

FUND REPORT

IP-EQUITY HEDGE BRAZIL

FOURTH QUARTER / 2005



INVESTIDOR
PROFISSIONAL
DESDE 1988

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INDEX

Introduction	2
IP-Equity Hedge Brazil	3
Introduction	3
Main positive contributions in 2005	4
Main negative contribution in 2005	5
Outlook	6
Informations	7
Miscellaneous	8

INTRODUCTION

The Brazilian stock market recorded very strong appreciation in the last three years. In contrast with the last few bull cycles, this one very likely represents a secular movement and no longer a cyclical rise. The recent rise was not solely and exclusively the result of another global liquidity phenomenon irrigating peripheral countries with doubtful fundamentals and high returns. This rise is based on an unprecedented improvement in Brazil's financial fundamentals, in Brazilian companies and in the capital market.

We are moving rapidly towards the previously unimaginable level of an investment grade country. The environment for investors has improved noticeably, thanks to more market-friendly legislation (the new Corporate Law), and especially the success of self-regulation (Bovespa's "New Market"). The last two years will be remembered in the future as the beginning of true capitalism in Brazil, in which a significant portion of new investments in the economy is funded by the capital market, which is even on the brink of surpassing its old rival, the BNDÉS.

The beginning of true capitalism in Brazil is taking place – and it could hardly be otherwise - at a time when the degree to which the Brazilian stock market represents the economy (by the number of companies and diversity of sectors) is extremely low in relation to the GDP. Phase 1 of true capitalism in Brazil, which may last for a few more months or years, will be marked by a great imbalance between the supply and demand for good assets. We have, therefore, a clear scenario for the appearance of speculative bubbles in this class of assets: shares of companies with the proper "presentation". This is what we are experiencing at present, and in the base scenario we will continue to do so in the next few months and years.

If this scenario indeed materializes, the funds managed by IP will be exceptionally well positioned.

OPPORTUNITY

The situation depicted above has given rise to a peculiar phenomenon: for companies with the proper "presentation", the stock market is paying more than any other class of investors (strategic investors, private equities, etc.).

The great appreciation potential for the next 3 years is in the PIPE (Private Investments in Public Equities) category, whose rationale was described in the Fund Report for the third quarter of 2004. The standard deviation of the valuation of companies traded at the Bovespa is at a very high level. While the companies in fashion (especially IPO companies and some retailers) trade at EV/EBITDA multiples of around 12 to 15 times for 2006, other companies, just as well managed as these and in some cases also with greater expected cash-flow growth, are being traded at EV/EBITDA multiples of less than 4x for 2006.

The great opportunity for the next few years, therefore, will be the "re-launching" in the market of Small Caps whose quality is still unknown to most investors, thus achieving significant increases in these companies' multiples.

Potential effect of re-rating of our portfolios' PIPEs

	EV/EBITDA (Current)*	EV/EBITDA (Target)**	Upside
Coteminas	3.3	5.0	53%
Globex	4.7	9.0	117%
Panvel	3.2	9.0	150%
Marcopolo	4.3	7.0	91%
Distribuidora Ipiranga	3.2	5.0	58%

* Base: 30/12/2005

** Average of comparable peers

At present, PIPEs represent about 50% of the IP-Value Brazil Classes portfolio. The combined potential of these investments is huge. The focus of IP management team in 2006 will be on releasing the hidden value of the PIPEs in our portfolios, generating liquidity for these shares and originating new investments within this category, which will continue to represent a significant part of our funds in the coming years.

IP-EQUITY HEDGE BRAZIL

IP-Equity Hedge Brazil recorded an appreciation of 0.36% in the month of December. In the year 2005, this Class has accumulated an appreciation of 9.85%. Since its inception on December 29, 2003, the IP-Equity Hedge Brazil has accumulated an appreciation of 12.54%.

INTRODUCTION

Having concluded another year in the management of the IP Equity Hedge, it is necessary to assess the yearly results.

2005 was especially important because it offers a good proxy of what the investor should expect from the IP Equity Hedge, not only with regard to strategy and target operations, but also in relation to the pattern of the Fund's returns.

As we wrote in the Fund's placement report (3rd Quarter of 2003),

"The fundamental analysis methodology, developed and perfected by IP over the last 15 years, will be used as the main tool to identify significant distortions between the trading price and the intrinsic value of assets. The Fund will maintain long positions when it identifies assets undervalued by the market and short positions when it identifies assets overvalued by the market, always in comparison with the intrinsic value estimated by IP.

In addition, the Fund will seek arbitrage opportunities between assets issued by one and the same company or group of companies."

Of course, this is a simplification of the management philosophy, which includes other elements such as the pre-identification of catalysts (especially in short positions) and risk management, among others, but it is unquestionably the "backbone" not only of the Fund's management, but also that of Investidor Profissional.

The year 2005 was marked by two distinct phases with regard to the results earned. In the first phase (January to April), there was an increase in the distortions observed previously, which naturally had a negative effect on the Fund's short-term performance. The positive counterpart

to this event was the creation of a very favorable situation with regard to the portfolio's upside potential, not only because of the increase in distortions, but also because of increased positions (given that the fundamentals remained unchanged). This situation, as might be expected, favored the future results in a second phase (May to December), which was when we reaped the gains relating to the positions built up in the course of the first quarter. As may be observed, precisely the same positions that contributed negatively during the first phase offered much more significant gains in the second phase (see table below).

Performance per asset in the period:

	Jan 05 to Apr 05	May 05 to Dec 05	Year 2005
BBAS12 (includes BBAS12/BBAS3)	- 0.3%	6.0%	5.7%
B RTP3	- 0.3%	2.5%	2.5%
CTNM4	- 0.7%	2.1%	1.0%
Total Contribution from Operations	- 1.3%	10.6%	9.2%
IP Equity Hedge Brazil Performance	- 0.3%	10.2%	9.9%
Libor 1 month in the Period	0.9%	2.5%	3.4%

The effect of the contributions described above may be seen more clearly when the Fund's monthly results are observed.

This pattern of results reflects the philosophy that gives priority to "IF" over "WHEN". The questions we always ask are the following: "IF" the distortion between the price and the fair value is significant, "IF" the company has a solid competitive position, "IF" there is strong alignment between the controlling shareholders and minority shareholders, "IF" the company allocates capital efficiently, "IF" a company's specific result is due to structural factors or the current situation, "IF" the likely rupture is in our favor, "IF" there are potential catalysts that would favor a

price correction, "IF" the company is at a favorable point in the investment cycle.

Although we understand the appeal of aiming at "WHEN", this question is not the focus of the Fund's management. "WHEN" the price of commodities will change trends, "WHEN" the sector will be in fashion, "WHEN" the market will realize the company's qualities – these are questions that are most definitely outside Investidor Profissional's area of competence and where we do not believe that we have a clear competitive advantage in relation to the market. Thus the focus on "IF" is explained.

MAIN POSITIVE CONTRIBUTIONS IN 2005:

1. Two operations involving Banco do Brasil warrants (long position in BBAS12 and arbitrage BBAS12/BBAS3)

After recording a positive result in the year 2004, the operations involving Banco do Brasil warrants earned significant gains once more. The objective of this operation was to take advantage of the incorrect pricing of a relatively illiquid asset, trading at a significant discount to its fair value.

The Banco do Brasil warrants originate from a capital increase effected in 1996. In order to encourage shareholders to participate in the capital increase, warrants were issued free to those taking part in the deal. This "incentive" produced a huge limitation on the subsequent appreciation of the stock, because the warrants represented a constant threat of significant dilution at low prices.

In August 2004, Banco do Brasil finally did away with this "obstacle" to the appreciation of its shares. A tender offer was made for the warrants in circulation in the market, and a capital increase was carried out. The tender offer was successful and took about 92% of the total outstanding warrants off the market.

It was at that time that our trades involving Banco do Brasil warrants were put together. An excerpt from the Fund Report for the third quarter of 2004

highlights the attractiveness of the asset in relation to the prices prevailing at the time:

"Each warrant gives its holder the right to purchase 1.04 shares of Banco do Brasil in 2006 (BBAS12) and 2011 (BBAS13) for a price equivalent to R\$ 20.79 per share, restated by the IGP-DI inflation index. At present, Banco do Brasil is trading at the Stock Exchange at R\$ 25.20 per share, and even after the recent appreciation, its warrants are acquired at prices below their intrinsic values. The warrants closed the quarter (third Quarter of 2004) quoted at R\$ 4.00 (BBAS12) and R\$ 4.16 (BBAS13).

This distortion was the reason for putting together two trades for the Fund: 1) A synthetic put option: short in Banco do Brasil shares and long in warrants; 2) long in warrants ... The purchase of this asset is one of the best opportunities to capture a possible appreciation of the Brazilian stock market."

As the maturity date for subscription under the warrants approaches (April 06), the distortion between the price of the warrants and the stock price is declining. This reduction in the distortion, as well as the appreciation of Banco do Brasil, has been favoring the trades.

2. Long position in common shares of Brasil Telecom Holding (BRTP3)

The aim of this operation was to take advantage of an asymmetry in perceptions regarding the probability of a tag along in the case of a change in the control of Brasil Telecom. Given that we consider that the chance of a tag along taking place is much higher than the chance priced in to the common shares of Brasil Telecom Participações by the market, we put together a long position in the asset.

CVM's decision regarding the operation involving the Pão de Açúcar Group and the French group Casino, detailed in the Fund Report for the third Quarter of 2005, increased the probability of a tag along in a possible change of control at Brasil Telecom. Some excerpts from the report are quoted below:

"A few weeks ago, in an event of great significance,

the CVM's technical area took the position that a tag-along tender offer for minority shareholders holding Pão de Açúcar (CBD) common shares must be effected, in the complex operation between this company and the French group Casino.

Although what is written in the "Association Agreement" is that the objective is to continue the sharing of control at CBD, the CVM interpreted it differently and stressed the following, among other things:

"... one concludes that the simple fact that a certain shareholder signs an agreement with the controlling shareholder does not automatically grant the former the status of a controlling shareholder, since this type of agreement may only aim at establishing protection mechanisms for the minority shareholder's interests related merely to the assets of same; it is then far from being an effective discipline for sharing the power of control, which remains in the hands of the controlling shareholder."

Despite the insignificant practical impact for Pão de Açúcar's shareholders, considering that the free float of common shares is lower than 1%, we think that the position taken by the CVM was of great value, because it makes the view of the regulatory body clear on the subject.

This decision strengthened our view that in the case of an intra-block concentration of control, when a shareholder that has signed a shareholder agreement leaves the position of minority shareholder to assume the majority of the controlling block, a sale of control is then characterized and a tender offer should be compulsory – even if the agreement in question contains clauses giving veto powers, the right to nominate directors, preference in acquiring shares, etc.

Legal technicalities aside, we base our understanding on the fact that this shareholder will have (individually) the votes necessary to elect the majority of managers, and thus decide on the company's orientation.

Another excerpt from the report for the third Quarter of 2005:

"The most visible example of this situation is the "Brasil Telecom" case, where a possible acquisition of the stock of the controlling shareholders – Pension Funds and Citibank – by Telecom Italia has given rise to doubts and confusion among qualified lawyers and investors.

Careful reading of the various corporate documents of the complex shareholder chain, especially the recent shareholder agreement of Zain Participações S.A, dated March 9, 2005, reinforced our view that the control of Brasil Telecom is exercised by Zain, which in its turn is exclusively controlled by the Pension Funds and Citibank, as may be seen right at the beginning of the agreement:

"...WHEREAS the Company, in its turn, holds the direct and indirect shareholder control of various corporations, including the corporations listed in the Exhibit hereto (jointly referred to as "Companies Receiving Investments", including any corporations in which the Company holds, at any time, direct or indirect shareholder participation, except however Argolis Participações S.A. ("Argolis") and any corporations in which the Company holds shareholder participations exclusively through Argolis)."

That said, in our opinion, if Telecom Italia, as speculated, acquires the participations of the Funds and Citibank, there will be a sale of control. At this time, the probability that we attribute to the occurrence of a tag along is high - and, even more important for our investment, much higher than that being priced in by the market to the common shares of Brasil Telecom Holding (BRTP3)."

After significant profit-taking, the long position in Brasil Telecom Holding common shares was increased once again.

MAIN NEGATIVE CONTRIBUTION IN 2005

1. Short position in shares of two companies recently floated in IPOs

The aim of this operation was to take advantage of the valuation gap between companies whose shares had been recently distributed in initial public offerings (IPOs) and the other companies in the market.

The identification of this distortion was described in the management report for the Fourth Quarter of 2004 (see excerpt below):

"While the market value of IPO companies incorporates a scenario of very high and profitable growth, in addition to minimizing several significant risks, other quality companies in the market are trading considerably below their conservative fair value, in a scenario in which their growth potential is not priced in."

Several factors influenced this distortion, among which the following may be highlighted:

- Intense marketing efforts by the placement agents.
- High level of corporate governance – which is not exclusive to IPO companies.
- Very aggressive growth estimates on the part of some companies and placement agents.

We believe that this large distortion is not fundamentally justifiable and that it tends to be corrected in the course of time as:

- The priced-in growth gap between IPO companies and the other companies in the market does not materialize.
- Significant risks of IPO companies, which are minimized today due to their brief history, do materialize.

In view of this, we put together a short position in a basket of IPO companies, containing the companies with the greatest distortion between their price and fair value.

This operation has been having a negative impact on the Fund's results, since the companies in question continue presenting strong results without showing the risks we perceive. The good operating performance of these companies has resulted in their shares appreciating strongly, expanding even further the valuation gap between the recently floated companies and the other companies in the market.

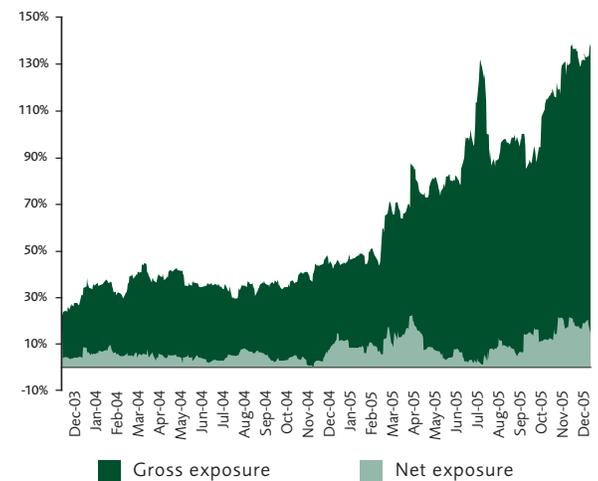
We are convinced that this distortion is due to the current situation rather than being structural, and it should be

corrected as the companies' fundamentals are better understood. We continue holding a short position in certain assets that have recently been floated in IPOs.

OUTLOOK

When we talk about the Fund's outlook, it is necessary to mention its equity exposure. As can be seen in the chart below, the Fund's exposure is at the highest level since inception. This movement is explained by a growing number of distortions presented by the market.

Gross Exposure



The main recent additions were concentrated in: (1) Two new arbitrage operations, positioned in favor of the likely rupture (long in common shares and short in preferred shares) in companies that present unstable control structures and high discounts in the common shares in relation to the preferred shares; (2) Two new pair trades in the pulp & paper and steel sectors.

IP-EQUITY HEDGE BRAZIL X LIBOR 1-MONTH



Performance (US\$)	IP-Equity Hedge Brazil	Libor 1-month
December	0.36%	0.35%
November 05	0.66%	0.34%
October 05	0.33%	0.33%
September 05	3.77%	0.31%
August 05	1.41%	0.32%
July 05	-1.75%	0.27%
June 05	1.94%	0.26%
May 05	3.17%	0.27%
April 05	0.55%	0.23%
March 05	-1.69%	0.24%
February 05	0.92%	0.20%
January 05	-0.10%	0.21%
2005 (YTD)	9.85%	3.38%
2004	2.42%	1.49%
12 months	9.85%	3.38%
Since inception (1)	12.54%	4.92%

(1) 2003, Dec 29

STRUCTURE

IP-Equity Hedge Brazil is a class of the IP Investment Fund, Ltd., an open-ended investment fund organized as a limited liability exempted company, incorporated under the provisions of the Companies Law (2001 revision) of the Cayman Islands.

Investment Manager: Investidor Profissional Gestão de Recursos Ltda.

Net Asset Value Calculator and Brazilian Custodian: Banco Itaú S.A.

Bank: UBS AG, Stamford Branch, CT (USA)

Registrar and Transfer Agent: UBS Fund Services (Cayman) Ltd.

Auditor: Deloitte & Touche

Inception Date: 29/12/2003

INVESTMENT OBJECTIVE

The Fund's objective is to provide sophisticated investors returns above the one-month Libor in periods of one year through operations in the Brazilian equity market, while limiting the Brazilian currency and government default risk, by investing most of the principal in U.S. Treasury Bills and USD money market funds. The Fund expects to maintain little or no correlation to main equity indices.

INVESTMENT STRATEGY

The investment strategy is to seek distortions between the trading price and intrinsic value of the Brazilian equity assets. In order to identify those distortions, the main tool used will be the value-oriented, bottom-up analysis.

The Fund will hold long positions when it identifies assets that are undervalued by the market and short positions when it identifies assets that are over-valued by the market, always in comparison with the intrinsic value estimated by Investidor Profissional.

In addition, the Fund will seek arbitrage opportunities between assets issued by a company or group of companies.

The Fund will also invest opportunistically in shares of companies involved in corporate events, including, without limitation, changes in the shareholder control, mergers, spin-offs and absorptions.

TERMS AND CONDITIONS

Subscription: Daily, in the first business day immediately following receipt of cleared funds and the Subscription Agreement.

Minimum Initial: US\$ 100,000

Minimum Additional: US\$ 50,000

Redemption: The Redemption Day for the IP Equity Hedge Brazil Class Shares shall be:

If the original Redemption Form duly completed and signed is received by the Registrar and Transfer Agent on or before the 10th day of each calendar month (or the preceding Business Day, if eventually this day is not a Business Day) the Redemption Day will be the last Business Day of such calendar month.

OR

If the original Redemption Form duly completed and signed is received by the Registrar and Transfer Agent after the 10th day of each calendar month, the Redemption Day will be the last Business Day of the calendar month immediately following such calendar month.

Payment of redemption proceeds shall generally be made within 5 Business Days following the Redemption Day

Minimum Redemption: US\$ 50,000

Minimum Balance Left: US\$ 100,000

FEES

Management Fee: 2% per year of the Net Asset Value per Share, accrued daily and paid monthly.

Performance Fee: 20% above the one-month Libor, accrued daily and paid monthly or in the redemption, subject to a high water mark.

ADDITIONAL INFORMATION

For additional information regarding the management of IP-Equity Hedge Brazil, please contact us by phone at (55 21) 2104-0506 or by e-mail at contactus@investidorprofissional.com

MISCELLANEOUS

A recent survey of institutional investors by consulting firm Watson Wyatt Worldwide found that 90% characterized corporate executives as "dramatically overpaid," while 85% said current pay models have hurt corporate America's image.

Value Investor Insight Dec 2005

The keys to perpetuating success? "We have a process and discipline that's well defined and has been in place for a long time," says Langerman. "It's what attracts people to come here in the first place – if you like this kind of investing and you're good at it, there's no better place to be." Adds Chief Investment Officer Michael Embler: "From a development standpoint, we've made sure that everyone involved in the investing process is an investor and an analyst. Everyone gets the benefit of very smart peoples' thinking – there's no pool of analysts who do all the work and then portfolio managers who are just picking ideas."

CEO Peter Langerman and Chief Investment Officer Michael Embler of Franklin Templeton's Mutual Series in Value Investor Insight Dec 2005

"Although all the attention Sears Holdings is receiving is, in some fashion, flattering, I would caution you to approach much of what is written and said about us with an appropriate amount of healthy skepticism. This is particularly so with respect to the loudest views, the most widely held views, or the so-called "expert" views. For many commentators, analysts, and reporters, their success is dependent on the excitement or controversy generated by their articles - not on the accuracy of their writing or of their predictions."

"As a long-term value investor, I am constantly on the lookout for situations in which the conventional wisdom of the commentators and "experts" is incomplete. There are many such examples, and those are the situations that produce real opportunities."

Chairman Edward Lampert of Sears



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