Investor Letter

3rd Quarter, 2024

"You say you want revolution
Well, you know
We all wanna change the world
You tell me that it's evolution
Well, you know
We all want to change the world"

Excerpt from the lyrics of the song "Revolution" by the Beatles.

The **Porto SFA** fund ended the 3rd quarter of 2024 with a year-to-date return of -3.81%, while its benchmark, Ibovespa, had a return of -1.77%

Period	Porto SFA	Ibovespa	CDI
3Q24	4.78%	6.38%	2.63%
YTD	-3.81%	-1.77%	7.99%
Last 3 years	11.49%	16.05%	39.81%
Last 5 years	49.63%	26.90%	49.13%
Since inception	341.28%	146.36%	174.39%

Introduction

The third quarter of 2024 reinforced the challenges faced by local assets. While the global market is showing historic records on several exchanges, driven by a scenario of lower interest rates and positive expectations for economic growth, Brazil continues to go against the trend. The country's fragile fiscal context has kept our stock market and our currency among the most devalued in the world this year.

The environment of inflationary pressure, aggravated by the exchange rate depreciation, with the real devaluing significantly against the dollar throughout the year, led the Central Bank to begin a new cycle of Selic rate hikes.

In the stock market, companies most exposed to the domestic economy are the ones that have suffered the most. Despite this, we observe that many of these companies are trading at extremely depressed prices, reflecting a significant degree of pessimism. However, without clear triggers for structural improvements, such as fiscal consolidation or relevant economic reforms, these opportunities remain hampered by uncertainty.

As long-term investors, we understand that current challenges are part of the natural cycle of the markets. It is precisely in these moments of uncertainty that the best opportunities arise for those who maintain discipline, patience and conviction. Our strategy continues to be based on building a robust portfolio, balanced between real assets – solid and resilient companies – and strategic protections, such as dollar hedging, to mitigate short-term risks.

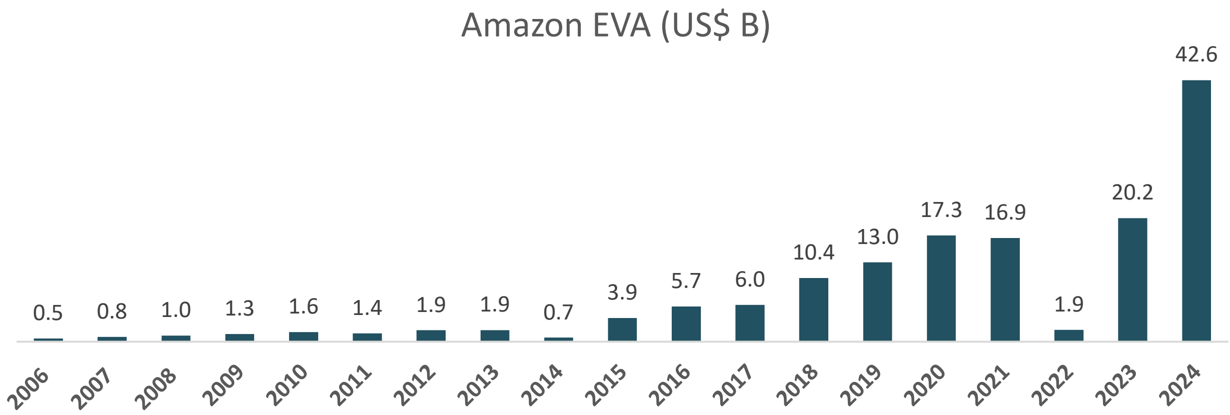
We remain confident that by maintaining our focus on solid fundamentals and our long-term vision, we will be well-positioned to take advantage of the recovery and capture significant returns when the outlook stabilizes.

Amazon: 30 Years of Value Generation. And More?

"You say you want a revolution, well, you know, we all want to change the world." This is how "Revolution" begins, one of the Beatles' greatest hits, a hymn to transformation, to the search for something greater and to the desire to change the status quo. In many ways, this phrase seems to sum up the trajectory of Amazon – a company that not only wanted to change the world, but actually did so.

Amazon, founded in 1994 by Jeff Bezos in the early days of the internet's popularization as an online bookstore, has become a global technology giant with operations in several segments, including online retail, logistics, advertising, streaming and cloud computing. Its culture, focused on customer obsession, constant innovation and operational excellence, has driven the company to achieve a dominant position in several markets. Amazon is a company with operations in several countries and a workforce that employs more than one million people. The scope and complexity of its activities range from the sale of everyday products to the development of cutting-edge technologies in artificial intelligence and robotics. Over the years, the company has built significant competitive advantages, such as its vast logistics network, the network effect of its marketplace, and the development of proprietary technologies, in addition to having become a leader in cloud computing.

From an economic and financial perspective, Amazon's track record is impressive, with unprecedented value generation in the history of capitalism. The company has found opportunities to monetize its various services. For example, Amazon created a new business that arose from the need to optimize its own computing infrastructure and began offering computing infrastructure services to its customers, creating the cloud computing service, AWS, an area of activity that took the company to a new level of value generation.



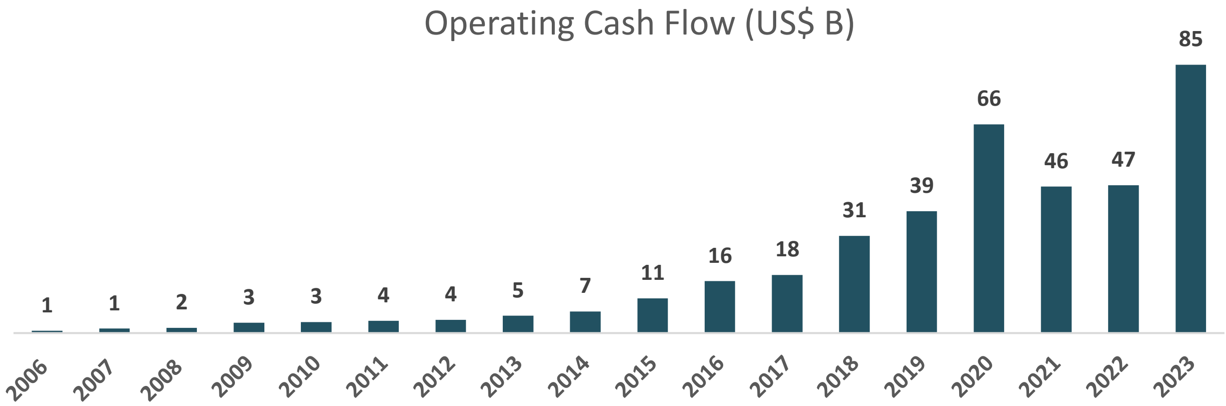
Source: SFA

The company continues to invest in innovation, seeking new markets and technologies to fuel its growth. The company has also expanded its business internationally, replicating its successful model in new countries and expanding its customer base globally. With a strong culture, focused leadership in capital allocation, and a track record of exemplary execution, Amazon is well-positioned to continue to lead and create value in a variety of markets in the years ahead.

Amazon's track record of value creation is impressive, but what matters to us investors is future value creation, and in our thesis, we believe that Amazon still has a lot of value to deliver to its shareholders. When we come across a company with 30 years of history and that generates a lot of EVA, we wonder if the company has reached maturity. In this letter, we will explore that there are still opportunities for capital allocation in new markets, results to be reaped from the investments made in recent years, the increase in its shareholding outside the US, opportunities to cut costs and expenses, and consolidate its presence in cloud computing. We believe that Amazon, using its competitive advantages and execution capacity, will be able to transform the various growth opportunities into value creation for its shareholders.

I. Capital Allocation

Since its inception with investments from family and friends, including $250,000 from Jeff Bezos' parents, Amazon has always valued the good use of capital. After its IPO in 1997 and throughout its history, Amazon has distinguished itself from other technology companies by having financed its own growth by reinvesting the cash generated in its operations. The company has not raised any funds through subsequent share issuances or issued any debt and has delivered exponential results in value generation, a good example of a company that reinvests its own capital well.

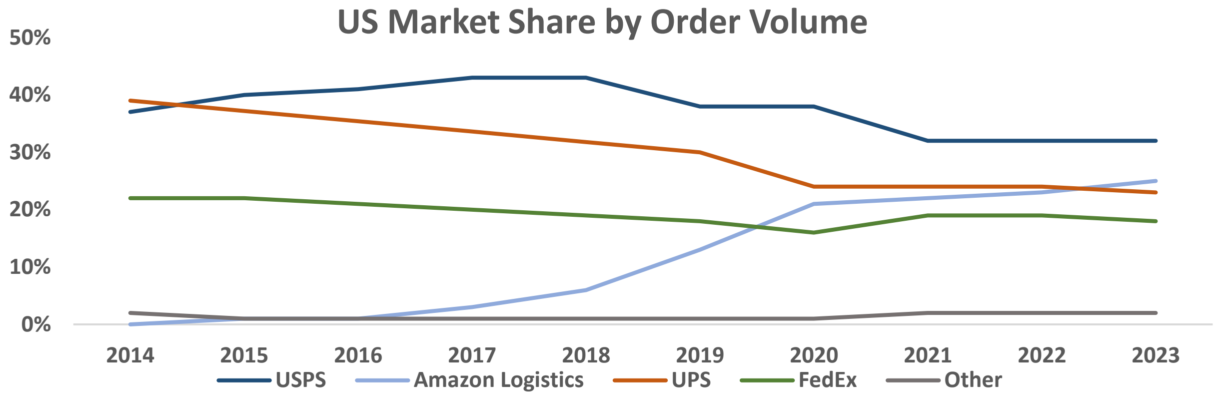


In its main segment, e-commerce, Amazon still has a lot of value to be extracted from the continued execution of its playbook. Amazon must continue to improve its level of service, increasing buyers and sellers (network effect) and capturing ever greater revenue. Therefore, part of our thesis is based on the continuation of the exemplary execution it has had so far in retail, to gain greater share not only in e-commerce, but in the retail sector as a whole. In addition to the growth of this segment, we see room for Amazon to increase its take-rate in e-commerce, Prime monthly fees and advertising. There is also value in the efficiencies that can be unlocked, reducing operational costs. To illustrate this, let's talk a little about the monetization of services and logistics.

Monetization of “Services” and Logistics

Cloud computing is an example of what Amazon itself calls “monetizing the P&L line.” AWS was born out of the idea of monetizing Amazon’s fixed assets. The idea for AWS came about primarily because of two factors Amazon observed: the need for robust computing infrastructure to handle spikes in demand on its own e-commerce site, and the realization that this computing capacity was often underutilized. This led to the idea of renting out this excess capacity to other companies or developers, which would allow Amazon to monetize its infrastructure.

Logistics is another more recent example. The financial turnover of Amazon's e-commerce business is already close to trillions of dollars, and to achieve this, its services need to reach unprecedented scale and excellence. Amazon's complex logistics operation ends up being a business in itself, as it is already so significant in its market that it starts to serve third parties and generate incremental value. In 2023, in the US, Amazon processed approximately 5.9 billion packages, ranking 2nd in the logistics ranking, and for the first time in history, surpassing UPS - one of the largest logistics companies in the world, which moved 5.5 billion packages in the same period. It is worth noting that in addition to e-commerce, Amazon is a giant logistics operator in the US.



Source: Pitney Bowes, Chartr

Amazon is strategically expanding its logistics services by offering air cargo capacity to third-party customers through Amazon Air. This service includes options such as on-demand bookings, charters, and blocked space for various types of cargo, leveraging a fleet of over 100 aircraft and 250 daily flights globally. Previously, Amazon had been selling space quietly but is now promoting it more openly to attract a broader range of customers beyond Amazon Prime subscribers. The move is seen as a way to streamline operations and compete with established carriers like FedEx and UPS without directly confronting them. As Amazon positions itself more prominently in the logistics industry, potential challenges include pricing strategies and managing the complexities of different types of cargo. This expansion marks a significant step in Amazon's growing role as a logistics provider, aiming to sharpen its competitive edge while making better use of its existing capabilities. So, from a capital allocation perspective, we see a company that will increasingly be able to get more bang for its buck.

aircargonews.net/airlines/amazon-air-takes-on-cargo-carriers-with-launch-of-sales-to-third-parties/

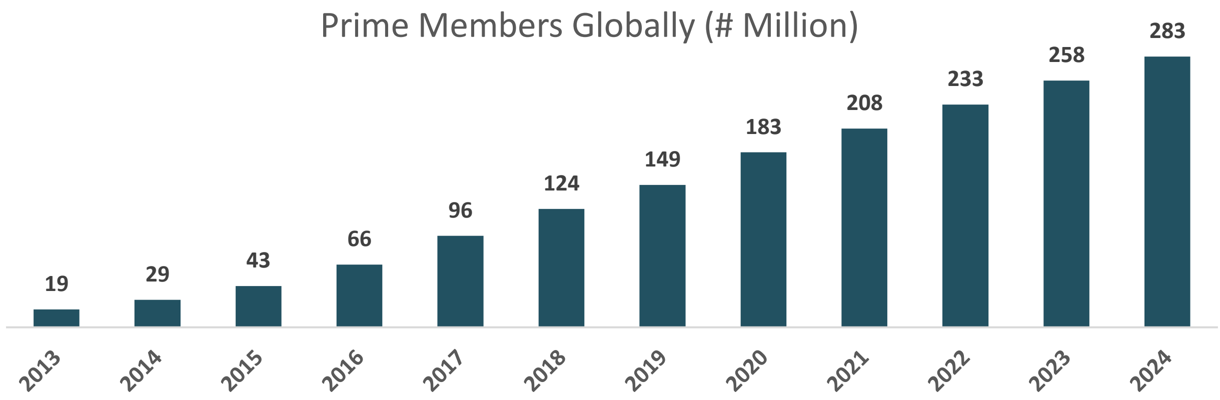
Amazon Prime Video – Capital Allocation Beyond Streaming

A good example of capital allocation is Amazon Prime. Amazon identified an opportunity to increase the value of its existing customer base by enriching Prime Video's content offerings. The goal was to transform Prime Video into a core value engine that not only retains existing customers but also attracts new subscribers through exclusive, high-quality content.

Responding to this opportunity, Amazon has committed billions annually to both creating original content and acquiring exclusive streaming rights. Notable investments include popular series such as "The Marvelous Mrs. Maisel" and "Jack Ryan," and significant deals for licensed content and broadcast rights to live sporting events such as the NFL's "Thursday Night Football."

The benefits of Amazon's strategic investments in content creation and acquisition are profound. Prime Video has been instrumental in growing and retaining Amazon Prime subscribers, increasing the perceived value of the subscription and reducing churn rates. By integrating Prime Video with other Prime services, such as free shipping, Amazon has strengthened brand loyalty and encouraged greater spending on its platform. This focus on content has opened up new revenue streams through advertising on the streaming platform and partnerships with third-party content providers.

Amazon's strategic focus on creating and acquiring streaming content has solidified its competitive position and created significant value for its subscribers and shareholders. These benefits, both present and future, highlight Amazon's ability to innovate and deploy capital in a rapidly evolving digital environment.



Source: SFA

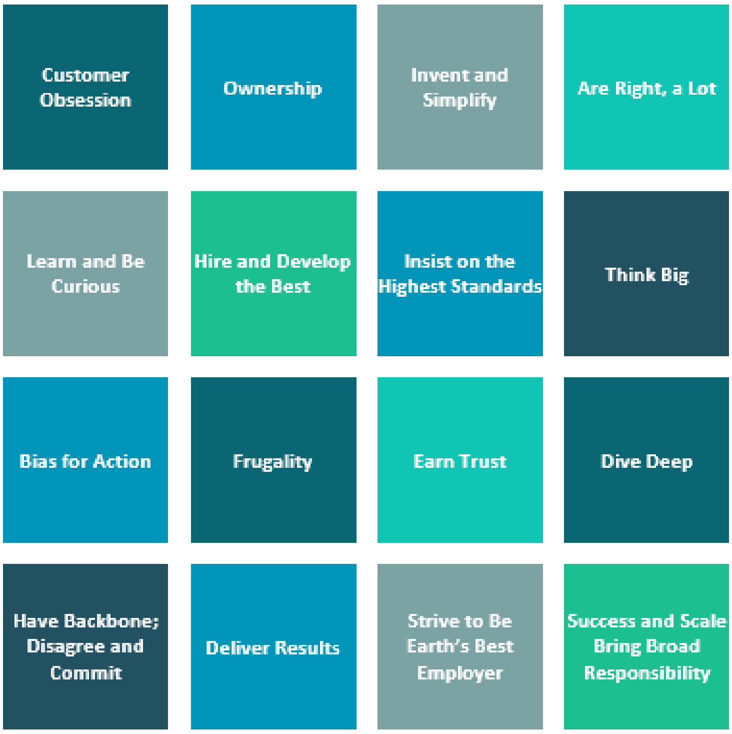
Andy Jassy, RTO and Culture

Algo que notamos em empresas que possuem boas decisões de alocação de capital é que possuem uma cultura empresarial muito forte. No começo da Amazon, as decisões de alocação de capital podem ser atribuídas principalmente a Jeff Bezos. À medida em que a Amazon foi crescendo, a forma que Jeff Bezos encontrou de disseminar boas práticas em processos decisórios foi fortalecendo a cultura. Quanto mais forte e clara for a cultura da empresa, melhores tendem a ser as tomadas de decisões importantes.

One thing we've noticed about companies that make good capital allocation decisions is that they have a very strong corporate culture. In the early days of Amazon, capital allocation decisions can be attributed primarily to Jeff Bezos. As Amazon has grown, Jeff Bezos's way of instilling good practices in decision-making has strengthened the culture. The stronger and clearer the company culture, the better the important decisions tend to be.

To this end, Bezos established 16 leadership principles at the beginning of the company, which continue to this day and should permeate and shape the way employees act. In conversations with former employees, we heard how the principles are in fact part of daily discussions and, above all, are part of the metrics for evaluating employees individually. Those who adhere more closely to the principles benefit in the individual evaluation.

16 Amazon Leadership Principles



Although the principles are of great value, Jeff Bezos' "retirement" as CEO in 2021 left us cautious. As an important figure in the company's history, we wondered whether his successor, Andy Jassy, would have the caliber needed to fill the void left by Bezos. However, after a few years of monitoring and research, we have evidence that makes it clearer that the company is being run by a good leader, who has Amazon's strong culture, understands the company's business, and is focused on efficiency and good capital allocation.

Reports from dozens of current and former Amazon employees point to Andy Jassy's focus on operational efficiency, cost cutting, and unnecessary projects, which certainly seems to have been reflected in recent margins. His capital allocation seems to be quite thoughtful, often opting for more modest investments and protecting capital. Negative examples of the "Bezos era" are "The Lord of the Rings: The Rings of Power" and "Alexa," which spent billions and billions in a somewhat chaotic and megalomaniacal way. Andy Jassy seems to be on the tighter side and keeping his accounts in check.

Since his arrival, the company's growth has rebounded, costs have been controlled and profits recently hit a record high. Amazon's shares have more than doubled, pushing the company's market value above $2 trillion for the first time. One shareholder commented: "You're seeing a much more focused and highly determined company now. I prefer Jassy to Bezos." Jassy has put a distinct personal stamp on Amazon, making sharp cuts and more calculated investments, a shift from Bezos's growth-at-all-cost management style. However, Jassy is much more attuned to Wall Street, often making key decisions with shareholders' reactions in mind.

In June 2023, Bernstein's Shmulik wrote a scathing open letter to Jassy demanding clarity on Amazon's spending to "alleviate investor concerns." Since then, the CEO has implemented dramatic improvements in nearly every area where investors were eager to see change. A year later, Shmulik acknowledged, "He delivered." Jassy has pushed the company to become more cost-conscious, cutting corners on even the smallest details. In May 2024, he released a series of internal videos where he shared his take on each of Amazon's 16 leadership principles, as outlined in an internal memo. Some employees saw the videos as a reminder to return to the company's frugal roots.

Still, some staff members have grown frustrated with the “do more with less” culture that Jassy seems determined to maintain. He has eliminated long-term, expensive projects and cut approximately 27,000 jobs. Amazon’s leadership has instructed its One Medical health unit to reduce its projected losses by at least $100 million. Even historically profitable areas like AWS and advertising have been cut.

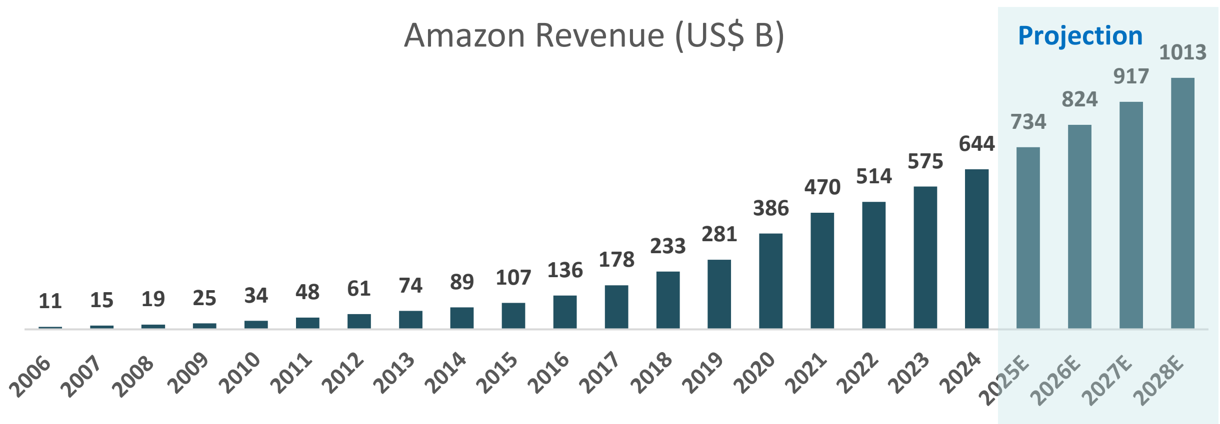
Finally, a rumor recently surfaced that Amazon is planning to reduce the number of managers in the company. This would be done in order to increase the ratio of people “doing” to people supervising/delegating. This is another move that we welcome.

Additionally, Amazon recently announced a strict return to office (RTO) policy that requires corporate employees to work in person five days a week starting in January 2025, an increase from the current three-day requirement. There have been substantial backlashes among employees. The majority express dissatisfaction, with 73% considering resignation and 80% aware of colleagues considering leaving. We believe that in-person work can foster direct collaboration and interpersonal relationship building, enhancing communication and team cohesion, which can accelerate problem-solving and innovation. Therefore, as investors, we give the benefit of the doubt to more restrictive work-from-home policies. Regardless, this demonstrates Andy Jassy’s political clout, as well as the Board’s willingness to work through friction/challenges to achieve future success.

Today, we can say that we are comfortable and optimistic with the leadership of Andy Jassy, who has the culture, discipline and capital allocation profile that we like.

II. Revenue Growth Opportunities

Amazon has a history of exponential revenue growth and value creation that is almost unprecedented. Led by a visionary and big-thinking founder, it has conquered very large markets and disrupted American retail, riding the wave of the internet, digitalization and personal devices that has created billions upon billions in market value in the US.



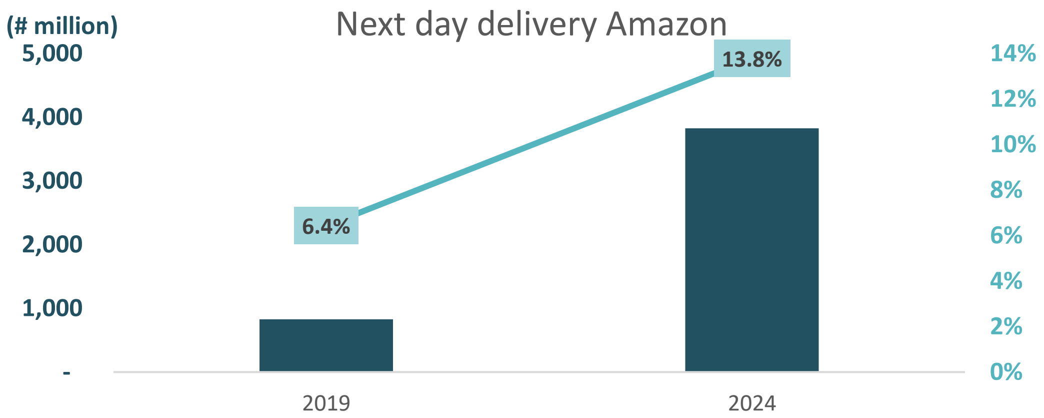
Source: SFA

Even after decades of growth, Amazon is still one of the big tech companies with the greatest growth potential. Below, we will discuss an initiative that exemplifies the potential path that Amazon still has ahead to continue increasing its revenues.

TAM Expansion: Delivery Speed and New Markets

Amazon has recently begun to more aggressively attack a market that, for it, had not been explored much until now: everyday items for its consumers, such as supermarkets and pharmacies. These categories are characterized by the need for more urgent deadlines, a higher average turnover and tighter margins in general. Some examples of categories with these characteristics would be cleaning products, daily kitchen supplies and many types of medicines that are needed immediately.

Amazon has been developing its services to improve the delivery time required (service level) for more urgent deliveries, such as restocking pantry items. In the largest US metropolises, Amazon's delivery times are getting shorter and shorter, which translates into a new addressable market. It mainly serves younger demographics, who are now buying supermarket items such as detergent and other consumer packaged goods from Amazon, instead of going to a local market.

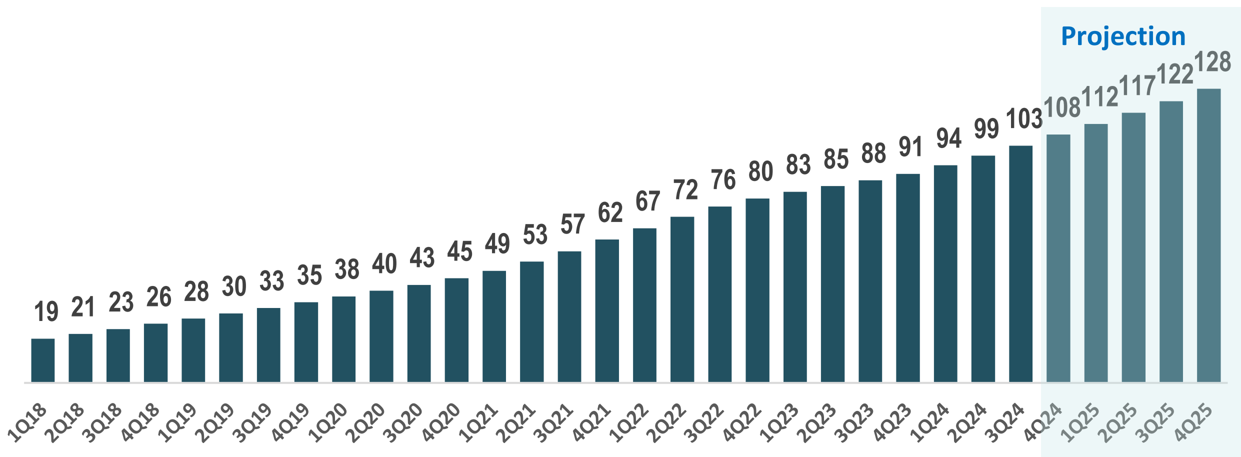


Source: Amazon and SFA

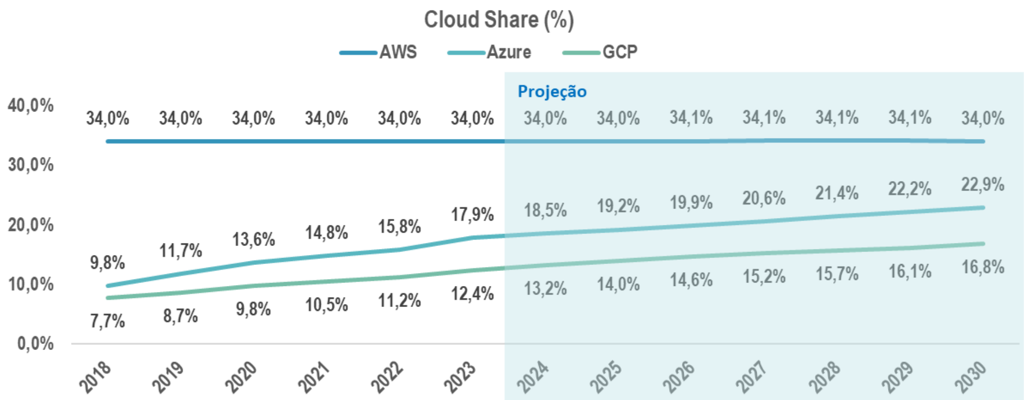
And this ends up being Amazon's playbook in e-commerce: Service level (delivery time) leads to an increase in conversion and sales, which in turn reduces unit cost and this leads to the expansion of the TAM, enabling a whole new market (and more SKUs). It is a self-reinforcing cycle with its own inertia.

Amazon Web Services: The Cloud Pioneer

Regarding revenue growth, let's talk a little about the Cloud market, where it is also the market leader. The graph below shows AWS' revenue per quarter (U$ B).

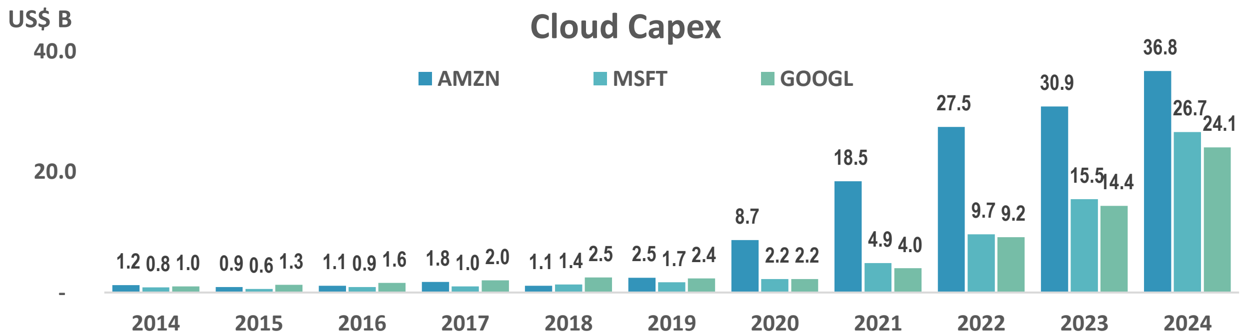


With revenues that have already surpassed US$100 billion in the last 12 months, AWS's growth rate in recent years is impressive. One very positive point is that, since the cloud sector is very capital intensive, this naturally tends to benefit those with more scale, as they have more capacity for reinvestment and data center acquisitions, as well as better dilution of depreciation and G&A, which are usually very high. Therefore, we are talking about a business with high fixed costs and whose scale tends to help. Today, we estimate that Amazon has almost twice the market share of Azure (Microsoft's, which does not disclose the numbers for its cloud business explicitly) and three times the market share of GCP (Google's cloud business). Therefore, scale is the first natural advantage for AWS. Additionally, we note that some consultancies estimate a market share for Azure that is larger than what we see, which, however, we refute based on some rumors and leaks about Azure's revenue level.



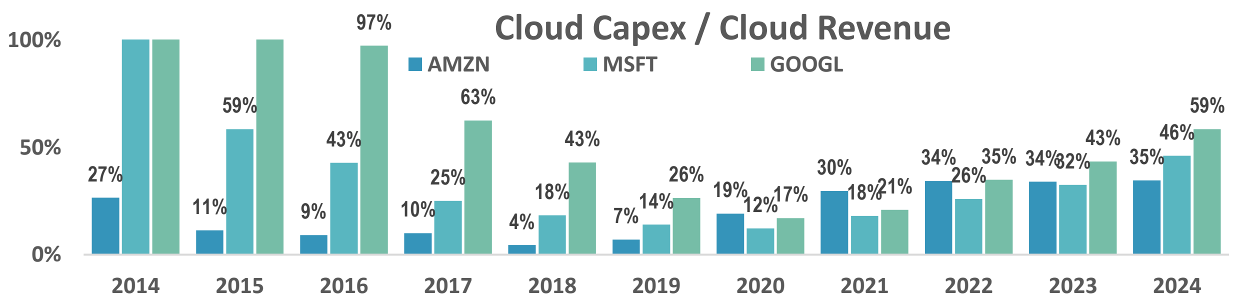
Source: SFA

At the same time, AWS has the highest capex, which helps with the bargaining power it has with its suppliers.



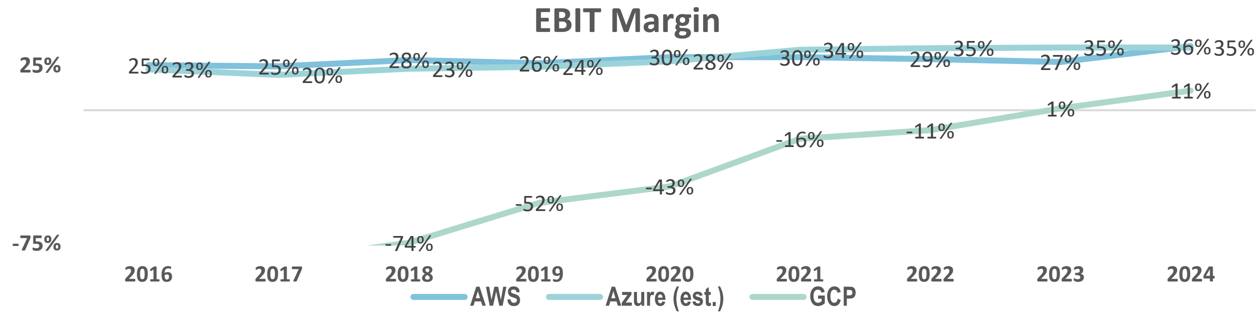
Source: SFA

Despite nominally higher capex, AWS is able to “dilute” these investments better, compared to the revenue level.



Source: SFA

Looking at profitability, we estimate that AWS has the best margins along with Azure and is well ahead of GCP.



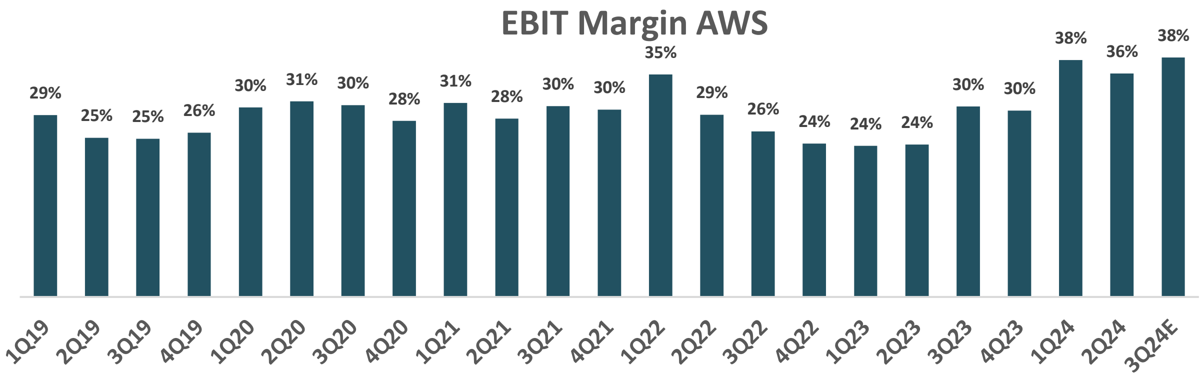
Qualitatively, Amazon has a greater amount of functionality, being the “Swiss army knife” of hyperscalers. Today, it is the easiest platform to plug and connect advanced and specific solutions. Having been the first cloud, it is natural that more people also master AWS technologies, making labor cheaper and more abundant.

When it comes to Artificial Intelligence (AI), AWS has been seen as behind the times and unresponsive. However, we should highlight its ASIC (application specific integrated circuit) chips Trainium and Inferentia, which give Amazon an interesting position in this technological race and also greater possibility of vertical integration.

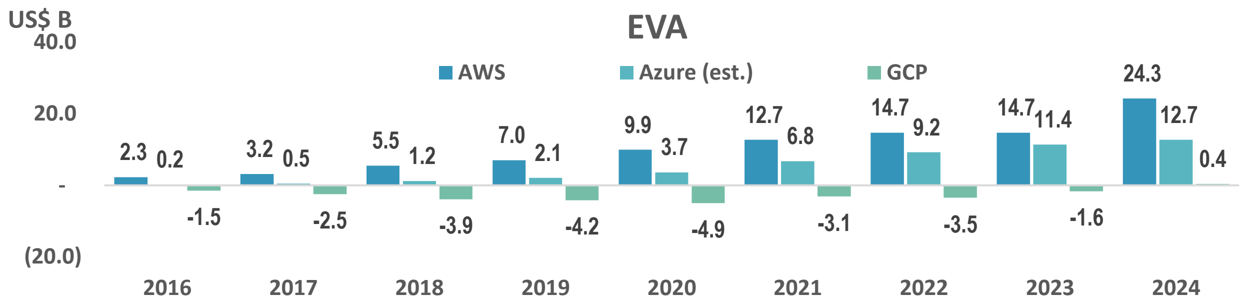
‘Trainium’ chip, developed by Amazon for AI.

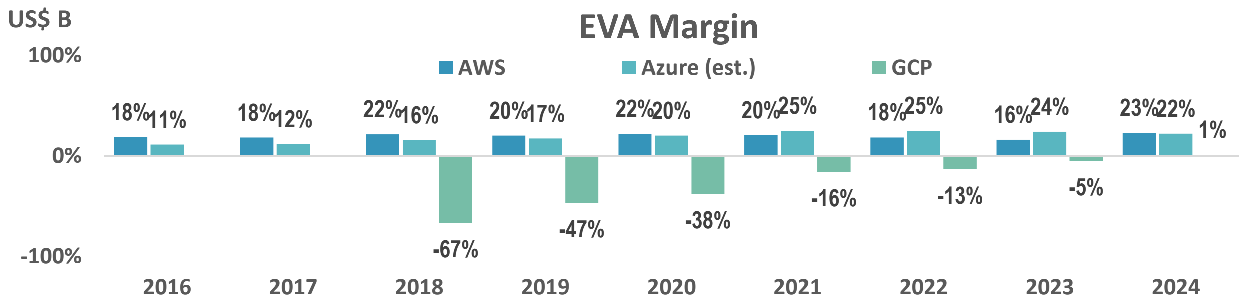
It is worth noting that Amazon's approach to AI so far has been to focus on IaaS (infrastructure as a service) and PaaS (Platform as a service). Historically, Amazon has had good returns by exploring infrastructure and platforms. Regarding IaaS, Amazon has high-end GPUs available and is working hard to increase the adoption of its own ASIC (application specific integrated circuit) boards. In platform, we can mention Sagemaker and Bedrock, which are Amazon's efforts to provide broad access to the end user to the various types and sizes of different models. It is an agnostic platform that aims to make it easier for the customer to navigate this world of complexity, with the difference in offering unique flexibility to projects.

Last but not least, we see AWS margins at all-time highs. This suggests that incremental ROIC has been positive. Therefore, as soon as invested capital is deployed, it already has an attractive return from an EBIT and NOPAT perspective. It has already been signaled by Meta and Microsoft, for example, that marginal investments in AI would bring a “weight” to short-term operating margins.



In short, AWS's leadership position in terms of scale and technology, its efforts in ASIC, agnostic approach (it does not necessarily need to win with the base LLM), positive incremental operating margin, and a good investment in Anthropic (one of the great AI and LLM startups) make us think that Amazon should surf well this lasting movement that will be the demand for AI, in addition to being positioned to continue being the leader in market share and value generation in this market for many years.





Advertising

Another revenue growth lever is Advertising. Amazon, with its network effect, aggregating supply and demand, took advantage of an opportunity that arose naturally: advertising. Initially, it offered services to increase visibility beyond the "banner", also known as display. The effectiveness of advertising was quickly noted, and this market has not stopped growing. Over the years, it has become a trend. The so-called "retail media" is nothing more than the retailer who uses its space to capitalize on advertising opportunities.

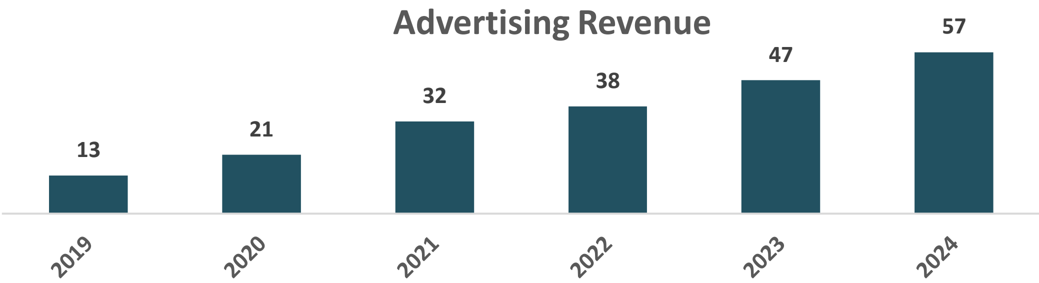
In an interview we conducted with the director of one of the largest media agencies in Brazil, we discussed the state of retail media in the country and its implications for brands in the coming years. Brazil currently has only 1% of the retail media market, while in the United States this number reaches 15%. The disparity is explained by the strength of the American market, especially the bargaining power of companies like Amazon, which has a great influence in the area of "Trade Marketing". This concept, which dates back to physical retail, involves positioning customers' products on the shelves at eye level, a prominent location that can significantly increase sales and strengthen the brand's branding over time.

The analogy is clear: just like in physical retail, those who do not invest in retail media in the next five years may face brand erosion. In the online environment, this erosion occurs more quickly and intensely, since consumers can easily compare products and prices. If a brand does not pay to highlight its product, the competition can quickly capture its market share, leading to the loss of brand power. A good example would be a brand like Duracell. If the company does not invest enough in retail media, it can quickly lose market share and its consolidated position in the consumer's imagination (brand power).

In this and other interviews, it was clear that retail media is a path of no return. Large companies have not yet reorganized themselves to allocate resources strategically in this area. Today, the media budget is usually divided between the traditional "bucket", which includes offline channels, and the "online bucket", which is mostly made up of Google and Meta. However, the big challenge is to integrate retail media into this structure and start investing robustly and focus on this new trend.

In short, the retail media market represents a significant change in companies' marketing and branding strategies. Ignoring this movement, especially in a country like Brazil, where digital is increasingly gaining relevance, can result in serious consequences for brands in the coming years. As a result, Amazon has grown more in advertising in recent years than other big techs and has also reached a very significant scale. In addition, growth expectations for the coming years are also greater.

	4Q20 Revenue	3Q24 Revenue	CAGR
YouTube Ads	$6.9 billion	$9.2 billion	10%
Amazon Ads	$7.4 billion	$15 billion	26%
Meta Ads	$27 billion	$39 billion	12%
Google Search	$32 billion	$48 billion	15%

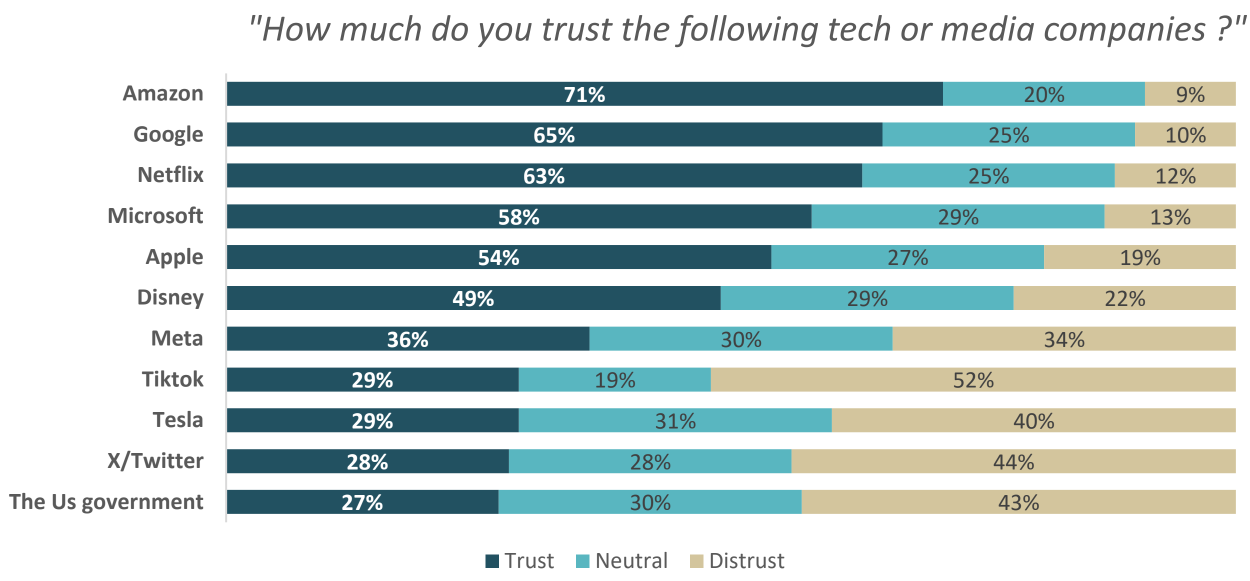


Additionally, Amazon earns revenue from advertising through its Prime plans. In a broader industry trend toward increasing average revenue per user, Netflix and other streaming networks are prioritizing cheaper plans that display ads, and reserve ad-free plans only for those willing to shell out a larger portion. As such, Prime Video has also been an important advertising driver and should continue to grow above market rates in the coming years.

Amazon Expected to Continue Growing Despite Asian Competition

Regarding Amazon's future growth in the US, there is some doubt in the market regarding the possible threat that some Asian players may pose. Among the competitors that we have been constantly evaluating are Temu, Shein and Alibaba, Asian giants that have been very successful globally in capturing market share mainly due to the strategy of working with lower average prices and with greater vertical integration and proximity to the distributor, thus reducing the costs involved as much as possible.

The main argument here is around Amazon's Moats. Since Amazon has reached a larger scale, it can have a wider, faster and more efficient logistics network (cost/delivery). This allows it to defend itself in what represents the majority of sales: delivery in a few business days. In addition, the brand and people's trust in Amazon, means that customers, due to long-standing relationships and even custom, simply prefer to use Amazon for most of their purchases. Below is an indication of people's level of trust in the brand.



Source: allaboutcookies: "Based on a survey of 1000 US adults"

Therefore, we believe it is difficult for these players to migrate to a higher ticket price, based mainly on Amazon's superior logistics, in addition to strong relationships and trust with customers, which is crucial for purchasing more expensive items. Regarding market share, we also understand that these platforms have "expanded" the market, taking market share predominantly from physical retail, without stealing as many sales as possible from Amazon, which generally has a different proposition. The question that remains is regarding lower ticket items.

In the lower ticket segment, we recognize the value and innovation of Asian players who have created a "new" market using a lot of data and algorithms directly linked to the supplier, with greater vertical integration and a faster response to customer demands. Even so, Amazon, with its innovative culture, recently announced a response to low-ticket marketplaces, announcing that it will soon launch its own low-cost platform. The launch is expected by the end of 2024, with the aim of directly competing with Chinese e-commerce giants such as Shein and Temu. The new platform will offer a wide range of products, including fashion, homeware and lifestyle items, all at competitive prices, to appeal to budget-conscious consumers.

To support this initiative, Amazon is leveraging its extensive logistics network and introducing new fulfillment methods. The company is allowing Chinese sellers to ship products directly to Amazon's warehouses in China, from where orders will be airlifted to the US in 9-11 days. This approach helps avoid expensive inventory fees and allows Amazon to offer lower prices while maintaining faster delivery times compared to Temu and Shein. Additionally, Amazon has also set a price range that it intends to work within. For some categories, it has set a price ceiling for items that can be listed. Initial rumors point to a price cap of $8 for jewelry, $9 for bedding sets, $13 for guitars, and $20 for sofas, which seemed really competitive to us.

Overall, we believe Amazon has the scale, logistics, capital and culture of innovation needed to compete and succeed against these new platforms and could potentially even be a new avenue for value creation.

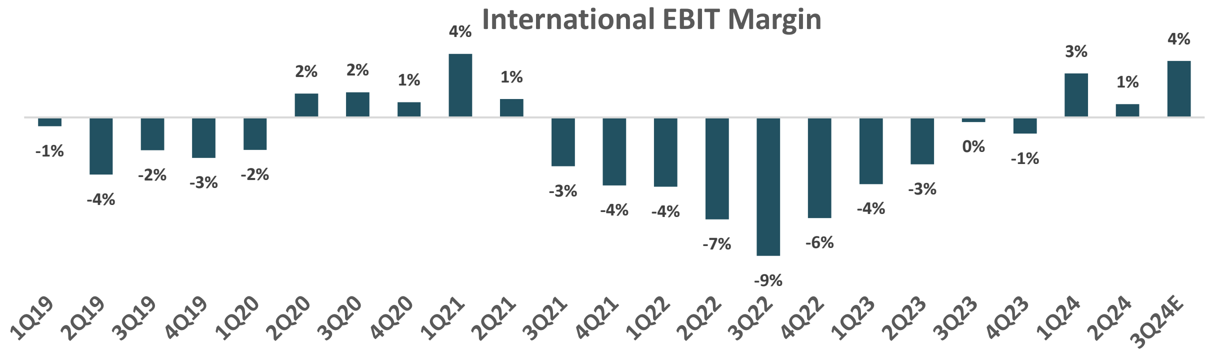
International

Amazon has distinguished itself over the years by successfully entering and succeeding in many international markets, notably in Europe. We have observed considerable capital discipline and an execution strategy that aims to replicate Amazon's success in the US in other countries. This strategy involves improving delivery speed, expanding assortment, gaining scale, and further building loyalty with the Prime plan. Today, Amazon is already a leader and is able to generate value in many of the countries in which it operates, illustrating its good capital allocation that has borne fruit over the years. However, there has recently been some criticism regarding Amazon's reported operating results in the "international" segment.

The reason is that some countries, due to a natural issue of scale and maturity, do not yet have positive operating margins or, until very recently, have not had positive operating margins. Although Amazon does not explicitly disclose this, most countries have a positive and healthy profitability trajectory, with the issue of maturity being the main difference. Therefore, part of our thesis is that the international operation is quite valuable and, despite some quarters with discouraging numbers in the past, we see good potential for this part of the business over a 5-year horizon. Our conviction is basically based on the maturation of many of the countries where Amazon began operating more recently, in addition to exemplary execution in some European countries where the operating result is already positive. See below the list of countries where Amazon has operations.

Country	Start Year
United States	1995
Germany	1998
United Kingdom	1998
France	2000
Japan	2000
Canada	2002
Italy	2010
Spain	2011
Brazil	2012
India	2013
Mexico	2015
Australia	2017
Singapore	2017
Turkey	2018
United Arab Emirates	2019
Saudi Arabia	2020
Netherlands	2020
Sweden	2020
Poland	2021
Egypt	2021
South Africa	2024 (expected)

In fact, we see that there are 10 countries that have been operating for less than 10 years. And 5 that have been operating for less than 5 years. This, together with the fact that operations take years to mature, leads us to conclude that Amazon international as a whole is an operation that is still "maturing". Similar to stores, which only have a few years to perform at their full potential when they open, the countries where Amazon starts take years to reach breakeven. In the case of Brazil, speaking to former Amazon employees, we obtained information that the Brazilian operation reached breakeven in approximately 2022. In this case, it would be 10 years since the beginning of operations in the country (2012). We know that Amazon in Brazil has grown slowly, and this case does not reflect most of the countries in which the company operates. Therefore, we estimate that it will take between 5 and 8 years for a new country to contribute positively to the results.



Our view is positive for the long term of Amazon's international business, with good examples being the United Kingdom, Japan and Germany, countries whose results are as good as those of the United States, according to our research. International retail is another positive generation lever for Amazon, and having conviction in the long term, despite a not so encouraging short term (as was the case in 2022), allows us to make a time arbitrage when finding this opportunity.

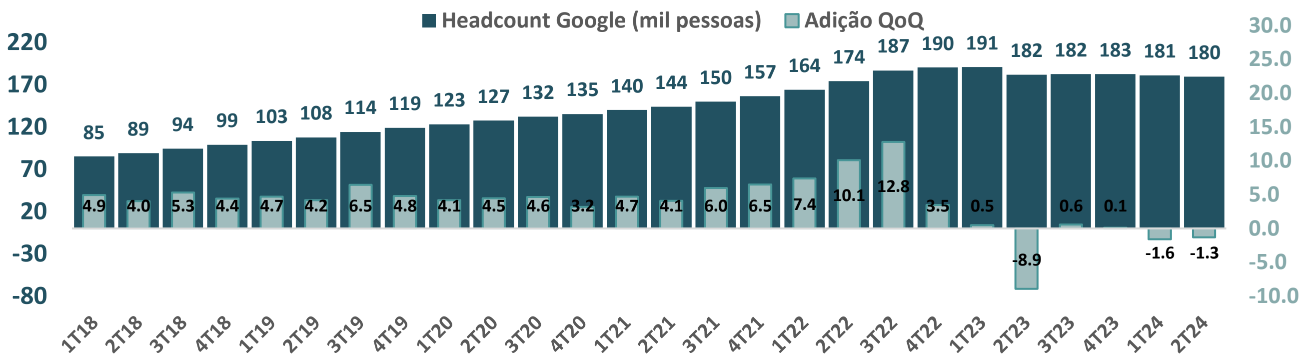
III. Cost Cutting Opportunities

Another important lever for value generation is cost cutting and efficiency improvements. Despite Amazon’s size and growth, we still see excellent opportunities to continue generating value through cost reduction. Below, we list some initiatives that we consider relevant when seeking to generate more value through cost cutting.

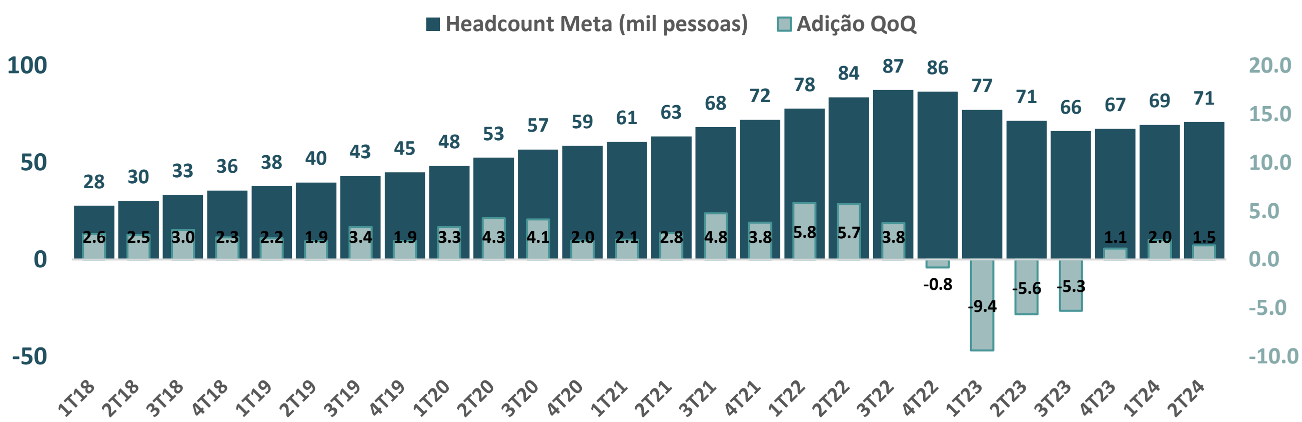
Efficiency and Headcount

The first point about cost reduction is related to headcount. Both retail and AWS have been through a phase of super growth over the last 10 years, and little has been done to “cut the fat.” Amazon has always had the potential to operate at higher margin levels, especially in recent years. Cost control and efficiency have been common themes in Big Tech after 2021. With this goal in mind, after decades of growth without looking back, we had a moment to digest processes, improve efficiency, and make specific cuts, in addition to taking capital out of areas that clearly had little chance of providing significant returns. After a cycle of more than 10 years of stepping on the accelerator, the (opportune) time has come to step on the brakes and straighten the course. As an example of this, we show below the headcount of some large companies.

Google headcount:

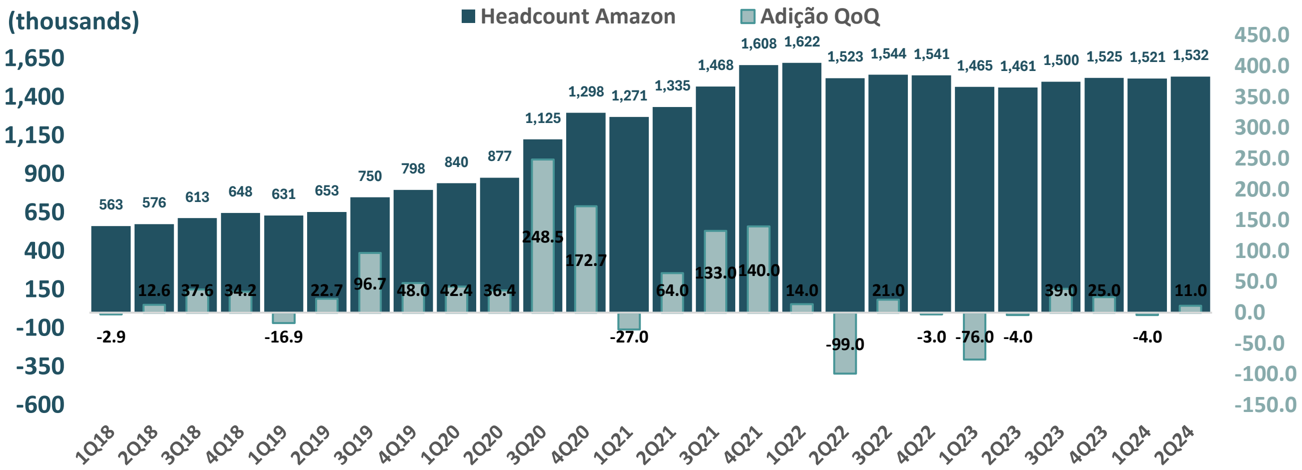


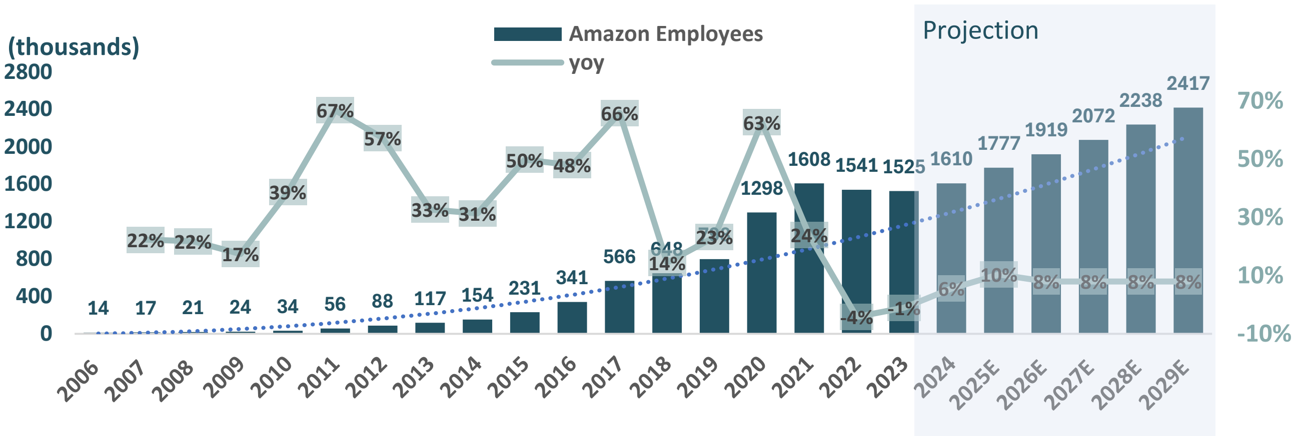
Meta headcount:



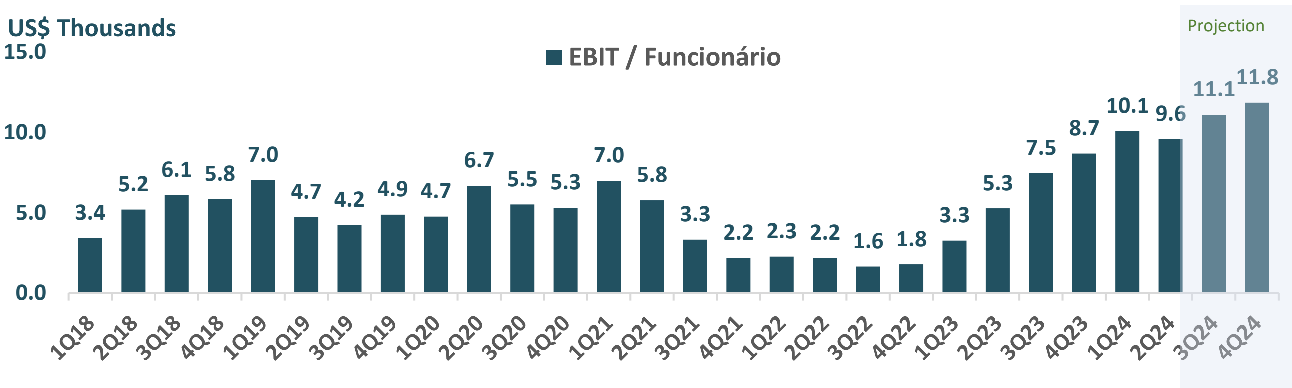
And it was no different with Amazon, both Blue Collar and White Collar. There was excessive growth in 2020 and 2021, and now Amazon, after two consecutive years of job cuts, is returning to its long-term trend (dotted line in the second graph below). Going forward, we project growth of 8% per year.

Amazon headcount:





And when we look at the EBIT/Employee ratio as an efficiency metric, we see that Amazon hit a 14-year high in 3Q24.



So Amazon is delivering more with fewer people. Many tech companies have managed to cut a lot of headcount without affecting their operations too much. In addition to those mentioned above, it is also worth mentioning Twitter, which laid off +70% of its workforce. Big Tech, at the core of its operations, needed far fewer people than it actually had.

And so, all the Tech companies trimmed some of the fat they had in the form of extra employees. Some Big Tech companies are known for having become a bit too bloated and bureaucratic, notably Google, where many engineers earned more than US$500,000 and did not have much responsibility for the company.

In short, one lever was simply cutting people. And we believe that this new level of EBIT per employee should be maintained or improved, either by deliberate efficiency targets or by robotics.

Logistics Efficiency

A second important point related to cost reduction is making logistics more efficient. In addition to the aforementioned gains in scale, the company continues to work internally to improve its efficiency in the most basic aspect: price per unit delivered. In other words, Amazon's classic “unit economics” still has room for improvement in the US, its largest market.

One initiative in this regard has been the geographic diversification of its facilities. In addition to traditional distribution centers, Amazon has focused its efforts on improving the efficiency of sorting centers, delivery stations, inbound transshipment centers, and air hubs. Additionally, more capital has been invested recently in smaller facilities than in the past. This allows for more efficient inventory management, faster order processing, and faster last-mile delivery. In recent earnings calls, the company has talked about potential additional gains in logistics efficiency.

Unifying Distribution Centers: “Our shift earlier this year from a single national fulfillment network to eight distinct regions across the U.S. represented one of the most significant changes to our fulfillment network in our history. This shift has gone more smoothly and had a greater impact than we had optimistically anticipated, and you can see the benefits in several ways. Regional fulfillment clusters with higher local inventory levels and optimized connections between fulfillment centers and delivery stations mean shorter distances and fewer steps to get items to customers. Shorter travel distances and fewer steps mean lower service costs. But perhaps most importantly, shorter distances and fewer steps mean customers are getting their packages faster. [...] We’re obviously pleased with the results, but we don’t think we’ve realized the full benefits yet — and we continue to make constant improvements to fine-tune our placement algorithms to enable even more fulfillment in the region and further consolidate into fewer shipments.”

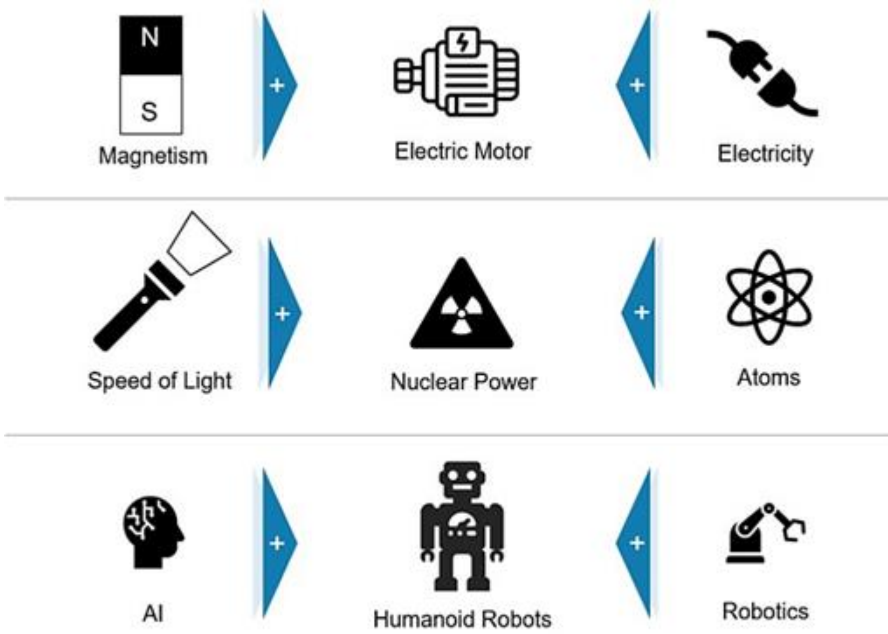
Inbound (inbound or collection of merchandise) as an area for improvement, and 2018 is not the peak of profitability: “And I mentioned one area in particular that you’ll see us focus on over the next year or two is that we just think there are real opportunities in our collection network and our collection processes and then where we position inventory in association with that. Which will optimize both of those tasks. But for us, I don’t think 2018 is North Star for cost to serve. We believe we can continue to evolve and be better than that.”

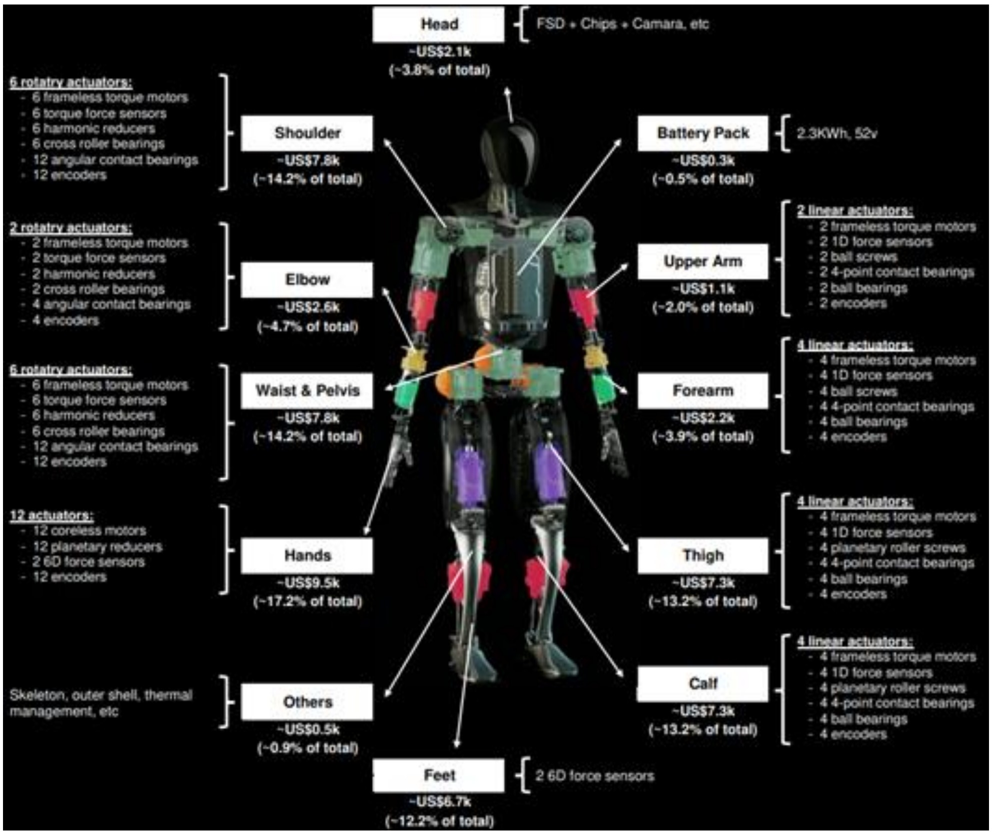
Advances in Robotics and Automation: “Amazon has launched its 12th generation fulfillment center, which incorporates new robotics technologies to streamline the processes of storing, picking, packing, and shipping products. This is expected to reduce fulfillment processing time by up to 25% and improve cost efficiency by 25% during peak periods in these facilities. Amazon’s significant investment in AI and robotics aims to speed delivery, reduce costs, and improve safety in its fulfillment networks. Amazon’s continued innovation in this area is part of a long-term strategy to improve operational efficiency and customer satisfaction.

Robotics

Finally, and one we consider optionality, an important cost reduction theme is robotics. Robotics is a long-term secular theme and has emerged as the fastest-growing category in recent months, according to studies of open-source databases. Private markets are already pricing in the opportunity. Pure-play companies like Figure are already worth $2.6 billion. However, public markets have not yet priced in the optionality of this theme.

A basic idea is that advances in AI and parallel computing will be an “enabler” of robotics. In analogy, magnetism and electricity were the enablers of electric motors. Furthermore, the estimated cost for a humanoid robot is approximately US$60,000 in the future.





Source: Morgan Stanley Research

Although TAM is difficult to determine, Amazon is one of the big beneficiaries, given its high exposure to automation and the size of its operation.

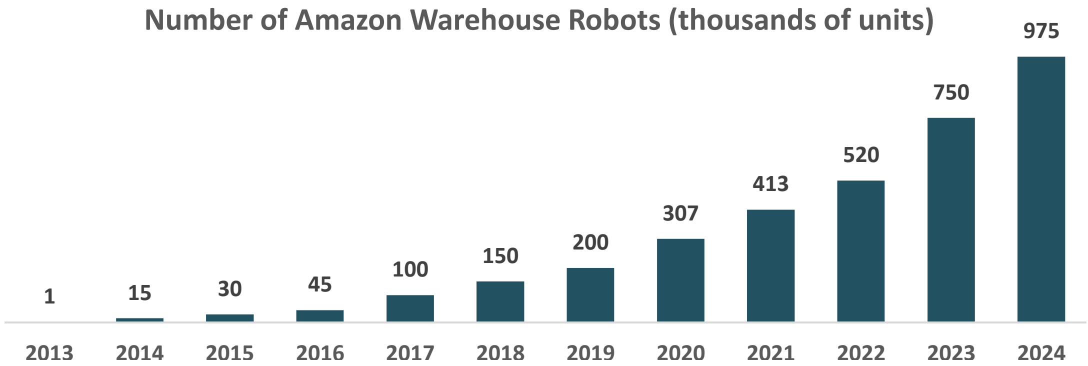
Source: Morgan Stanley Research

We believe that, as the technologies involved mature, robotics should be a growing topic in the coming years, just as cryptocurrencies and AI have been in recent years. Some estimates suggest that the humanoid robot market could be worth as much as $3 trillion in “attainable wage equivalents” by 2050. We don’t have a precise estimate of how big this market will be in the long term, but by investing in Amazon, we are also buying into this optionality.

Amazon is proficient in robotics and is investing heavily in R&D on several fronts. The number of employees underscores the size of the opportunity the company can capture. As a result of these robotics efforts, Amazon acquired Kiva Systems in 2012 and renamed it Amazon Robotics. Kiva’s mobile robots move shelves of products to human workers for picking and packing.

Source: [Introducing the Full Amazon Robot Line Up | Amazon News]

Amazon already has 750,000 Hercules robots in operation, with the first deployment over 10 years ago.



Source: Amazon and SFA

The company is also working on “robotic arms,” which are used to pick and pack individual items, working alongside human employees. In 2022, one-eighth of all orders delivered worldwide (1 billion packages) were handled by **Robin** (pictured below), one of Amazon’s robotic handling systems.

Sequoia is a new integrated robotic system that simplifies and optimizes storage and picking of goods.

Digit is a new bipedal robot developed in partnership with Agility Robotics for tasks such as box positioning.

Amazon is working on integrating robotic systems into existing facilities without drastically altering the human work environment, allowing robots and humans to work side by side. Robotics has great potential to be a "next thing" (after crypto, electric vehicles, metaverse, and AI) in the coming years. And Amazon is one of the clear beneficiaries, simply because of the potential for automating its current operations. Even if Amazon is not the leading innovator, simply employing technologies developed by others should positively impact its operations.

Conclusion

Amazon has an enviable financial track record built on a solid foundation of efficient capital allocation and a relentless pursuit of new growth opportunities. The company stands out not only for its ability to allocate capital wisely, but also for its innovative and customer-focused culture. This culture, which permeates all levels of the organization, is a key driver of Amazon's success. It enables the company to identify and exploit new market opportunities, such as streaming and online retail, while also investing in cutting-edge technologies such as artificial intelligence and robotics. Andy Jassy, Jeff Bezos' successor, has demonstrated great skill in managing the company, maintaining a strong culture and financial discipline, while driving efficiency and innovation.

Furthermore, Amazon has an impressive ability to control costs and improve efficiency in its operations. This is evident in its initiatives to optimize its logistics, reduce headcount, and invest in automation. These measures ensure that Amazon remains competitive and generates value, even in challenging markets.

Amazon is also aware of market trends and is quick to adapt to changes. This is evident in its response to Asian competition, with the launch of a low-cost platform (Haul) to compete with companies such as Shein and Temu. The company is also expanding its business internationally, replicating its successful model in new countries and consolidating its position as a global leader in e-commerce.

We believe Amazon offers a unique combination of proven track record, strong culture, competent leadership, adaptability, and operational excellence. These factors, combined with an attractive long-term valuation, make Amazon a solid investment with significant potential to create value for its shareholders.

Thank you for your trust,

SFA Investmentos Team

Management
SFA INVESTIMENTOS LTDA
Rua Gomes de Carvalho, 768 – 8º andar
Vila Olímpia – CEP: 04547-003
São Paulo - Brasil
Tel: +55 11 2780-0690
ri@sfainvestimentos.com.br

Administration
BTG Pactual Serviços Financeiros S.A. DTVM.
Praia de Botafogo, nº 501, 5º andar (parte), Torre Corcovado, Botafogo, CEP 22250-040
Tel: +55 0800 772 2827
www.btgpactual.com