



Shorting Brazil

Hedge fund manager Luciano Tavares beat peers by betting against the South American country's biggest stocks. **By ALEXANDER RAGIR and LAURA PRICE**

LUCIANO TAVARES's hedge fund came out near the top of recent rankings of peers thanks to his unusual view of Brazil. By short selling the country's biggest stocks, he didn't need a bull market to make money.

Tavares's view differs from those of many investors in another way, too. His office looks out on a snarled 16-lane highway in São Paulo, the country's financial center and largest city. No beaches in Rio de Janeiro for him. "I like it a lot here," Tavares, 34, says. "I've been in São Paulo for 18 years, so I'm

almost a Paulista."

Tavares's Nest Fund Ltd.—Long Short Equity, a \$117 million Cayman Islands—incorporated fund, beat 93 percent of its peers in the 12 months ended on Sept. 30, according to data compiled by Bloomberg. The co-founder of hedge fund firm Nest Investimentos Ltda., who manages the fund with fellow firm co-founder Francisco Meirelles de Andrade, 36, did it by betting against Brazil's biggest oil

producers and metals miners while buying agricultural commodity producers such as SLC Agrícola SA. The Nest fund gained 25 percent in the year through the end of September, while Brazil's benchmark Bovespa Index was down 18 percent. Type NESTFUA KY <Equity> HFA <Go> to use the Historical Fund Analysis function to track the fund's performance.

In the second half, Tavares and Andrade short sold shares of Petróleo Brasileiro SA, Brazil's

state-controlled oil company, and Cia. Vale do Rio Doce, the world's biggest iron ore miner. "With a global recession looming, the commodity cycle has reached its end," Tavares says, adding that Petrobras and Vale will likely fall more than their competitors in the downturn.

For years, Petrobras and Vale, Brazil's biggest companies, have been two of the country's best stocks to hold. During the five years ended on Dec. 31, 2007, Petrobras rose 51 percent a year on average, while Vale gained 44 percent annually.

Andrade says that for many years, a trade that worked for many investors was simply buying hard commodities and shorting every other industry in

Brazil. That changed when commodities started to drop in July, however. "We think there is a good probability that hard commodities will keep falling in the next quarters," he says.

PETROBRAS WAS down 45 percent this year through Oct. 10, while Vale was down 53 percent. You can use the Financial Analysis (FA) function to display oil- and mining-industry-specific data for a selected

'With a global recession looming, the commodity cycle has reached its end,' Tavares says.

Cheat Sheet

Type **HFND <Go>** for the Hedge Fund Home Page function, which lets you access fund rankings, functions and information.



Tavares says that parts of the Brazilian economy are poised to perform well.

company. Type VALE5 BZ <Equity> FA <Go> to analyze Vale, for example. Click on the Industry tab at the bottom of the screen and then on Other Metals under Mining & Metals Analysis to display data

including the company's actual quarterly iron production.

Tavares and Andrade also made bets on financial stocks this year. They bought shares of Brazilian banks such as Banco Bradesco SA and Banco Itaú Holding Financeira SA while shorting U.S. financial institutions such as Citigroup Inc. and Lehman Brothers Holdings Inc. Lehman, a 158-year-old New York-based investment bank, filed for bankruptcy protection on Sept. 15, sending its stock plunging to 21 cents a share.

Short sellers typically borrow shares to sell in the expectation that the price will drop and they can then buy back the stock for less. Short interest refers to the number of shares currently being sold short.

You can use the Short Interest (SI) function to track data on shorting for a selected stock. Type C US <Equity> SI <Go>, for example, to graph short interest, price and volume data for Citigroup. The short interest ratio is the total number of shares being sold short divided by the average daily trading

volume. Citigroup's short interest ratio on Aug. 29 was 2.27, indicating that traders were short selling more than twice the number of shares that typically change hands each day.

That was before the U.S. Securities and Exchange Commission temporarily banned short selling of financial stocks on Sept. 19. The ban was lifted on Oct. 9. Type SSR <Go> to monitor bans around the world with the Short Selling Restricted function. "All of the stocks tied to credit that have been punished so much lately are going to be very cheap as the crisis subsides," Tavares says. "These sectors should rebound when this crisis calms down a bit."

THE NEST FUND'S gains from selling short U.S. banks this year were augmented by increases in Brazilian banks. The MSCI Brazil Financials Index rose 12 percent from January through June.

In October, the fund added to holdings of Brazilian banks in the expectation that policy makers will lower interest rates in Brazil in 2009, Andrade says. "With commodity prices falling, inflation should ease and let the central bank cut rates," he says. "We've stuck mostly to banks because they're more liquid, but eventually I think real estate and retailers may start looking good, too." You can use the Economic Forecasts (ECFC) function to display historical data and composite forecasts for Brazil's key economic indicators and central bank rates. Type ECFC <Go>, click on the arrow to the right of Country and select Brazil. Click on Central Bank Rate (%) to display details of the economists' forecasts that are included in the composite projections.

Another Brazilian company the Nest fund has held this year is SLC Agrícola, a Pôrto Alegre-based cotton, soybean and corn producer. Its stock rose 94 percent in 2008 through the end of June. "One of our strategies that is still valid is soft commodities over hard commodities," Tavares says. "We're pretty bearish on commodities overall, but if we buy any commodity it would be agricultural because we think they are much better prepared to deal with slower growth."

A stronger dollar cuts demand for commodities as a hedge against inflation, Andrade says. "If the

Luciano Tavares

Nest Investimentos
Portfolio manager

EDUCATION

Earned a bachelor's degree in business administration from Fundação Getúlio Vargas in São Paulo in 1995.

CAREER

Went to work at Merrill Lynch in São Paulo in 1995 structuring equity derivatives. Co-founded Nest in 2005.

PERSONAL

Age 34

HISTORICAL FUND ANALYSIS

Type HFA <Go> to track the performance of a selected fund versus a benchmark.



95) Edit Columns		Agriculture Supply and Dem			
Soybean		Source	All	Year	
Crop Calendar		Unit	1000 Metric Tons	Type	
Location	Src	Open Stock	Production	Import	Consumption
1) Africa					
2) Nigeria	USDA	.00	450.00	3.00	453.00
3) South Africa	USDA	19.00	350.00	70.00	410.00
4) Asia/Oceania					
5) China	USDA	3,356.00	16,500.00	36,000.00	51,570.00
6) China	DCI	6,414.00	14,750.00	39,150.00	51,720.00
7) Europe					
8) Russia	USDA	19.00	700.00	250.00	945.00
9) Ukraine	USDA	20.00	700.00	.00	470.00
10) North America					
11) United States	USDA	3,811.00	79,848.00	272.00	53,049.00
12) Canada	USDA	146.00	3,170.00	350.00	1,746.00
13) South America					
14) Brazil	USDA	3,235.00	62,500.00	160.00	35,525.00
15) Argentina	USDA	680.00	50,500.00	3,450.00	39,440.00
16) World	USDA	13,659.00	236,888.00	75,511.00	234,045.00

AGRICULTURE STATS

Type **AGSD <Go>** to display data on supply and demand for food-related commodities around the world.

dollar rises, agricultural commodities will fall along with everything else,” he says. “We just think they will do better than hard commodities.” The dollar traded at \$1.3408 per euro on Oct. 10, up 19 percent from the record low of \$1.6038 per euro touched on July 15.

To analyze data on agricultural commodities, type **AGSD <Go>** for the Agriculture Supply and Demand—Balance Sheet function. For data on soybeans—of which Brazil is the world’s largest exporter—click on the first arrow in the upper-left corner of the screen and select Soybean. You can click on the next arrow to the right to select whole soybeans, soybean meal or soybean oil.

To chart Brazil’s soybean consumption, click on the number for Brazil in the Consumption column. You can add other countries or regions to the chart by clicking in the boxes on the left side of the screen. Global soybean consumption rose 66 percent to 234 million metric tons in 2008 from 1998. To view the data in table format, type **1 <Go>**.

You can use the Commodity Price Forecasts (CPF) function to display analysts’ forecasts for agricultural commodities. Type **CPF <Go>** and click on the View Products button on the red tool bar. Press **<Page Fwd>** twice and click on Soybeans to display forecasts.

Tavares and Andrade also bought the stock of Brazil’s biggest food producers, Perdigão SA and Sadia SA. The food industry is one part of the Brazilian economy that’s poised to perform especially well, Tavares says. “When we say soft commodities, we’re not just talking about agriculture but the food supply chain in general, like food processors Sadia and Perdigão,” he says.

The two managers use leverage to magnify bets by buying on margin or using borrowed money to purchase securities. Andrade says the fund usually borrows the same amount it owns, so its gains, or losses, are doubled. In August, Nest reduced leverage to less than 50 percent of its assets because the market was going through what Andrade termed a moment of uncertainty.

TAVARES, WHO WAS BORN in Salvador, the capital of the Northeastern state of Bahia, graduated with a degree in business administration in 1995 from Fundação Getulio Vargas in São Paulo. After school, he got a job at Merrill Lynch & Co. in São Paulo, where he worked for five years structuring equity derivative products for Latin America. Merrill sent him to work for a brief stint in New York. Tavares joined fellow Fundação Getulio Vargas alumni Andrade and two other partners in founding Nest in 2005. As of October, the firm oversaw \$250 million.

To find funds that use strategies similar to those of the Nest fund, type **FSRC <Go>** for the Fund Search function. Tab in to the field and enter **BRAZIL**. In the list of matches, click on the Geographic Focus listing for Brazil. Then enter **LONG SHORT** in the field and select Long/Short Equity for Management Style. Type **1 <Go>** to view the results. To sort the funds by any of the criteria on the screen, simply click on a column header, such as Tot Ret 1Y for the one-year total return.

During an interview in August, Andrade points out the office window and indicates the other side of the highway. “I live in that building over there,” he says. “Some people move to Florianópolis or Rio de Janeiro because they think it’s a nice place to live or they like the beaches, but I like São Paulo. It’s the center, a big city. There’s always something to do. It’s like New York.”

Andrade’s apartment, where he lives with his wife and a daughter who was born in July, is only 2 kilometers (1.2 miles) away from his office. Yet it takes about 10 minutes to get there because of traffic. “I drive,” he says. “It’s pretty dangerous to walk.” **B**

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