net return of 147.65%, or 25.3% p.a. in US$ terms. In our next letter, when we address details of our investment philosophy, we will see that the measurement of risk under the value investment philosophy is very complex. However, we choose the standard deviation merely for purposes of illustration; this does not mean at all that it is our view of a definitive risk parameter.

As we can see below, in this same period, the disciplined application of the chosen investment philosophy has produced a risk/return ratio that is more attractive than the alternatives represented by the market through the indices.

Table 1: Risk/Return



Source: Economática and BNY Mellon Brazil.

However, when forced to make a choice of quantitative parameters to gauge the fulfillment of our mandate, we prefer to analyze the tables 2-5.

The analysis of moving windows (tables 2 and 3) is more faithful to the goal of obtaining good risk/return levels in the course of time. Comparing the results of the 1-year windows with those of the 3-year windows, we see that the fund's risk/return differential improves significantly in the latter.

Also, in table 4, measuring the percentage of windows in which the Fund outperforms the indices that represent the market, we see that the number improves substantially as the period over which the investor remains in the Fund increases.

The table that most calls our attention is the one that translates our interpretation of the capital preservation concept. In table 5, we see that the Fund's "least lucky" investor, who bought at a high NAV and sold without being able to recover his opportunity cost, had a 0.9% loss in nominal US$ terms over a 3-year period. However, if this same investor had bought a market index, he would have lost between 9% and 12%.

Table 2: 1-Year Windows

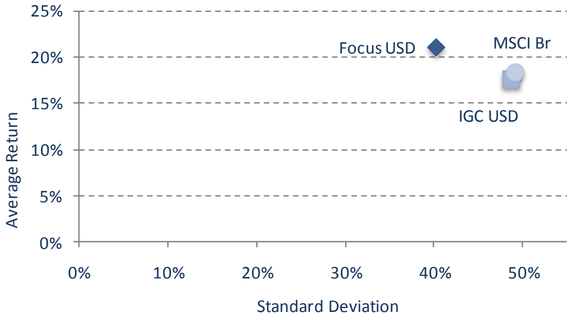


Table 3: 3-Year Windows

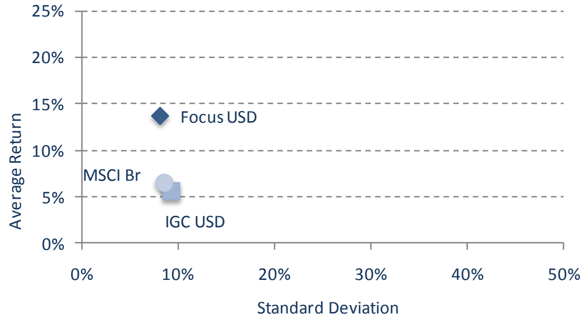
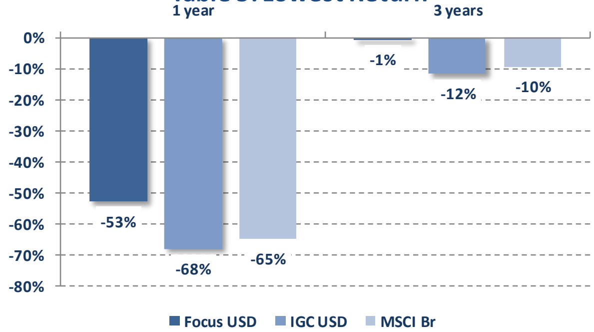


Table 4

Windows	% better than IGC	% better than MSCI Brazil
1 year	59%	66%
3 years	100%	99%

Table 5: Lowest Return



Source: Economática and BTG Pactual DTVM (the statistics were calculated from moving windows samples of the JB Focus FIA in USD. It considers one sample as one three year or 1095 days moving window. Currently, there are a total of 264 three year moving windows. The statistics were generated from annualized returns.)

In the course of almost 4 years of JB Focus FIA's history, the companies that have contributed the most to the results are CVRD (with 18.5%), Itaúsa (18%) and Marcopolo (17.5%). And those that have contributed the least are Login (with - 0.58%), Klabin (-0.58%) and Odontoprev (-0.11%).

Up to August 31, 2009, the Fund has produced a net return of 76.7%, in comparison with the IGC's 85.2%, and 26.3% inflation (IGPM index) plus 6% p.a. The reason why the Fund tends to underperform market indices during periods of sharp recovery will be clearer when we address details of our philosophy in the next letter. For the time being, we would just point out that in our opinion, the result obtained year to date is perfectly in line with the precepts of our mandate, always focusing on the risk/return equation issue, on the emphasis given to capital preservation, and on the value-oriented philosophy, which tends to produce higher results over longer periods than in a period of just one year. We believe that in atypical years with severe crises, such as 2008, our philosophy will tend to produce better relative results. In 2008, the price of JB Focus FIA's shares fell by 42.9%, in comparison with the 55.5% fall suffered by the Ibovespa, and 58.8%, by the IGC.

In the current year, our portfolio's positive highlights are as follows: Rossi Residencial (with an 15.3% contribution to the performance of 76.7%) and Itaúsa (7.7%). We have had no negative contributions so far this year. Among the stocks that contributed the least to the portfolio are Klabin PN (0.29%), Fosfértil PN (0.38%) and Tractebel (1.4%).

II. ROSSI RESIDENCIAL

We began to analyze the real estate sector more closely at the end of the first half of 2008. Although the sector's full potential (repressed demand, credit, etc) was already clear in our long-term view, we had made no investment as yet, because we had found no value to justify a position in our funds. When the crisis started to affect the prices of Brazilian companies, the real estate sector was among the worst hit , and some opportunities began to appear.

At the end of the 1st half of 2008, the scenario of rising inflation and interest rates discouraged investors in relation to the sector. The market anticipated a reduction in available credit, and the companies revised downwards the number of projects to be launched in 2009. Although the stock exchange index closed the semester in positive territory, the shares of the main companies in the sector were already showing negative returns year to date. However, in our view, this situation created a very attractive opportunity for us to start investing in the sector.

Before starting to study Rossi in greater depth, we looked at other, smaller companies in the sector, but decided to concentrate only on the five largest in the industry (CYRE, PDGR, GFSA, MRVE and RSID), not only because they are consolidated names and have more solid financials, but also because, except for MRV, they do not depend on a single market niche.

Once the universe of analysis had been defined, RSID was the one that had suffered the greatest fall in its stock price. However, in this specific case, the problem was not only sectorial, but also related to the company itself. Communication with the market was very muddled, which led a large number of analysts to classify it as a company with low visibility, resulting in a large discount in relation to its peers.

	(%)	**(%)**	**(%)**
	Δ Jun-07 x Jun-08	Δ 1S08	Δ 2S08
Cyrela - CYRE3	*5.20*	*-8.39*	*-58.45*
Gafisa - GFSA3	*-7.85*	*-16.15*	*-62.10*
MRV - MRVE3	*35.73*	*-6.48*	*-72.41*
PDG - PDGR3	*9.58*	*-7.89*	*-50.80*
ROSSI - RSID3	*-40.70*	*-46.69*	*-68.54*
IBOV	*19.53*	*1.77*	*-42.25*

Although the market was questioning the company's financial situation, we intensified our contacts with the company, increasing our knowledge and our confidence that the risk was far below what the market was pricing in. We took the decision to invest in RSID as soon as we started to see a comfortable safety margin, even if it took a long time for the company's stock price to recover. In this specific case, we based ourselves on the calculation of its liquidation value, which gives us a close approximation of the company's floor value, in the event it stopped launching new projects and completed the construction of projects already launched in the next few years, receiving payment for the sale of same, paying its obligations and selling the land in stock at acquisition cost[3]. Its average P/LV (Market Cap./Liquidation Value) was 0.5x over the second semester of 2008.

The main points that led us to choose to invest in Rossi were as follows:

- Consolidated brand and almost 30 years' tradition in the real estate market
- Exposure to all income segments (without being greatly concentrated in any of them)
- Geographical diversification (land bank in 129 towns) through local partnerships, which allows better knowledge of the characteristicsand legislation of each region.
- Confidence that the company's capital structure was sufficiently solid to get through the credit squeeze of the end of 2008 without severe consequences.

In addition to the strong fundamentals mentioned above, the company was starting to show a trend that is particularly important to JBI: a change in its corporate governance. Rossi hired a specialist consulting firm, was considering a change in its independent members of the board, and was making plans to replace some executives, among other initiatives to make the company more professional.

Because we were close to the company, we were able to follow this process closely and to witness a significant improvement in transparency in the course of our investment period.

We started with a small position in RSID3 in August 2008, and increased it as the crisis continued to negatively impact the stock even further and we reinforced our belief in the investment thesis. In November 2008, the company <u>was trading at no more than 30% of its liquidation value</u>. After that, it booked a positive return for two consecutive months; but in February it was penalized again (a 26% fall in R$ terms) due to misunderstood information and lack of clear communication with the market in relation to its results. Only after the announcement of its results for the first quarter of 2009, were we able to see a significant improvement in this aspect.

Good results already started to appear in the 1Q09. Rossi improved the speed of its sales in relation to the 4Q08, diluted expenses, reduced inventory levels, and performed well in the low-income segment, which was responsible for most of the projects launched in the period in question. During the month of April, the stock price shot up from R$4 to R$8 (in comparison with the Ibovespa's 15% rise) in anticipation of the good results that would be announced in mid-May.

In July and August, RSID3 rose further: 50%, as against the Ibovespa's 14% (all in R$ terms). This rise, once again, was probably in anticipation of the 2Q09 results, which were very strong and above market expectations. The main highlights were the good sales speed and dilution of operating expenses, which led to a significant increase in the Ebitda margin.

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[3] *We calculate the liquidation value by adding together the following: receivables from units sold (net of obligations related to such units) + market value of the units in stock (net of costs to be incurred for construction work) + the asset value of the plots of land (net of amounts payable for the plots of land acquired) - net debt - minority participations.*

As a consequence of this extraordinary performance (up almost 260% in R$ terms) in the year, the company very rapidly approached the intrinsic value that we had estimated, and as early as July we started to significantly reduce our position, which is practically zero today. However, considering our investment philosophy, Rossi is an atypical success story for JBI. We do not expect our investment theses to be realized short periods of time of as little as one year. But it is an effect that, without doubt, can happen when investments are made at times of severe crisis, such as that which occurred in the second half of last year.

III. TRACTEBEL

We started our investment in Tractebel in April 2006. The company is the largest private electric power generator in the country. In the electric utility sector, we have a clear preference for the generation segment, because historically this has been less exposed to regulatory risk than the power distribution and transmission companies. In the latter two segments, companies are subject to regular reviews of their tariffs by Aneel (the Brazilian regulatory agency for the electric power sector), and are therefore exposed to the agency's decisions in relation to what their future profitability should be. In the generating segment, however, companies can sell power at auctions, and sign bilateral contracts in the free market or even in the spot market, with minimum regulatory interference and with exposure to the laws of a free and competitive market.

At the center of our investment rationale in relation to Tractebel is the company's attractive dividend payment record. It has paid out practically all its profits in dividends when it does not have to commit part of its cash-flow to investments in new projects.

In view of the company's stable results – owing to the very nature of the electric power sector (in the generation segment) – and to this "dividend play" classification, it is not surprising that the relative performance of Tractebel's stock should be lower than the market in a year like 2009 – one of significant recovery in quotations in general.

However, in addition to the company's tendency to achieve a strong cash-flow and to pay good dividends, we identify in it other attractive characteristics: (i) exposure to future (and potentially higher) energy prices, as it maintains on average about 25% of its power not under contract; (ii) shareholder safety: the company adheres to the highest corporate governance segment (New Market); (iii) attractive upside potential (at least 40%, considering only the present projects and conservative premises for future energy prices) and a projected dividend yield of 11% after 2010, when investments fall again and the company's net cash-flow increases.

The investment in Tractebel fits nicely into the strong capital preservation feature of JB Focus FIA's investment philosophy. However, we do pay attention to the company's risks, albeit relatively low: (i) the recent announcement that the power belonging to Itaipu's Paraguayan side will be sold in Brazil may reduce the prices for contracts with free clients – this may happen if Itaipu's entry into the market does not take place in a coordinated manner; (ii) the prospects for new hydroelectric power projects (not yet announced, or even planned) may always temporarily impact the attractive dividend distribution. But if that occurs, we are confident that, considering the company's value creation record, these new projects will increase our value perception for Tractebel and the return will come through capital gains; (iii) the contract with GDF Suez (controlling shareholder) for the development and transfer of new projects is a focus of extra attention here at JBI. Our governance bias always leads us to reject justifications for contracts with related parties. In the case of Tractebel, what mitigates this fact is that our monitoring of the record relating to that contract shows us that, up to now, there has been no harm of any kind to Tractebel. Obviously, our intention is to continue closely monitoring this contract and its possible future developments.

In respect of the risk/return equation, we remain very confident in this investment in Tractebel and maintain that its characteristics – stability, cash-flow generation and dividend payments – make it a suitable component of JB Focus FIA's portfolio.

DISCLAMER

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