

Four months after arriving at the retailer

Falabella's President: "The mandate is to emerge strengthened from this conjuncture"

He took the helm in the midst of the crisis of the leading Chilean retailer — controlled by the Solari and Del Río groups — with red numbers and distrust from customers and the market. This week, he announced his first major decision; Gaston Bottazzini, the CEO, will leave Falabella at the end of the year. In his first interview, Enrique Ostalé looks back on his first months, the ongoing challenges and the changes that are coming.

If a few months ago, Enrique Ostalé Cambiaso (63) spent most of the year traveling between Chile and the United States, today his residence is on this side of the world. 'Stability' that hasn't kept him off airplanes, quite the opposite. It's been four months since this Bachelor of Business, Administration and Economy, who rose to the top leagues of the giant Walmart — he was its president and CEO in Mexico and Central America — became the president of Falabella, the first outsider to the controlling families.

All, in the midst of an unprecedented crisis for the company — controlled by the Solari and Del Río groups — with red numbers and market distrust. If in 2018, the stock was above \$5,000, today it is around \$2,024, and in March, it completed three consecutive quarters with losses, with the fourth quarter seeing profits largely due to accounting effects.

Perhaps that's why Ostalé hasn't stopped flying. He visited operations in Chile, Peru, Colombia, Brazil, Mexico, Uruguay, and Argentina. And this Tuesday, he announced the first big decision: the CEO, Gaston Bottazzini, will leave Falabella in January. 'Gaston had a very difficult last five years (...), in any leader, that generates natural wear and tear, and he had the generosity to understand that his cycle at Falabella was coming to an end,' Ostalé will say in this conversation. With headhunter Egon Zehnder, they are now looking for his successor.

Meanwhile, the retailer navigates through the closures imposed by the pandemic, first; the incentives that later took consumption to the clouds, and the drop that the economic crisis brought. An almost perfect storm... 'Falabella has enough liquidity and the capacity to meet all its financial obligations,' responds its president, and will say it several times.

—How did the opportunity to lead Falabella come to you?

'Falabella has always seemed like a very attractive company to me. The controlling shareholders made the decision to make a significant change in the board of directors, inviting three new members. In my case, I was invited by the Bethia group because they thought I had something to contribute and wanted new perspectives that would complement the directors who were staying.'

—What perspective do you bring?

'My experience is in the retail world, not in a company identical to Falabella, but the challenges in retail are quite similar. I lived it for the last 10 years with a fairly global perspective, which gives me a broader view. In addition, there are two major areas where my experience can be beneficial. In driving and continuing to develop Falabella's business models. And two, in how we continue to

increase the effectiveness of this organization, we are more effective and with the necessary sense of urgency.'

—One thing is to be a director; another is to be president. What mandate did you receive?

'I am the president of a board where we have the same responsibility, we act as a team, and contributions are made when we discuss and take action. Those mandates are directed towards the executive team, that in the end, leads the company.'

—Priorities are always set; where to start, what was your first priority?

'I would summarize it by saying that Falabella is a great company, and the mandate is to emerge strengthened from this conjuncture.'

—Conjuncture or, rather, a crisis?

'The crisis is part of the conjuncture. Indeed, there is a crisis that is synchronized in the three main markets — Colombia, Peru, and Chile — which makes it more challenging.'

—What was your diagnosis of the company's crisis?

'I have focused on getting to know the people, the businesses; traveling to all the markets where we operate, meeting with our partners, getting to know the company. Based on that foundation, through the board, generate the discussions that I believe are pertinent to strengthen the company.'

—What discussions?

'How do we strengthen this organization to make it even more effective, with a sense of urgency. And the other is our business model; it has great strengths, but we also need to make some adjustments.'

—Do you already have those adjustments in mind, with three consecutive quarters of losses?

'Without a doubt, an organization is more effective when it is able to take charge and adapt to the new situation as quickly as possible. But a sense of urgency is not enough; you must take actions to achieve that effectiveness.'

—Four months later, what is your diagnosis? Why is Falabella the most affected retailer by the pandemic?

'Falabella began a very important transformation process, where much of the energy was focused on that, as with any transformation process, there are unintended consequences and pains. We were in the middle of that when this conjuncture arose, which also impacted our financial business...'

—Are you referring to the pandemic or the general economic crisis?

'The pandemic accelerated the need for that transformation. But the conjunction is coming from an excess of liquidity, in people's income, especially in Chile, but also in Peru and Colombia. And it transitioned to a period where inflation started to rise, interest rates increased, and there was a slowdown in consumption and economic growth. That impacts during this transformation.'

—Why did Falabella struggle more with it?

'These transformation processes involve the development of skills, for example, related to logistics, which take time. The pandemic caught Falabella in a transformation process that goes hand in hand with a strong investment to develop these skills. The timing of the pandemic with the development of these competencies was not ideal, but the important thing is that it was being addressed.'

—Where are the critical points?

'I have no doubt that more favorable winds will come, and consumption will start to recover. Another part has to do with the internal actions to better adapt and mitigate the negative impacts that this situation generates. The company has already been doing this; a cost reduction plan and an analysis of what things are working well and need to be pushed harder and what needs to be corrected.'

—The multi-million-dollar acquisition of Linio, was it a mistake?

'In the context of the time, many retailers made quite similar decisions, and it was thought to be the best decision. Obviously, Linio brought Falabella the ability to advance more quickly in this development agenda, especially on digital platforms and to develop a marketplace.'

—Falabella aimed for omnichannel, buying Linio while planning a megastore in Parque Arauco, how do you see omnichannel today?

'Perspectives and responses to that question have been changing. The answer from five or ten years ago is very different, but one aspect that has become clearer is that omnichannel is still very important because customers want to have this experience with brands, from physical to digital and in all possible combinations with minimal friction. Our advantage is that we can offer that to them.'

—That demands great flexibility to make adjustments; is it possible in a company as large as Falabella?

'In the end, we are a composition of different businesses. The conditions for the organization to take charge and have the flexibility to execute changes are by strengthening each team, each business.'

—Mercado Libre's success is built on the digital, how do both worlds coexist and are financially sustainable?

'As Marcos Galperín said: we are not obsessed with competition either. Both of us are developing an ecosystem, and the most important thing is the strength that attracts customers. How Mercado

Libre builds that ecosystem is different from how Falabella builds it because our strength is how with omnichannel and a value proposition heavily based on brands, we are able to deliver an experience where those exclusive brands are also our partners.'

—Do customers value that, or do they prefer to buy what they want with impeccable logistics?

'Logistics is a hygienic factor; we must be able to provide a logistics service as quickly as possible. In the end, it will be more of a commodity. The difference ends up being that in a generalist marketplace like Mercado Libre, there is absolutely everything, and it is difficult for brands to differentiate themselves. We seek to build a winning ecosystem, and for that, it must generate customer preference. That preference is built with an offering where our assortment will always be more refined, which is what the customer expects from us.'

—It has been quite a challenge to achieve that commodity; it is the main problem with customers...

'Indeed. It is one of the most important skills to acquire in this transformation, and it has happened to everyone in the physical world. Companies like Falabella have been logistics operators for many years, but the competition required by the e-commerce business is different. It is not just about having the capacity to distribute large volumes to stores but also delivering small units to households. We have been making rapid progress in that regard: if in 2021, 38% of our shipments reached customers in less than 48 hours, today it is 60%. During the peak of the pandemic, the volume increased significantly, but now it has tended to normalize, and that also helps provide better service. We have a lot of room for improvement because the challenge is not only to deliver in less than 24 hours but also to be cost effective.'

—That harmony with the client was the greatest cost of the pandemic, how are you doing to rebuild it?

'There are two challenges: the more hygienic aspect of shipping and customer service, and we must be as good as the best, but again, that will not differentiate us. There, the two main challenges are the marketplace as part of this digital transformation. And while the company made the decision to develop it, understanding its importance, it had unintended consequences. The customer could have been confused because they have a perception of what Falabella, Sodimac, and Tottus are, and by enhancing the marketplace as the entry to our vertical businesses, the customer got confused. Today, we are improving it.'

—How? Was it a mistake to consolidate all the businesses in the marketplace?

'These decisions had a purpose, and, of course, it's easier to say it with Monday's newspaper. But the important thing is that we are returning to strengthening the websites of the different businesses separately.'

—What will be the role of the supermarket business in this transformation, which has shielded others like Cencosud?

'It has been challenging in Chile, but we have an attractive presence in other markets. The role of supermarkets in our portfolio is important, not only as a way to diversify risk but also because there are good opportunities in the countries where we operate.'

—Do you want it to be a relevant business?

'There is a challenge to enhance our presence in Chile, but it is not the only market where we have opportunities. We would like to have a larger share, but for now, we are satisfied with what we have.'

'The main focus is to improve our financial results'

—Falabella's stock has risen, but it is still under pressure. Credit rating agencies and investors continue to be critical. How do you expect to regain the market's trust?

'The main focus for everyone at Falabella is to improve our financial results. The most relevant thing is to improve our operational cash flows, our EBITDA, our results. Additionally, we are looking at how to strengthen our balance sheet, and measures have already been announced. We have a much greater focus on investing where the best growth opportunities are. Nevertheless, I want to be very emphatic: Falabella has the liquidity and capacity to meet all its financial obligations.'

—What measures are you taking to strengthen the balance sheet?

'I don't want to get into the details because a lot of information has already been released.'

—What are the main ones?

'All I can say is that the focus and energy are now on improving Falabella's profitability; it's our number one priority. Second, strengthening the balance sheet. We are evaluating all options, but the important thing is that we don't see any problems in meeting our financial obligations.'

—Are you prepared for credit rating agencies to downgrade the company's rating?

'Markets are quite dynamic. We are making every effort to find what is best for Falabella.'

—Do you see the rating at risk?

'We are currently under watch by the credit rating agencies, and they have given themselves a period to continue evaluating the situation.'

—Can it be reversed in those 90 days?

'I insist, we are doing everything necessary to improve our accounting and strengthen the balance sheet. I am optimistic, and I see events that will be catalysts; better times are coming, with more tail winds, and not as against us as we have faced since last year. We already see it in our financial businesses, especially in Chile, where the risk is now under control, and we are beginning to see the benefits. Although consumption remains very impacted, especially in the construction sector,

we also expect it to start recovering towards the fourth or first quarter of 2024. Those changes will find us in better physical shape as a company.'

—How much more can Falabella downsize?

'As much as necessary. If we want to be more effective as an organization, we have to adapt to the circumstances.'

—Debt is at 8.6 times EBITDA, how do you expect to reduce it?

'By improving our EBITDA, which means improving our financial results, and I am confident that we will start to see it. And by strengthening our balance sheet. We are taking care of everything, with a focus on results, which has the greatest impact.'

—Are you not considering a capital increase?

'Not that I am aware of.'

—Part of the market believes it's the way out...

'It is evident that it would not be a good business for shareholders to dilute themselves at the current share price. Capital increases are done more in situations of strength than weakness. The company maintains its financial strength; we are not in that scenario today.'

—How do you assess the leadership within Falabella?

'There is a great team of people, including young and passionate individuals who know the business. It's a good mix of youth and experience. I have no doubt that we have a great team, but that is not enough; what is important is how they work together in a more collaborative and finely tuned manner.'

—Did the board determine that Gaston Bottazzini was not the appropriate conductor?

'The board is very grateful for Gaston's contributions over the past 15 years. He faced the last five years, which were very difficult, and he not only had to lead this digital transformation but did so in the context of a pandemic, inflation, rising interest rates, which did not make these processes any easier. In any leader, this generates natural wear and tear, and he had the generosity to understand that his cycle at Falabella was coming to an end. Also help us in the succession process, looking for a new leader who does not bring this wear and tear and can help us continue in this process.'

—What does this new leader need?

'Hopefully, it will be someone who knows retail, the digital business, someone with experience in similar transformations, who understands the challenges and how to lead these change processes more effectively. And someone with interpersonal skills that allow them to generate this collaboration, increasing the chances of being a conductor who succeeds.'

—Traditionally, changes have come from within; now, do you prefer an external candidate?

'We are open to both options. Falabella always has a succession plan, which includes looking both internally and externally.'

—Is this the beginning of a deeper restructuring?

'We do not plan for it to mean a restructuring, although when you face more complex challenges in an industry that is changing, we always look for opportunities to simplify our organizations, as it also goes hand in hand with being more effective.'

—You have made moves in some divisions, such as the bank; does it respond to an evaluation?

'These are processes that have been ongoing for some time, through discussions, or in this case, from the executives themselves making personal decisions. The important thing is that we had a succession plan, and we are very pleased with the person who will take over the leadership of the bank in Chile.'

—When will you decide on the new CEO?

'When it is defined. Gaston agreed to accompany us in this process. We hope the timing will coincide, although we are more concerned with finding the right person than meeting a deadline.'

—As chairman of the board of directors, how do you lead and cohere a company in crisis, and one also marked by family conflicts?

'First, Falabella is a great company, and it will emerge stronger from the current conjuncture. The board, as a board, has only one agenda: what is best for Falabella. The shareholders, especially the controlling ones, made a very important decision to make changes. On the board, we take on the challenges with a sense of urgency. Obviously, there are discussions, there are positions, it's part of the richness, but we make decisions with the executive team and mandate them to execute.'

—Defamiliarizing the presidency, was it a timely or late decision?

'I am not qualified to answer that. You would have to ask the shareholders.'