Rio de Janeiro, July 25th, 2017

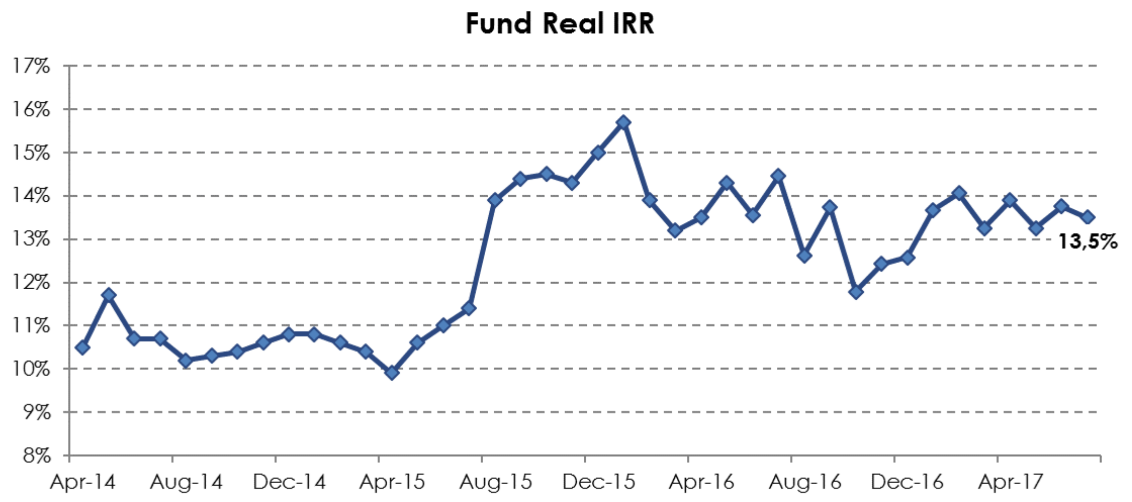
A lot has happened in Brazil (and the world) since we started 4 years ago. Despite many headwinds and high volatility we are proud of the team's discipline and the evolution of our investment process. By focusing on long-term fundamentals we have been able to look beyond short-term factors and keep the Fund fully invested in a concentrated portfolio of 5-10 companies.

Over 90% of the portfolio is invested in these 5 companies:

WSON33 (Logistics) and **TRPL4** (Transmission) since launch
ELET6 and **ENBR3** (Utilities) since 2013
PCAR4 (Food Retail) since 2015

Although 4 years is still a short period to analyze performance, we are pleased to share that since inception[1] our Fund is up 135% in BRL (103% net of fees) and 64% in USD (42% net of fees)[2], while the Ibovespa[3] is up 28% in BRL and -11% in USD during the same period. Unfortunately, we cannot say the same about our investment universe, which has been shrinking since 2013. This limits our capacity as we want to continue managing a concentrated fund and still be able to own mid and small caps. This led us to close for new investments in early-2016 and return 20% of capital to our investors in late-2016. Again, it was not because we couldn't find compelling investment opportunities, but because we were becoming too big for some of them which could start to negatively impact our expected returns.

Evolution of Expected IRR in real terms (in BRL)



[1] Since inception: From August 1st, 2013 until June 30th, 2017
[2] Please refer to the Notice at the end of this letter for additional detail regarding performance calculations
[3] Please refer to the Notice at the end of this letter for additional detail regarding comparisons to index performance.

As shown above[4] we expect an IRR of 13.5%[5] in real terms for the Fund, with the aggregate portfolio at 10.2x P/E 2018 with 9% FCF Yield and 7% Dividend Yield. Despite the macro improvement and sharp decline in local interest rates we continue to avoid leveraged balance sheets. Our invested companies have what we view to be clear moats, sound capital structures and predictable cash flows.

The most complex case is Eletrobras (ELET6 BZ), which we believe to be misunderstood by the investment community and even under-appreciated by its controlling shareholder, the Government. This is why we decided to continue the discussion we started in our previous letter and dedicate this letter to explain some issues that have severely hurt the company and what is being done to turn it around.

A Brief History of Value Destruction

In our last letter we talked about the Brazilian infrastructure sector and the opportunities arising due to the lack of investments caused by the innumerous government mistakes made through 2015.

In addition, we have argued that the absence of corporate governance and mismanagement of state-owned companies also played an important role in keeping away sustainable private investments in the sector. In this letter, we have decided to shed some light on the huge impacts of such inefficiencies, not only for the companies' direct shareholders, but also for most of its stakeholders, especially electricity consumers and taxpayers.

Discussing such impacts is far from simple – it requires a long-term approach as well as a complete understanding of its side effects in other segments and public accounts.

In developing countries with very high cost of capital like Brazil, inefficient allocation in capital intensive sectors can have a significant long-term impact for the country and for private players in the sector. Sometimes, capital allocation mistakes take time to be perceived, and their short-term effects can pass unseen. Over the long-term though, these negative consequences compound and can be easily analyzed and measured.

In state-owned companies, this long-term aspect makes accountability difficult as company management mandates are short-lived. Given political ties, many decisions are driven by populist arguments such as "lower future tariffs" and "capex impact in the economy" in favor of inefficient investments – questionable short-term "benefits" at an expensive long-term cost.

On top of the regulatory complexities, confusing accounting procedures also make the analysis challenging, but we believe that if we take a long-term approach, conclusions can be very clear. We discuss many of them in this letter.

We have held a significant position in the Brazilian electricity sector since the fund launch, through four different holdings, one of them being Eletrobras.

[4] Weighted average return of the expected implied real return of each portfolio holdings. The expected implied real return of each holding is calculated based on 3G Radar's estimates of the future free cash flow of the company in real terms and its current market price. This graphic illustrates a hypothetical long-term return profile for illustrative purposes only and relates to only a portion of the Fund's investment history. Actual returns on the Fund's investment strategy over the life of the Fund may differ materially from the returns shown.

[5] Please refer to the Notice at the end of this letter for additional detail regarding limitations associated with expected returns.

Eletrobras is a public company controlled by the Brazilian government operating in the areas of generation, transmission, and distribution of electricity. The company has a large asset base within a complex corporate structure (17 subsidiaries, 178 SPCs and minority stakes in 25 companies) and more than 23,000 employees. Total Federal Government direct economic stake in the company amounts to approximately 63%. If we add tax revenues, such economic stake would be close to **75%.**

The generation capacity of Eletrobras, including half the power of Itaipu, reaches 47 GW, which corresponds to **32% of the total Brazilian capacity**. This energy is produced by 29 hydroelectric plants, 20 thermoelectric plants, 6 wind plants, 2 thermonuclear plants and 1 solar plant. In terms of transmission assets, Eletrobras has 70,201 kilometers of lines, accounting for **47% of total lines above 230 kV in Brazil**. Eletrobras also operates six distribution companies in the North and Northeast of Brazil.

According to our estimates, as we show in this letter, the carrying cost of Eletrobras for the Federal Government amounted to approximately **R$ 228 billion** in the last 15 years. At first sight, this figure seems too high, but it is not difficult to calculate. Unfortunately, this cost was not associated with efficient capex and services quality, but rather with capex delays and poor-quality indicators in all segments, especially on the distribution side.

Eletrobras' current market cap is only **R$ 20 billion**, a very low value considering all the company assets, and is a clear indication of the mismanagement and problems it has been facing. However, with the right efficiency measures plus improved governance and regulation, this company could be worth multiple times the current market cap – which could be monetized through dividends, asset sales, income tax revenues, investment capacity or privatization.

Under the leadership of the new Minister of Mines and Energy (MME) Fernando Coelho, the government has appointed Wilson Ferreira as CEO – former CPFL CEO and one of the most respected electricity sector managers – and has appointed we believe to be a highly qualified and technical board of directors for the company.

As shareholders, we were proud to have supported the appointment and election of names like Vicente Falconi, Elena Landau, Jose Monforte and Wilson Ferreira to the current board and of Mozart Siqueira and Jose Alqueres to the previous board composition.

This team has been conducting a deep turnaround process in the company which consists of (i) cost cutting, (ii) asset sales, (iii) financial deleveraging, (iv) new governance standards, and (v) leaner administrative structure. It is worth mentioning that they are doing this heavy lifting as patriots – The compensation system will need to change if the Government wants to keep or attract such a high-quality team.

In addition, Minister Coelho has also appointed a very technical and competent executive team, in our view. Highlights are the executive secretary Paulo Pedrosa and the president of EPE (Energetic Research Company) Luiz Barroso, who have been supporting many positive regulatory changes presented by MME.

We believe these changes are steering the sector in the right direction, towards attracting private investments in a sustainable and healthy way, and are very powerful value creation drivers for the sector. Good examples are the changes in the transmission lines auction terms, the cancelling of new reserve energy auctions given current surplus, the recently proposed changes in sector rules and the discussions for improvements in the natural gas market.

As minority shareholders of Eletrobras we could write a letter focused on the quality of the company's assets, but we chose instead to go through some of the impacts that the mismanagement of the past 15 years has caused to the company (and country).

We also lay down arguments that justify our belief in why the next 15 years should be very different, and why this tarnished reputation should be reverted, as the company continues with its current turnaround initiatives and the sector's regulation continues to evolve in the right direction.

In our view, the following factors explain the prejudice that investors have with Eletrobras

1) The so-called "Structural Projects" – A R$ 20 billion loss

One of the key aspects of the model implemented in the sector in 2004 was the inclusion of the so-called "structural projects" as pillars of the sector capacity expansion planning. These were defined as projects with large energy generation capacity, which would theoretically bring more supply reliability at lower costs given: scale gains, the low hydro marginal costs (with Amazon´s large hydro potential), and Brazilian "engineering expertise". The capacity of these projects – Santo Antonio, Jirau, and Belo Monte – correspond to 18.6 GW (13% of Brazilian capacity).

To assure that the projects were implemented, the government created exclusive auctions for them ("market reserve"), given that through real market mechanisms it would not be possible to compete with other projects. These were large projects with high engineering and commercial risks, high transmission costs and, consequently, no financing. In addition, it was also assured that Eletrobras would have a significant minority stake and in two of these three projects, construction companies were the controllers.

In order to justify the creation of a market reserve for these projects, the Federal Government worked to set lower than average cap tariffs for them. The result was a low implied rate of return for the projects – a burden only Eletrobras would have to bear, as construction companies would profit from valuable construction contracts.

The reality proved to be completely different than the one marketed by the Government officials – it was only a matter of time before it became clear that the official assumptions were a piece of "engineering" fiction. As we show in the exhibits below, many factors impacted the theoretical returns:

a) Capex estimates for these projects (especially Santo Antonio and Belo Monte) were increased by 20-25% on average;
b) Hydrological risk;
c) Project delays;
d) Corruption investigations (Car Wash operation).

Exhibit 1: Estimated vs Reality of Belo Monte, Jirau and Santo Antonio projects

	Estimated (A)	Reality (B)	(B) – (A)
Capex	R$ 61 bn	R$ 76 bn	R$ 15bn (+23%)
Implied Real Return	7%/8%	-1%/0%	-8p.p
Delay	0	~14 months	~14 months
Value Destruction	R$ -6 bn	R$ -47 bn	R$ -41 bn
Value Destruction (% Elet)	R$ -3 bn	R$ -20 bn	R$ -17 bn

Source: 3G Radar

The combination of these factors led the expected initial returns of 7%/8% (already very low given the risks involved) to -1%/0%. Yes, **ZERO.** Assuming a cost of capital of 10% in real terms, this would correspond to a R$ 47 billion value destruction (R$ 20 billion value destruction for Eletrobras).

Of the R$47 billion value, R$ 6 billion corresponds to the initial lower tariffs, but we estimate the remaining R$ 41 billion were due to inefficiencies and corruption. Not to mention the fact that these projects prevented other more efficient projects to be developed at lower costs by private players.

The key question on these projects is – did anyone benefit by this colossal value destruction? Yes. Corrupt construction companies, suppliers and politicians. One could argue that electricity consumers benefitted from lower tariffs provided by these projects, but this is not true either:

a) by our estimates the value of such benefit (R$ 6 billion) is lower than the R$ 20 billion loss to Eletrobras and the country (i.e. taxpayers) and;
b) the delays in such projects caused an estimated R$ 15 billion loss to final consumers (variable cost of thermal plants dispatched because of the delays).

These structural projects are a clear evidence of how Eletrobras was assaulted by corruption involving some construction companies, suppliers and politicians. The rest of society, including final consumers, taxpayers and shareholders were the ones to bear all the costs.

The Future – After the unimaginable losses caused by such projects, we believe that the risk of similar gigantic projects, using the same economic model adopted in the past, is minimal for the following reasons:

a) The conflict of interests of having construction companies as both shareholders and suppliers is no longer allowed under Eletrobras policies;
b) The huge consequences and costs of conducting these types of projects are now clear and proved, increasing the scrutiny on future similar projects;
c) Sector expansion being led mostly by renewables ex-hydro and gas fired plants (projects that are appropriate for private players). In the recent published PDE (10-year Sector Expansion Plan), the expansion to be contracted is 85% renewables and only 5% hydro (biggest project with 725 MW capacity);
d) Car wash leniency agreements, which can cause significant losses and legal problems if the same constructions companies are involved again in the illegal practices of the past.

It is worth mentioning that partners in existing projects are looking to sell their stakes and Eletrobras is likely going to tag along.

2) The Nuclear Economic Disaster – A R$ 20 billion loss

In 2011 the Federal Government decided to go on with the Angra III nuclear project, a 1.4 GW plant. Once again, not having market mechanisms to justify such investment, the federal government allocated the energy to be produced by such project as the so-called “reserve energy”. The tariff of the plant was set at R$ 230/MWh (today’s price) that would not justify the economic risks of such a challenging project.

The project, which was initially expected to start generation in 2017, is now halted after a capex of R$ 10 billion and estimates for its completion amount to an additional R$ 16 billion (R$ 26 billion in total). When the construction was approved, the expected capex was R$ 16 billion, hence the total increase corresponds to a whopping 63%.

Exhibit 2: Estimated vs Reality of Angra 3 project

	Estimated (A)	Reality (B)	(B) – (A)
Capex	R$ 16 bn	R$ 26 bn	R$ 10bn (+63%)
Implied Real Return	7.5%	n.m.	n.m.
Start Operation	2017	2024	7 years delay
Value Destruction	R$ -1 bn	R$ -20 bn	R$ -19 bn

Source: 3G Radar estimates based on public company data

Considering the initial capex value, the expected return for the project was 7.5% in real terms. After all the project revisions, the value destroyed equals R$ 20 billion, including the cost of capital. So far, Eletrobras has written off R$ 10 billion of investment in this plant. If project construction is resumed, the return will depend on the new tariff level that is now under discussion in the Government.

Again, the same question can be asked: with such unthinkable value destruction, who has benefited? The answer is the same, corrupt suppliers, construction companies, politicians and executives.

By establishing a lower tariff (given a higher capex budget) for the plant, and accepting a lower return for such plant, we could say that consumers would have enjoyed a R$ 1 billion benefit, but these same consumers, as Brazilians, lost R$ 20 billion through Eletrobras.

The Future - It is not clear yet how the equation on Angra 3 will be solved. In order to complete the plant, an estimated tariff of R$ 360/MWh is required (a 56% increase). After the huge losses booked on Eletrobras' balance sheet and all the corruption impacts that the Car Wash operation had on this project, we expect the decision to be a technical one. Eletrobras management and the Federal Government are working on a model to allow the entrance of private players in the project, with sustainable long-term financing and efficient capex.

A possible solution would be to allow part of Angra 3 tariff to be quoted in USD (use part of Itaipu USD tariff that will end in 2023) and facilitate the entry of international players with minority stakes and access to cheaper funding.

3) The "Out of Control" Distribution – A R$ 41 billion loss

Eletrobras operates six distribution companies in the North and Northeast regions – these are huge loss-making companies. Such losses are a consequence of years of mismanagement. The regions where these companies are located are complex – isolated systems with high thermal costs, low-income consumers and enormous tariff subsidies.

These distribution companies were transferred to Eletrobras around 15 years ago as part of these companies' privatization process, but given the change in government orientation from 2003 onwards, privatizations were halted and Eletrobras ended up becoming the manager of these assets.

The accumulated losses at these companies during the last 10 years correspond to R$ 41 billion and have led Eletrobras to capitalize them through this period and to delay fuel payments to suppliers, generating a R$ 16 billion debt (mainly with Petrobras).

The value lost in such companies (only 5% of Brazilian electricity consumption) in the last 10 years is so impressive that this sum is close to the value of all the net regulatory asset base of Brazilian distribution companies (excluding Rio and São Paulo). In other words, with the money lost, Eletrobras could have built almost an entirely new distribution grid in Brazil.

Exhibit 3: Main figures of Distribution Companies

Last 10 years	Real Term	NPV @ 10% real
Net Income	R$ -31 bn	R$ -41 bn

Company	DEC* (h)	FEC** (times)
ED Acre	58.9	43.5
ED Amazonas	47.3	29.9
ED Rondônia	32.2	21.6
ED Roraima	34.5	50.5
ED Alagoas	21.5	16.8
ED Piauí	23.4	16.4
Eletrobras D (A)	**31.9**	**22.8**
Brazil Average (B)	**15.8**	**8.9**
(A) / (B)	2.0x	2.6x
N/NE Benchmark Companies' (C)	**17.9**	**11.0**
(A) / (C)	1.8x	2.1x

*DEC: Duration of Power Outages (Hours/Client/Year) and **FEC: Frequency of Power Outages (Times/Client/Year)

Source: 3G Radar estimates based on public company data; the distribution companies in Exhibit 3 have been selected by 3G Radar for illustrative purposes only and do not represent the full range of possible comparative outcomes which may differ materially from the results shown.

Again: Who has benefited? Definitely not Brazil, but rather dishonest people stealing energy and corrupt politicians. As shown above, consumers in these regions have the worst quality indicators in the country and still must pay for the energy stolen by others.

Future: In a very important decision in July 2016, Eletrobras' shareholders decided not to renew the concession contracts to operate these assets from August 2016 onwards.

As a result, Eletrobras has until the end of 2017 to privatize these companies. If they are not privatized by the deadline, the assets revert to the Federal Government. Eletrobras would remain with the liabilities and receive an indemnification for their RAB (regulatory asset base).

It is worth mentioning that the role of the national regulatory agency (Aneel) on this front was very important: Aneel established minimum quality levels and maximum financial leverage levels for distribution companies whose concession contracts expired in 2015 and needed to be renewed.

The regulatory body gave Eletrobras no other choice than not renewing these concessions – given the established criteria, Eletrobras would soon be forced to return the concessions. So, the company's decision only anticipated something that would have ended up taking place in 2 years. Regulation played a key role in halting the economic losses and in providing "hope" that consumers in these areas could have a better quality service.

3G RADAR

4) The Overall Inefficiencies – R$ 85 billion loss

In this section, we discuss how Eletrobras inefficiencies were another source of big value destruction during the last 15 years. We use two different approaches: The first is an absolute one where we estimate the annual inefficiency cost by assuming benchmark figures on cost standards. The second is a direct comparison we have conducted between Eletrobras Generation and Transmission subsidiaries with selected private players in order to measure differences in tax paid, dividends, and capex.

i) Direct benchmark comparison

In our calculations, when comparing Eletrobras with its closest private companies, operating costs could be R$ 4.1 billion lower per year (excluding distribution companies). Assuming that the size of this inefficiency was the same in real terms in the last 15 years, the **accumulated inefficiency cost** would amount to **R$ 85 billion** (adjusted by cost of capital).

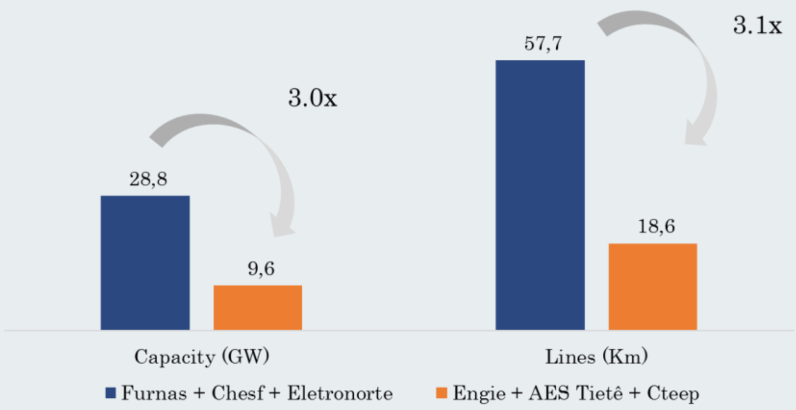
ii) Comparisons with Privatized companies

As the following table shows, we compare two privatized generation companies in 1999 and one transmission company privatized in 2006 (Engie, AES Tietê, Cteep) with Eletrobras' three most representative subsidiaries – Furnas, Chesf and Eletronorte.

We have conducted two comparisons:

a) Direct comparison: Furnas + Chesf + Eletronorte **vs** Engie + AES Tietê + Cteep;
b) Adjusted comparison: Furnas + Chesf + Eletronorte **vs** **3x**(Engie + AES Tietê + Cteep) in order to adjust for the companies' asset sizes (see below).

Exhibit 4: Comparison between Furnas + Eletronorte + Chesf vs Engie + AES Tietê + Cteep



Source: 3G Radar estimate based on public company data; the privatized companies in Exhibit 4 have been selected by 3G Radar for illustrative purposes only and do not represent the full range of possible comparative outcomes which may differ materially from the results shown.

Once again, the compounded cost of such inefficiencies is somewhat surprising even for those who follow these companies for a long time. It is worth mentioning that we have adjusted the main numbers for the Selic rate and the capex was adjusted by inflation.

Exhibit 5: Taxes, Dividends and Net Income of Eletrobras (Furnas, Chesf and Eletronorte) vs Privatized Companies (Engie, AES Tietê and Cteep)

Last 15 years (R$ bn)	Eletrobras (A)	Privatized (B)	(B) – (A)	3x Privatized (C)	(C) – (A)
Taxes	20.6	25.9	5.3	77.7	**57.1**
Dividends	0.1	61.3	61.2	183.9	**183.8**
Net Income	32.7	72.4	39.7	217.2	**184.5**

Source: 3G Radar estimates based on public company data

1) The amount of income tax/social contribution plus dividends that Eletrobras subsidiaries have paid to the Federal Government/Eletrobras amounted to R$ 20.7 billion versus R$ 25.9 billion in taxes paid by 3 privatized companies (Selic adjusted), if we adjust by their asset sizes this difference would jump from R$ 5 billion to R$ 57 billion! **Only 3 privatized companies generated a higher cash flow to the country through taxes than what Eletrobras subsidiaries paid with both taxes and dividends.**

It is interesting to notice that Engie represented only 5% of Eletrobras asset when privatized in 1998 – today, Engie's market cap is 15% larger than that of Eletrobras.

Exhibit 6: Capex and Value Destruction of Eletrobras (Furnas, Chesf and Eletronorte) vs Privatized Companies (Engie, AES Tietê and Cteep)

Last 15 years (R$ bn)	Eletrobras (A)	Privatized (B)	(B) – (A)	3x Privatized (C)	(C) – (A)
Capex	84.2				
Value Destruction	-20.3				
Efficient Capex	63.9	21.7	-42.2	65.1	1.2

Source: 3G Radar estimates based on public company data

2) Regarding investment levels, Eletrobras subsidiaries' capex amounted to R$ 84.2 billion (inflation adjusted) versus R$ 65.1 billion for the private companies' asset adjusted figures (R$ 21.7 billion non-adjusted). By this comparison, we can say that Eletrobras has invested more capital. However, as we have discussed in previous sections, the value lost only with structuring generation projects (Belo Monte, Santo Antonio and Jirau) corresponds to R$ -20.3 billion. Adjusting only for this effect, we can say that the real capex of private companies (efficient capex) was equivalent to Eletrobras figures.

As these tables show, despite private companies not belonging to the Federal Government, they provide higher revenues to the Government and invest more efficiently than state-owned companies and to top it off, with no public capital allocated by the country. In addition to that, they create better opportunities for their employees.

On the contrary, state-owned companies have been primarily working for the ones that directly benefit from its inefficiencies. The losers were the competent employees, its shareholders, electricity sector players, and consumers in general.

The value destruction caused by such inefficiencies and corruption (as evidenced by the Car Wash operation findings) correspond to R$ 166 billion, eight times higher than Eletrobras current market cap.

Exhibit 7: Subtotal of value destruction in Eletrobras (does not include the "MP 579" impact)

Value Destruction	R$ bn
Structural Projects	20
Angra 3	20
Distribution Companies	41
Overall Inefficiencies	85
Subtotal	**166**

Source: 3G Radar estimates based on public company data

We conclude that during the last 15 years, Eletrobras' "true shareholders" were the aforementioned corrupt construction companies, suppliers and politicians, together with those who benefit from inefficiencies, who created significant value for themselves without paying anything back to the country.

The Future: The company has launched a program to:

a) Reduce its workforce by 30%;
b) Optimize real estate assets;
c) Create a Shared Service Center;
d) Improve corporate governance / capital discipline process;
e) Privatize distribution companies (sold Celg at 28% premium to minimum price);
f) Simplify its complex structure (17 subsidiaries, 178 SPCs, etc.);
g) Initiatives to solve legal contingencies relative to the compulsory loan.

Despite all the progress so far, we believe that Eletrobras' CEO still needs more autonomy to replace/appoint executives for key positions at the company's subsidiaries. We see no reason why he should have less autonomy than Pedro Parente at Petrobras. Both companies are listed on B3 and NYSE, have institutional minority shareholders and an obligation to improve corporate governance after the recent corruption scandals. The new "Lei das Estatais" has been an important instrument to the board of directors to reject indications that do not fulfill the minimum technical background for these positions.

Eletrobras also needs a more efficient compensation plan for its top management given that current policies are not enough to recruit and retain top tier professionals.

It is also worth mentioning that other federal companies, such as Correios, Petrobras, and Banco do Brasil, have also been conducting cost cutting initiatives, which evidences the urgent need to improve efficiency at federal companies.

In addition, new regulatory proposals could make it easier to privatize some of Eletrobras assets, but many details on how this could take place are still open. This could add tremendous value to the company and the Government as full privatization is the "once and for all solution" for key inefficiencies. The model used in 2004 to "re-privatize" Cemar could be a first step in this direction, allowing Eletrobras to sell control while maintaining a minority stake in a much more efficient company.

5) The "MP 579" – A R$ 20 billion economic loss

In addition to all the problems that we have mentioned, Eletrobras was highly affected by the so-called "MP 579" back in 2012, which artificially forced electricity prices down 20% in a re-election year, entailing massive negative impacts to the entire sector, while causing an imbalance in supply/demand, price distortions, and balance sheet problems for state-owned companies.

Since 2015, some of the negative consequences of the "MP 579" to the transmission business have been reverted, but the key problems in the generation segment – the insufficient tariff to cover costs and the economic compensation for the non-depreciated assets on the renewed plants – are still there and have caused a **R$ 20 billion**[6] economic loss to the company.

Exhibit 8: Total of value destruction in Eletrobras

Value Destruction	R$ bn
Subtotal of Inefficiencies and Corruption	166
"MP 579" Economic Impact	20
Total	**186**

Almost 10 times actual Market Cap!

Source: 3G Radar estimates based on public company data

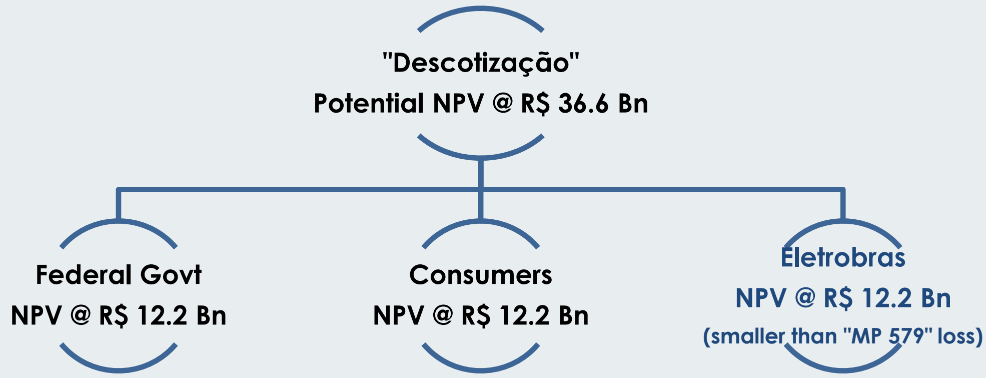
It is worth mentioning that Eletrobras was the only company to accept the "MP 579" terms for the generation segment. Other state-owned companies like Cesp and Cemig rejected the proposal and did not renew their generation concessions under such terms. This fact highlights the unfavorable terms for the generation segment and their acceptance constituted a clear conflict of interest (condemned by the CVM in 2016) and were only approved through the extensive use of political influence. Minority shareholders voted against the proposal.

The Future: On this front, we are glad to see that MME is proposing to partially revert the impacts of "MP 579" in the generation sector through a process known as "descotização". In this process, the plants whose concessions were renewed in 2012 will be able to freely sell its energy if sold in a privatization process. The economic value created from the "descotização" would be equally split between Eletrobras, consumers and the Government if it is done by the end of 2019.

In a simple exercise, considering that Eletrobras sells all of its assets affected by "MP 579", we estimate it could generate a positive NPV of R$ 36.6 billion with the "descotização". In order to fully compensate Eletrobras for the negative impacts of the "MP 579", the company would have to keep 55% of the value (higher than the 33% proposed in the draft law).

[6] 3G Radar' estimates of the difference in Eletrobras' results (2013-2015), adjusted by cost of capital, if the company did not renew their generation concessions under such terms.

Exhibit 9: Potential NPV of "Descotização"



Source: 3G Radar estimates based on MME public technical note

If we also include the value destruction of the structural projects and Angra 3, the total loss would be of R$ 60 billion – even if Eletrobras retained 100% of the gains of the "descotizacao" process it would still not be enough to cover the losses caused by the Federal Government´s direct influence in the company.

It is worth mentioning that the only scenario where it would make sense for Eletrobras to accept the proposed "descotizacao" is the one where part of the economic value created would be captured by the company through direct revenues. This would be a win-win situation for the company, country and consumers. On the other hand, any decision based on directing the potential revenues exclusively to the Federal Government and resulting in a capital increase at Eletrobras would be a clear conflict of interest and would not make sense for the company and minority shareholders.

In addition to the above-mentioned impacts suffered by Eletrobras, we think it is similarly important to show the cost of bad Federal Government capital allocation:

A simple approach shows the absurd cost that the combination of bad investment decisions, corruption, and inefficiencies at Eletrobras had to the country.

Considering Eletrobras book value of R$ 67 billion at the end of 2002, the average cost of the Brazilian debt measured by the Selic rate and the dividends distributed by the company as well as the capital increases, we estimate that allocating capital in Eletrobras during the last 15 years costed the country approximately R$ 228 billion. Yes, **R$ 228 billion!** (considering only Federal Government 63% stake). This value is equivalent to 4% of Brazilian GDP and 7% of the Brazilian public net debt.

The compound negative impact of capital allocation in an inefficient state-owned company is much higher than most people imagine. This is just the direct impact. We can count as indirect impacts the poor quality of services, the delays in many important projects, and the under-investment by serious private players.

This R$ 228 billion corresponds to approximately the replacement value of all the hydro generation capacity in Brazil, or 4-5 times of the entire distribution grid.

The Future: The good news is that given Brazilian Fiscal constraints and the need for infrastructure investments in the country, the Federal Government has been conducting measures to attract private investments through a series of positive regulatory changes and Eletrobras size reduction (as already discussed). We believe that such a move is very positive for the country, for electricity consumers and for Eletrobras.

A Brief Note on the Proposed Regulatory Changes

The Minister of Mines and Energy has recently launched a public consultation on proposed changes to the Brazilian electricity sector. In our view, the measures are in the right direction to attract sustainable private investments for the sector. The pillars are:

a) Right market price signal (correcting different price distortions and introducing capacity and energy payments);
b) Increasing free market (end of market reserve and correcting distortions in the migration from captive market to free market);
c) Optimizing sector transaction costs;
d) Solutions for different sector legal issues (GSF, RBSE dispute, CDE payments);
e) Eletrobras efficiency (potential assets privatization);
f) Adjusting subsidies regulation.

Although the measures might still suffer some adjustments, they are a clear positive and important turning point for the sector. If Eletrobras is able to directly compensate part of the R$ 20 billion loss caused by the "MP 579" political interference, it could be another important step in the path of the company recovering from the many shocks it suffered in the past (from mismanagement to disastrous Government decisions, most of which we covered in this letter).

In our view, it is clear to the team at the MME that recovering Eletrobras is a key development to achieve an efficient electricity sector regulatory framework and that Eletrobras' role in the next 15 years should be very different than it was in the last 15 years. Of course, the final measures will depend on many different parties involved such as Congress and the Finance and Planning Ministries.

Our Eletrobras investment is based on the intrinsic value that we estimate for the company's assets under conservative long-term assumptions, as well as reasonable minimum dividend figures for its preferred shares. Our assessment of value was not based on any potential change in regulation nor in efficiency gains.

Although they are not factored in our base case, we recognize that a highly capable management team, a market oriented MME and a good regulation are all factors that could greatly leverage the intrinsic value of the company, strongly benefiting all stakeholders (Government, employees, consumers, minority shareholders, etc).