

## CEO AND BOARD OF DIRECTORS' MANAGEMENT REPORT ALMACENES ÉXITO S.A.

The year 2016 was marked by major challenges, transformations and decisive steps for the future of Grupo Éxito, which was consolidated as the leading food retailer in South America, operating in Colombia, Brazil, Uruguay and Argentina, through 1,576 stores representing nearly 2.8 million square meters of sales area and thanks to the cooperation of nearly 140,000 employees.

The region went through a year of social and political turmoil and a highly demanding macroeconomic context, which saw a step back in the economies of the four countries and a downturn of nearly 0.7% in the region's GDP<sup>1</sup>. The high levels of inflation had a relevant impact on the fixed costs of the retail industry, including salaries, leases and utilities.

Even in this challenging context, Grupo Éxito maintained its leading position on the markets in which it operates, showing the resilience of its operation and implementing important strategies to compete in an effective and profitable manner within a fluctuating environment.

Some of the milestones of the year that ended include:

- The successful capitalization through a equity investment of FIC in Viva Malls, which represents the leading real estate operator and developer company of shopping centers and malls in Colombia.
- The simplification of the corporate and operating structure in Brazil through the integration of Via Varejo and Cnova, and the decision to begin a divestment process of this non-food business to focus the activities on the food segment in Brazil in order to consolidate our leadership in South America.
- The debt reduction at the holding level, thus achieving an adjusted net financial debt/EBITDA ratio below the year's goal, thanks to the successful definition and implementation of a financial optimization strategy, including the Company's working capital initiatives.
- The continued good performance of the hypermarket formats in the four countries: Éxito in Colombia, Extra in Brazil, Géant in Uruguay and Libertad in Argentina.
- The profitable expansion of the proximity format through the brands Éxito Express and Carulla Express in Colombia, Minuto Pão de Açúcar in Brazil and Devoto Express in Uruguay.
- The consistent development of the dual retail - real estate model in Argentina, through the expansion of commercial spaces in the Libertad shopping malls, ending the year with nearly 160,000 square meters of leasable area.
- The uniform implementation of several successful business strategies and initiatives (1,2,3 / “Ahorrá” (Save), “Precio Insuperable” (Unbeatable Price), “Hiper Feria” (Hyper Fair)), that are adapted to the economic and market environment of each countries in which the Group is operating.

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<sup>1</sup> Source: IMF.

- In the progressive materialization of synergies, after just 15 months following the acquisitions in Brazil and Argentina, the implementation of new successful business models between the countries stands out, which are currently generating recurring benefits of USD 25 million in the four countries, in line with the goals that were initially set.

## COLOMBIA

The year 2016 was marked by high inflation and an increase in interest rates with a significant impact on the Company's financial and operating expenses.

Our operation in Colombia ended the year with 566 stores, achieving revenue for COP 11.4 trillion, growing 7.5%, driven by the results of the Éxito banner, which had a 7.4% increase in sales. The recurrent EBITDA grew 3.2%, reaching COP 833 billion, which represents a margin of 7.3%.

The sales strategies, such as “Precios Insuperables” (Unbeatable Prices), the “Quincenazo” (“Save all the month”) and the implementation of a new textile model focused on everyday low prices; enabled the Company to successfully face the growing competition and improve transit levels in our stores.

In this context, it is important to highlight the performance of the textile strategy, which has shown excellent results thanks to a disruptive model focused on the democratization of fashion, providing our customers with access to the latest fashion trends at low prices. As a result of this strategy, our volumes in units grew by more than 22%, reaching sales of around 51 million garments and growing by 18%.

Faithful to our Customer-Centric mission, we have focused on getting to know our clients' needs and working day after day on improving our service levels. In 2016. Our Company made substantial progress service according to Invamer Gallup, with a rating of 4.4 over 5. We are pleased with this result and it challenges us to continue ensuring the preference of our clients, which places us on the right path for the future.

In Colombia, commerce is going through a time of dynamic expansion, led by discount formats. In this context, the Company is moving forward in the development of new formats that will enable it to reach new institutional customers (restaurants, cafeterias and hotels) and offer the end consumer a new discount alternative, as well as strengthen its convenient close presence at attractive prices.

In developing this strategy, the first wholesale or Cash & Carry store was launched under the Surtimayorista brand, which showed excellent results, exceeding the initial budget. At the same time, the growth of Aliados (Allies) under the Surtimax and Super Inter brands increased, ending the year with 1,307 points of sale, and our own brand continued to strengthen as a value proposition for the consumer, with a share of nearly 14% and 43% of the sale of food and textile products, respectively. At Grupo Éxito, we favor dynamic, but

profitable expansion, ensuring an adequate return on investment and consolidating a great alternative of proximity for all audiences.

In turn, our omnichannel strategy, as the center of commercial development of our Company, has continued to show high performance. During this year, our e-commerce business *Éxito.com* and *Carulla.com* achieved positive EBITDA levels of nearly 5% and a sales growth of 23%, 16% of which is from marketplace sales, launched at the end of 2015, enabling other outstanding brands and companies can offer their products to the end consumer through our virtual platform.

The Group's revenue in Colombia received the positive contribution of its complementary businesses: financial (through the *Éxito Credit Card*, transfers and remittances), insurance, travel, mobile, direct sales and the exceptional development of the real estate business that opened more than 75 thousand meters of GLA during the year, including the shopping centers *Viva La Ceja* and *VIVA Barranquilla*, the sixth largest in the country and the most important on the Caribbean coast.

In the real estate business, it is important to mention the agreement reached in December with Fondo Inmobiliario Colombia (FIC), a private capital fund managed by Fiduciaria Bancolombia, through which we created *Viva Malls*, the vehicle controlled by Grupo *Éxito* that increased the value of our real estate assets, represented by 434 thousand square meters of GLA, including assets in operation and ongoing projects at COP 1.6 trillion. Through this long-term partnership, we expect to become the main developer and operator of shopping centers in Colombia.

In the financial retail segment, the *Éxito Credit Card* is now the leading card in Colombia, with more than 2.5 million plastic issued. The successful franchise partnership with MasterCard offers customers more options and benefits. Our insurance business has also grown and now covers more than one million customers through micro-insurance alternatives.

Furthermore, *Viajes Éxito* closed with a 16% growth in sales and more than 210,000 customers, making it the sector's second largest company based on tourism package sales in Colombia. The mobile telephony business reached more than 1,200,000 users through the "*Móvil Éxito*" brand.

Finally, as part of the Company's deleveraging strategy, it is important to mention the effort to optimize working capital in Colombia, with a historical inventory reduction of more than five days, along with the improved supply level of stores in recent years. Along with other operational excellence initiatives, this optimization helped reducing the holding's adjusted net financial debt / EBITDA ratio from 3.8x in 2015 to 3.1x at the end of 2016.

## BRAZIL<sup>2</sup>

Brazil had a year marked by major transformations, particularly in the political arena. Despite the lower levels of consumer confidence and a volatile international environment, the Brazilian Real ended the year with a 21.7% valuation. In 2016, the GDP dropped nearly 3.5%, driven by the reduction of private consumers and a declining inflation reaching a level of 6.29%.

At the end of 2016, the Company had 904 stores and the operation achieved a revenue of COP 36 trillion, with an 11.7% growth in local currency and comparable sales of 6.7%, including the calendar effect. Recurrent operating profit reached COP 1.2 trillion and the recurrent EBITDA margin reached 5.0% with a contribution of COP 1.8 trillion to the Group.

Assaí, the Cash & Carry wholesale business was consolidated as the country's most attractive and dynamic format, attracting consumers focused on getting value for their money. Assaí currently represents approximately 35% of the total food sales, with a year-to-date growth of 38.6% in local currency. Assaí ended the year with more than 10 openings, amounting to 107 stores and several expansion projects in progress to be completed in 2017, which include, among others, the conversion of low-performing Extra hypermarkets, an initiative whose first two pilots were carried out in 2016 with excellent results.

In turn, Multivarejo, a business unit that brings together the Extra and Pão de Açúcar brands, with a diversity of formats between Hyper, Super, Express and Allies, ended the year with 797 stores. In 2016, Multivarejo focused on strengthening its market share through commercial strategies that would allow it to offer its customers solutions in accordance with their changing needs. Multivarejo made a significant investment in margins that enabled the gradual recovery on sales and the revitalization of its value proposition. The comparable sales of the last quarter confirm this trend, closing at 3.7%, up from the 1.9% reached throughout the year, particularly highlighting the performance of Extra, whose sales increased by 5.0% in the last quarter, gaining market share over competitor's comparable formats. As the pillars of this result, the brand implemented the Group's regional strategies adapted to the local economic context, such as “*1,2,3 passos da Economia*” (Save all the month), “*Hiperferia*” (Hyper Fair) and “*O Mais Barato*” (The Cheapest).

In addition, the proximity strategy was led by the Minuto Pão de Açúcar brand, completing 14 openings during the year and increasing its market share. The format has stood out for being a profitable model that offers customers a high added value alternative.

Several action plans were implemented with a view to reducing costs, which partially offset the operation's lower sales margin. In addition to the job cuts, the Company's energy consumption was optimized, supply chain efficiencies were achieved, the marketing expense was rationalized and leases were renegotiated. Thanks to these initiatives, we managed to keep expenses as a percentage of sales at 18%, where this item grew 30 basis points less than the income growth.

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<sup>2</sup> All of Brazil's figures exclude the non-food business consolidated at the level of Via Varejo, which is in the divestment process.

Since the food business will require significant investment to maintain the lead, develop the Cash & Carry format and continue growing in proximity and qualitative formats, we have begun the divestment process of the Via Varejo non-food business. This will strengthen our focus on food and the capacity to capture opportunities in this field, which represents the most important market in South America.

We believe that 2017, despite the continued challenging economic scenario, will show a gradual recovery in the sales and margins of our operation in Brazil, thanks to the acceptance of its brands, its concentration on food and the aggressive expense reduction strategy carried out in 2016, which we expect will pay off this year.

## **URUGUAY**

Uruguay, in turn, showed real GDP growth of nearly 0%, impacted negatively, among others, by the slowdown of its main business and tourism partners: Brazil and Argentina, as well as high inflationary pressures resulting from salary negotiations.

However, we maintained our market leadership and our revenue grew to 11.1%, with a solid recurrent EBITDA margin of 7.8%. Comparable sales show an 8.3% increase.

Our operation ended the year with 79 stores, 14 of which were openings under the proximity format, for a total of 24 stores, thus achieving market leadership in this segment. Among the openings, it is important to mention the innovative "Fresh Market" project, which is focused on supermarkets with a supply of fresh, high added value products in Punta del Este.

Uruguay continues to be a stable market in which our market share of nearly 44% of modern retail and the extensive recognition of the Disco, Devoto and Géant brands, have enabled us to continue obtaining very positive results.

## **ARGENTINA**

Argentina is going through a transitional stage, in which the current Government has made significant progress regarding investor and international banking confidence in the country and by reopening foreign trade, in addition to conveying a message of respect for private activity. However, the high levels of inflation, above 40%<sup>3</sup>, have pressured the profitability of most businesses and affected consumer confidence.

In this context, Libertad had outstanding performance, where its sales in local currency grew 25% and gained market share. The recurrent EBITDA margin reached 4.8% as a result of the action plans regarding productivity.

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<sup>3</sup> Source: Ecolatina.

Libertad ended the year with a revenue of COP 1.4 trillion, 27 stores in operation, and a new proximity format in the premium category under the "Petit Libertad" brand, which opened its first store in the last quarter of the year.

In turn, the dual retail-real estate model, an essential part of the Libertad business plan, made significant progress in 2016. The Chaco shopping centers in Resistencia and Salta were expanded and remodeled, contributing an additional 14,700 square meters to the real estate portfolio, which now amounts to nearly 160,000 square meters of leasable space, thus consolidating Libertad's position as the leading shopping center and mall operating outside Buenos Aires.

## **INTERNATIONAL STRATEGY AND SYNERGIES**

Part of the long-term value of integrating Grupo Éxito's sales and real estate activity in the region depends on the effective capture of synergies and the implementation of these synergies with the rest of the countries where the Group is operating through best practices (such as in the case of exporting Know-How in the textile and fashion segments from Colombia to Brazil and Argentina) and the development of business models (such as in the case of launching the Cash & Carry format in Colombia). During the year, 19 cross-cutting initiatives were promoted with the four countries, with a total contribution to consolidated operating profit of nearly USD 25 million, in line with the plan to progressively obtain nearly USD 160 million of recurrent impact on the operating margin.

In Colombia, we are venturing into the wholesale business through the opening of the first Surtimayorista store in Bogotá, whose benchmark is the wholesale or Cash & Carry format of Assaí in Brazil. The promising results of the first months of operation have inspired at least two openings for 2017.

In addition, the textile model of the Éxito brand was implemented in selected Extra and Libertad stores in Brazil and Argentina, respectively. The strategy considers all aspects from the export of more than 476,000 garments of private label, such as Arkitect and Bronzini, manufactured by its own textile industry, Didetexco, to the sales and lay-out process. The initial results are more than encouraging. In these stores, the textile segment has doubled their EBITDA and has gained a share among their sales. In 2017, the textile strategy will continue to be deployed in stores in these two countries, and it will begin to be implemented in Uruguay.

In the second half of the year, the Allies model began to be implemented in Brazil under the *CompreBem* brand, inspired by the Surtimax and Super Inter. This sustainable business model ended 2016 with 102 partners in São Paulo and with the goal of 400 openings for 2017.

The "*1,2,3 Ahorrá todo el mes*" (1, 2, 3 save all month) business model was simultaneously implemented throughout the region. This sales strategy was born in Argentina and has been replicated in Extra hyper-markets in Brazil as "*1,2,3 passos da economia*" (Three steps of Economy); in Éxito as "*Quincenazo*" (Save all the month) and in Disco supermarkets in



Uruguay as “*Ahorrá*” (Save). This discount campaign drove the growth in billing and volume, in addition to gains in market share in the regions where we are operating.

Moving forward in the sales integration process, our suppliers exported products from the food and non-food categories as a result of the multi-sector business meetings held in Uruguay, Colombia and Brazil, where buyers from the four companies got to know the local portfolio of our suppliers. In 2016, orders were completed for coffee, meat products, juices, wines, flowers, kitchen utensils, textile products and small appliances, with 15 region suppliers. Also, we jointly purchased more than 300 containers of commodities on domestic and foreign markets, including olive oil, salmon and fruits, among others, obtaining savings between 5% and 15% on the cost of the products. In addition, agreements were renegotiated with the main multinational food and non-food suppliers, improving the terms of these businesses for the entire region.

In 2017, we will continue working as a team between the different countries in an effort to create value for the Group and its shareholders. Next year, we expect to obtain benefits from synergies of nearly double of those achieved in 2016.

## **FINANCIAL RESULTS**

At the end of 2016, Grupo Éxito’s consolidated revenue amounted to COP 51.6 trillion, showing a growth of 114.8% compared to the previous year and a proforma increase<sup>4</sup> of 14.5%. This growth is explained by a positive sales result in Colombia, the recovery of the food segment in Brazil, the exponential growth of Assaí’s Cash & Carry format and the opening of convenience stores in Uruguay.

The consolidated gross margin reached 24.3%, reflecting the resilience of Grupo Éxito’s operational model with improvement in Colombia, Uruguay and Argentina. In Brazil, the margin dropped 144 basis points as a result of the decided and effective reversal in prices of the Extra brand on the market.

In turn, expenses were impacted by the inflationary pressures experienced by all the countries in the region during most of 2016, particularly Colombia, with the collateral effects of the El Niño phenomenon and the trucker strike. The implementation of expense control strategies, as well as productivity efforts achieved a proforma evolution of 14.4% in expenditure, which is lower than the growth of revenue.

Recurrent operating profit reached COP 2.0 trillion, with a 3.9% margin. At country level, Colombia and Uruguay have maintained their profitability, while Brazil and Argentina have successfully continued in their recovery process thanks to the strategies and initiatives

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<sup>4</sup> The consolidated proforma financial information is intended to illustrate the effects that would have occurred if the Brazil and Argentina operations, which began to consolidate on September 1, 2015, had been recorded and had begun to consolidate on January 1, 2015, in order to provide a comparable basis with the statement of income at December 31, 2016. Given the decision to sell the company, this information also considers the effect of the restatement of results of Via Varejo S.A. as Discontinued Operations.

implemented throughout the year. In addition, Grupo Éxito generated a consolidated recurrent EBITDA of COP 2.9 trillion, with a 5.6% margin on sales.

The consolidated financial result stood at COP 1.26 trillion. The holding has a share of COP 458 billion, which correspond mostly to the financial cost of the debt related to the acquisition of new businesses in Brazil and Argentina. The holding's financial expense derived from the transaction was incurred during the entire year (vs. just 4 months in 2015), and in 2016, it was negatively impacted by the increase in the intervention rates of the Central Bank of Colombia, Colombia (+175 basis points).

The consolidated net profit of the fiscal year for continued operations amounted to COP 212 billion, COP 101 billion of which are attributable to Grupo Éxito after deducting minority interest.

Finally, after incorporating the income from the Via Varejo operation declared in the fourth quarter of 2016 as a discontinued operation, the net profit attributable to Grupo Éxito after minority interest amounted to COP 43 billion.

## **SUSTAINABILITY**

The year 2016 was important for the sustainability in Grupo Éxito. Under the leadership of the Board of Directors' Sustainability Committee, the strategy regarding sustainability was redefined and the Sustainability Policy was created. In recognition of our work in this regard, we were included in the Dow Jones Sustainability Emerging Markets Index for the fourth consecutive year, with a score of 52 points above the industry average.

At Grupo Éxito, we promote sustainability through initiatives that generate shared value in order to contribute to economic growth, social development and environmental protection in Colombia, based on five challenges:

As part of the first challenge, “*Gen Cero*” (Zero Gene), we are working so that, by the year 2030, there are no children in Colombia suffering from chronic malnutrition. In 2016, we attended 38,823 children, invested COP 19,700 billion, signed agreements with 39 municipalities and 4 departmental governments and led the creation of the “Comprehensive Law for Early Childhood Care” through Fundación Éxito.

Under the second challenge, “*Comercio Sostenible*” (Sustainable Trade), we generated relations of shared value with our allies and suppliers. In 2016, 86% of the fruit and vegetables sold at our stores were acquired directly from the country's producers, thus fostering sustainable agriculture. In addition, our Surtimax and Super Inter Allies program already has 1,307 store owners, also contributing to the formalization of small business.

Through the third challenge, “*Mi Planeta*” (My Planet), we intend to mitigate and offset our operation's impact on the environment and raise environmental awareness. Through multiple initiatives, we managed to cut down on energy consumption by 26 million MWh, recycled more than 22,700 tons of waste and reduced the use of plastic bags in our stores by 9.35%.



We received the Leadership in Energy and Environmental Design (LEED) Gold certifications in the Viva Wajira shopping center and the Silver certification in the Éxito Mosquera hyper-market, in recognition of our commitment to sustainable construction.

We carried out the first “Limpiemos Colombia” (Let's Clean Colombia) day, in association with the Ministry of the Environment and Sustainable Development, the Ministry of Commerce, Industry and Tourism and Bimbo. On this occasion, we mobilized 23,000 volunteers who collected, classified and disposed of 113 tons of waste in 4 cities in the country.

Through our fourth challenge, “*Vida Sana*” (Healthy Life), we encourage healthy living habits among our customers and employees. During the year that ended, we assessed the nutritional profile of 1,442 products from our stores, trained 23 suppliers in product reformulation, and created specialized sections and days to promote healthy eating.

Finally, the fifth challenge, “*El Éxito del Grupo Éxito está en su gente*” (The Success of Grupo Éxito Is in Its People). As the largest private employer in Colombia, we offer an attractive and inclusive work environment and the development of our employees in being and doing. We delivered more than 530,000 benefits through more than 100 programs, provided 2 million hours of training and launched our professional equality policy. In our labor inclusion program, we employed 799 individuals with physical or cognitive disability, youths at risk, victims of violence, demobilized persons, militaries and their relatives.

For further details on the actions carried out and the achievements regarding sustainability in the year 2016, check the Sustainability Report.

## **CORPORATE GOVERNANCE AND INTERNAL CONTROL**

In 2016, the Company continued to move forward in the implementation of the Corporate Governance standards from the Colombian Corporate Governance Best Practices issued by the Financial Superintendence, as part of the OECD model, and in the voluntary adoption of international best practices.

The performance of the Company's internal control and financial information disclosure systems is adequate. In this regard, the financial statements, indicators and relevant events were presented on a periodic basis to the Audit and Risk Committee and the Board of Directors and have been certified by its Statutory Auditor. Through the Audit and Risk Committee, the Board of Directors supervised the processes of financial reporting and information, enterprise risk management, the internal control architecture and system, including the monitoring of Internal Audit and Statutory Audit management, transactions between related parties and conflicts of interest, compliance with the regulations applicable to the Company and the transparency program.

As managers, we certify that the internal control system showed no failures that would have prevented it from recording, processing, summarizing and adequately presenting the financial information, nor was there any significant fraud that would have affected the quality and

integrity thereof. The disclosure of financial information was verified and complies with the current regulations, ensuring that the information at December 31, 2016 is appropriate, and contains no defects, inaccuracies or errors preventing the knowledge of the Company's true asset situation.

For further information on Corporate Governance and the Company's internal control system in 2016, check the Corporate Governance Report, which is an integral part of this Management Report.

## **TRANSACTIONS WITH RELATED PARTIES**

The information regarding transactions carried out with related parties is detailed in the Annual Corporate Governance Report, which is an integral part of this report and in Note 34.2 to the Financial Statements. Said transactions were carried out in market conditions and in compliance with the best corporate governance standards, which include the information or approval thereof by the Audit Committee or the Board of Directors, depending on their classification as material or non-material, recurrent or non-recurrent, as well as that of the competent Conflict of Interest committees in each case.

It is also important to mention that the Audit and Risk Committee is made up exclusively of the independent members of the Board of Directors and that the members of the Appointment, Remuneration and Corporate Governance Committee include all the independent members of the Board of Directors, which are also the majority of said committee.

As provided in Article 29 of Law 222 / 1995, it is hereby declared that in the year 2016, the Company did not make or fail to make important decisions of interest to its subordinates that should be disclosed in this report. In addition, the Company did not complete important transactions with third parties of interest to its subordinates that should be disclosed in this report. Nor did its subordinates make or fail to make decisions of importance or interest to the Company that should be disclosed in this report, nor did they carry out transactions with third parties of interest to their parent company that should be included in this report.

The Company did not perform transactions with its managers other than those arising from the relationship of employment or fees on account of consultancy and assistance for the Boards of Directors and supporting Committees.

## **REGULATORY COMPLIANCE AND INTELLECTUAL PROPERTY**

It is reported that the Company has strictly complied with the regulations that regulate matters regarding intellectual property, it is the owner of the brands, names, insignias, slogans and distinctive symbols it uses to distinguish its products and services, or it is authorized to make use of them under a license agreement. The use of software products by the Company is in compliance with the current legislation. Finally, it is reported that the Company has not in any way restricted the free circulation of invoices issued by its suppliers of goods or services.

## CLOSING NOTES

In short, we have gone through complex economic times in the region. We are now better prepared to capture future opportunities with the modern Cash & Carry model; with hypermarkets whose value proposition has been renewed; regionalization of a high added value business that is the textile segment; capturing synergies at all levels and a strict control of working capital and operating expenses with consistent productivity initiatives. We believe that the gradual recovery of the two main regional economies, Brazil and Argentina, will bring great value to Éxito.

The gradual reduction of the Organization's financial debt and interest rates in Colombia, along with the progressive improvement of the net income of our operation in Brazil, will lead to the gradual strengthening of the Group's net profit and the share value, which has been recovering in a positive manner in recent months.

Grupo Éxito is the food market leader in four attractive markets in the region and, as a whole, in South America. Brazil and Argentina are going through a transitional stage, gradually overcoming their political and economic crises, and they will once again be the region's economic drivers, with great potential for companies that, like ours, have businesses with solid foundations, recognized brands and leading positions on the market. Colombia is facing a slowdown in demand, but has maintained solid economic foundations and the investment grade that allow trust in a stable business environment in the long term.

Grupo Éxito is also developing a customer traffic monetization model, with complementary services and real estate businesses that provide resilience in an environment of dynamic competition. Its recent steps toward the integration of its businesses in the region, the launch of its specialized real estate vehicle, its focus on food, with the consequent structural and strategic simplification, are all aimed at creating value for its shareholders.