Walmart

Walmart's Fiscal Year 2015 Q2 Earnings Results
Media Call Transcript
August 14, 2014

Randy Hargrove: Good morning. Thanks everyone for joining us today as we get into our second quarter earnings. We're going to have about 30 minutes for today's call. We're going to have some brief opening comments from Charles, and then we want to get to your questions. There will be a queue you can get into to ask those questions, just press * on your touchtone phone. We've got several of you on the phone today, so if you could limit your questions to one or two starting out, we'll try to cycle through those as quickly as we can and then start back up. You should all have a copy of our transcript, press release and the presentation that went along with the transcript. If for some reason you didn't get that, please let me know. We'd like to keep the conversation today to the financial performance. And with that, I'll turn it over to Charles.

Charles Holley, CFO of Wal-Mart Stores Inc.: Thanks, Randy. And thank you everybody for joining us and for your interest in Walmart. I'm joined today by Neil Ashe, our CEO for our Global eCommerce businesses. I plan to make a few opening comments. I'll turn it over to Neil for a few comments, and then we'll open it up for questions.

We were pleased that we were well within our EPS guidance at $1.21. Just a reminder, our guidance was $1.15 to $1.25. The International segment led the company. It had a very good quarter. Sales were up 3.1%, a little under $34 billion. But when you exclude the effects of currency, which were negative, we would have been up over 5% - which was very healthy, I think, with this global economy. Profit was up 8%. All of our countries had a positive comp except China.

Walmart U.S. recorded a flat comp and total sales of $70.6 billion. That was up 2.7%. Comps for every quarter last year were negative; and even a little bit negative – flat-ish – last quarter. So this quarter was really the first time that we crossed that true flat line. We think that's real progress, and we know that our focus going forward is to stay in that positive territory.

Walmart U.S. profit was down 2.4%, primarily from labor investment in our stores and then higher health care costs than we expected. You know, the health care cost has been a theme all year long. One highlight was that Neighborhood Market continues to have positive comps - the positive comp was 5.6% for the quarter.

Sam's sales were up 2.3% and flat comps, as expected. And Sam's also kicked off its Cash Back campaign for its Plus memberships, and it caused some additional investment expense and margin decline for the quarter, but we're very pleased with the early results of that.

I'll let Neil update everybody on Global eCommerce.

Now, looking forward, we forecast our third quarter earnings per share of $1.10 to $1.20. We do have pressure from our tax rate – we think it will be at the high end of our estimated range for the year, which was 32 to 34%. And it can and will and may be impacted by the lack of tax legislation I should say, on what you might have heard called extenders. We also have a 32 to

34% rate for the year that we put out, and that is really dependent on discrete items and whether or not there is tax legislation on those extenders.

Health care costs will also weigh down in the third quarter of the year. We'll have about $170 million more than we anticipated at the beginning of the year. And then Global eCommerce: we continue to invest in our Global eCommerce. That investment will be an additional one to two cents over what we anticipated at the beginning of the year. And then, we're still cycling through the reduction of SNAP [Supplemental Nutrition Assistance Program] through this third quarter.

Walmart has projected a comp of flat for the third quarter, and Sam's will be slightly positive.

With that, I'll turn it over to Neil, and Neil can provide a few comments.

Neil Ashe, President and CEO of Global eCommerce: Thanks, Charles. Good morning, everyone. It's nice to spend a few minutes with you to catch up on where we are in e-commerce. As you know, we're working hard here to build best-in-class e-commerce and then marry it with the assets of Walmart to do for customers what no one else can, and win what we're calling the integration of digital and physical.

We're pleased we grew sales about 24% in the second quarter, which is faster than the market around the world. We saw double digit growth rates in our largest markets – the U.S., U.K., Brazil, China – and triple digits in smaller markets like Canada and Argentina.

Spending a second on the U.S., we started the rollout of the new Walmart.com site. We also rolled out Savings Catcher, which is our new price comparison tool. It's a great example of integrating digital and physical to better serve customers and to reinforce the trust that they have in the Walmart brand around price. With the launch last week of Savings Catcher, the Walmart app was the number one app in the lifestyle category last week in the app store.

Switching to Sam's Club, we also re-launched the iPad app there, and the member reaction has been outstanding. We went from 3.7 stars as a rating in the old app to 4.5 stars in the new app. We've done a lot of work around Click 'n' Pull, which is where you can order online and pick up in a club, which is going really well.

As Charles mentioned, we're investing, and we're excited about the progress that we're making. We're focusing that investment around three key areas. The first is around team and our talent density, the second around our global technology platform and the third around our next generation fulfillment network.

So, on the team: over the last quarter we announced that Fernando Madeira was moving from Latin America to take over Walmart.com in the U.S., Latin America and growth for the rest of the world; we're excited about having Fernando here. We also created a new role, a chief operating officer role, and we brought Michael Bender over, who had been president of the western region of U.S. retail, to help us develop and grow this business, as we're growing really fast around the world.

On the technology platform: it's really a major feat to do what we're doing on our technology platform, and we're excited about it. We're re-building everything from the data centers to the website to the apps, and everything in between. And we've made a ton of progress that customers haven't seen. So we're really excited to talk about the new site that's rolling out in the U.S. because now customers can tangibly benefit and feel that site. There are new search, browse and front door pages - [mobile] is about 50% of the traffic. It's optimized for tablets, obviously, since that's an important part of our traffic. And you'll continue to see the rollout of new features across that. Better personalization, better shopping experience, etc.

On the fulfillment network side: we announced that we added another facility in Indiana, which is under construction. In the U.S., we add that to the facility we announced in Texas, as well as in Pennsylvania. We also announced a facility in Cajamar, Brazil, and we're expanding in other markets around the world as well. So you'll continue to hear us talk about that.

What we're really excited about on our fulfilment network is that we can build these e-commerce-specific facilities and then combine them with the larger distribution network to get efficiencies that are unique to Walmart, which allows us to serve customers better and faster – and for a business model, less expensively – which we're excited about.

So to close out and open up for your questions, we're excited that we're growing faster than the market around the world. We're pleased with the progress that we're making on our key initiatives around our talent, technology and fulfillment networks. And we're really excited about the opportunity that is unique to Walmart, which is to win this integration of digital and physical. So to have the best of e-commerce, as well as the best of retail, we can be the "and" solution for customers.

So I'll pause there and send it to you for questions.

Courtney Reagan, CNBC: Thank you. Good morning, Charles and Neil. Thanks so much for being with us again here today. I just have a quick question about traffic in U.S. stores. Again, another quarter of negative traffic. Is this something that we really should expect going forward, a negative trend as perhaps more customers are migrating online for both Walmart and competitors?

Charles Holley: First of all, our traffic – even though it's negative and we want it to be positive – the trend is actually positive from what we saw in the last quarter. I think it was up about 30 basis points. So going forward, our focus would have positive traffic. It's not something that we would just expect and say that's going to be it. We do think that we have a lot to offer for the customer. And I do think, when you look at the food traffic and you look at the holiday traffic – we would anticipate that we could continue to make improvements in those traffic numbers.

Courtney Reagan: Great. Thank you very much.

Anne D'Innocenzio, Associated Press: Hi. I wanted to ask you about the back-to-school selling season. How is it faring so far? And do you feel that the Rollbacks you announced and the other initiatives are resonating? You can comment on the promotional environment too.

Charles Holley: Well, it's always promotional, so I don't think that's anything different than we've seen in the past. So far – and it's still early in back-to-school – but we're very pleased in what we see. We'll have more on that in October, but so far so good.

Anne D'Innocenzio: Do you feel…so it's just as promotional as last year?

Charles Holley: Yes, I do. And I'll go one step further – I think that we'll continue to see that through the holiday season. It will continue to be promotional. And that's no different, Anne, than what we've seen in the last few years.

Anne D'Innocenzio: So it's nothing any more intense?

Charles Holley: No. But it has been intense in the past, so don't take that for "it's not intense."

Anne D'Innocenzio: Right. No, I mean just as intense as it has been.

Charles Holley: Yes, absolutely.

Anne D'Innocenzio: Thank you.

Julie Hyman, Bloomberg TV: Gentlemen, thank you for doing the call. Neil, I wanted to ask you about the new forecast for e-commerce growth year-over-year, for the full year, looking like it's going to be more in the 20 percentage point increase versus 30%. I just wondered if you could give us a little color around why the decrease? What has changed?

Neil Ashe: Thanks, Julie. As I mentioned, we're starting from the market comparison. We're pleased that we're growing faster than the market and some of the larger competitors. So that's really good. We have – not surprisingly, we're Walmart – so we have really high aspirations, and we're going to continue to chase those aspirations. We're going to continue to set really high targets and we'll have some quarters where we grow faster than others. Generally, we're really pleased that we're growing faster than the market and we're making progress.

Hadley Malcom, USA Today: I'm wondering if you guys can speak to, in terms of performance at U.S. stores with regards to sales and traffic, what do you think specifically needs to happen to turn that around in the coming quarters?

Charles Holley: I think we're on our way to doing that. As I mentioned, our comps just now getting past flat. It always comes back to, I think, three things in my mind: that would be price, assortment and service. And I know that the new leader, Greg Foran, is very focused on that. And those have been our success in the past and they will continue to be our success.

Hadley Malcom: With regards to the success that you're seeing at the Neighborhood Markets, what do you think is setting those apart or driving the sales and traffic there?

Charles Holley: I think convenience is where the consumers have been looking, if you look at the Baby Boomers or whatnot. We still do a very nice full basket trip at our supercenters. But if you look at what we call the "fill-in trip," I think there's been well over 10,000 new small stores in the U.S. in the last three years. I think convenience is becoming a factor. And if you look at what we offer at the Neighborhood Market that some of these small stores don't: you have the fresh categories, which a lot of these small stores don't, you have a pharmacy and you have fuel. Those are very important, I think, for the success of the Neighborhood Markets.

Hadley Malcom: When you mention other small stores are you referring to dollar stores?

Charles Holley: I'm referring to all: whether it's convenience or dollar or whatever. Just a small store being less than, I'd say 40,000 or 30,000 [square feet] and less.

Hadley Malcom: Thank you.

Phil Wahba, Fortune: Good morning. I have a question about the small format stores. You've been touting it for a few quarters now, but my back-of-the-envelope calculation shows it might be two or three percent of overall sales. When do you think that will play a meaningful part in your U.S. comps? I'm sure right now you wish there were more of them, but how many quarters are we away from the smaller format stores really making a difference in your U.S. comps?

Charles Holley: Thanks for your question. I'm not sure I can give you a definitive answer on when they would make a difference in the comps by themselves, because we are focused on the fleet of all of the stores and making sure we have positive comps. As you know, we're going to put about 200 new Neighborhood Markets up this year and 100 Express stores. As a reminder, those Express stores are still in pilot, so there isn't a plan right now to ramp up Express stores. However, you will continue to see increases in these Neighborhood Markets.

And as far as when those would take over comp, that's not how we think. What we think is really focusing on the core, the supercenters also, to make sure we get those in positive territory.

Shelly Banjo, Wall Street Journal: Good morning, Charles. I just wanted to ask again about inventory. You guys mentioned that a lot on the call. Is that mostly due to the store re-sets and things like that, or why is inventory continuing to out-pace sales?

Charles Holley: Thanks, Shelly. I think in the U.S., we were up about 6% or so for the total company; the U.S. was up a little over 5%, I think. And the U.S., which is the lion's share of our inventory, half of it is new stores, as we're trying to open new stores. And it's up a little higher than we would like, and that's because we had softer sales. But right now we don't think there's anything significant in the jump in the inventory that we see going forward. But it is something that we monitor closely.

I think International had something similar, where some majority of their increase was related to new stores. Also World Cup. One of the things that's important to remember is that most of our international countries are on a calendar year, which means that most of their inventory would have stopped for the books at the end of June. And they had a big build up for World Cup. So some of the increase you would have seen would have been an increase for the World Cup.

Shelly Banjo: And when you say new stores, does that also include the new e-commerce distribution centers? Does that also contribute to the inventory?

Charles Holley: That would. But it probably, since that's going to flow through a little quicker and turn probably quicker than a store in some of the items, that wouldn't have been a big contributor. I think the World Cup and the new stores themselves would have been one of the bigger contributors.

Shelly Banjo: Thank you. And then, Neil, just wanted to follow back on the decline in the growth target. What exactly went into that decline? What was not happening that made you reduce it from thirty to mid-twenties?

Neil Ashe: Thanks, Shelly. You know, as I said – it's really, we set high aspirations. And grew faster than the market, but we didn't grow quite as fast as we had wanted to. So we'll continue to push on that. The sales growth was kind of consistent around the world, as I mentioned in my comments. We had strong growth in Brazil, China and growth in the U.S. So growth is good around the world, it just wasn't quite as high as we had wanted it to be.

Shelly Banjo: And were there any specific factors?

Neil Ashe: No. As I said, we out-grew the market. So I think we're pleased with where we're growing. We'll continue to push to grow faster.

Sid Cavale, Reuters: Hi there, Charles. I just wanted to ask you about the special spending that you've mentioned. Do you have timing on when this will end or any positive signs that you see going forward that might actually ease this pressure? Can you add some color on this? I mean to say that, there's a lot of pressure on consumers cutting back on spending. Are you seeing any good signs of that easing soon or do you expect that to continue through the holiday season?

Charles Holley: You're talking about pressure on the consumer? You know, I don't think we've seen any dramatic change with the consumer over the last few quarters. They're still under pressure. Still concerned about the cost of living, employment and those kinds of things. One of the things, when you look at our business – the SNAP reductions they had, I believe occurred last November, we'll cycle through that when we get into the fourth quarter. But overall, we're not seeing any change in the consumer than we've seen in the last few quarters.

Sid Cavale,: Thank you.

Jo Kent, Fox Business Network: Hi, thanks for taking our call. I just had a question about China. We saw store closures there this year. Obviously comps down there – the only international space that saw that. What are you guys going to be doing to try to continue increasing market share and up your presence and get those comps back to positive levels?

Charles Holley: China itself, the economy is going through a little bit of a pullback. As you know, there's been a government austerity program, and that's affected all retail. I believe we actually increased our market share, even in a down market and even with negative comps. So it's been a tough market for all retailers. We're putting in more centralized distribution, making sure our stores and our supply chain are much more efficient. Just having more discipline in the supply chain and making sure that we're efficient. But we feel good about the direction of where we're going. I think our China results are more of a relation to the overall economy than our sales.

Jo Kent,: Thank you.

Anne D'Innocenzio: Hi. So how do you think the Dollar Tree/Family Dollar deal will impact Walmart? Are you looking at maybe further accelerating the expansion of small store formats? Do you feel it will put more pressure on Walmart?

Charles Holley: You know, our focus really remains on our business and what we feel works for us, versus what other people are doing out there. We pay attention to it, but like I said before, we really like the position of our small stores, our Neighborhood Markets and even the pilot Express. Because we think, for us, it's a real winning combination when you add the fresh, the gasoline, when you add the RX, and even frozen - we have more frozen than others. And it's really put us in a good position in the small store sector.

Anne D'Innocenzio: Ok. Thanks a lot.

Julie Hyman: Thank you. This is actually a follow up to the last question. I know you guys have commented in the past that you likely would not be looking to acquire smaller format stores. I just wanted to get an update from you on that, given that some things have changed in the landscape in terms of the battle over Family Dollar – I shouldn't say the battle – but Dollar Tree agreeing to acquire it. I wonder if your thinking on that situation has changed at all?

Charles Holley: No, it has not. Like I said, we very much like our format. These smaller formats can sell anywhere between three times to eight times what some of those stores do. And we think it's a much better fit for our customer – and for our shareholders, because they have really good returns for us.

Julie Hyman: Thank you.

Shelly Banjo: I was just hoping you could expand a little bit about the consumer. And what would it take in the U.S. to get your customers spending more?

Charles Holley: You know, I'm not an economist, Shelly, but I will say that I think it's pretty obvious we need to make sure that jobs are out there – good jobs – and the growth in jobs that are out there and the opportunities for our core customer. I think that's going to be very important going forward.

Shelly Banjo: And real quick – on the increase in associate hours, what is that in relation to?

Charles Holley: Just service. Making sure we have the appropriate service when the customers are in the stores.

Shelly Banjo: Can you quantify what the added hours are?

Charles Holley: No. I don't have that, honestly, and I don't think we disclose that in our release.

David Tovar, Vice President of Corporate Communications: Shelly, we have some information on the average associate hours have looked like over the last year or so. We can help you with that.

Shelly Banjo: Ok. Thank you.

Phil Wahba: Hi. Just to go back to the formats a bit: one way to get comp sales to go up is to close stores. I'm wondering is there any discussion – is it possible to close any of your supercenters? Is it desirable? Are store closings, even a small number, part of things that you're looking at?

Charles Holley: First of all, the supercenter still has one of the highest returns of any format we have in the company. So overall, it is a great format and still does a very good job of one-stop shopping and that large-basket trip. So we like where we're headed. Now, making sure we have good ancillary services for our customers – making sure that we tie it in and expand the assortment tremendously, tying it in with our e-commerce operations – we think makes it very powerful. And like I said, we have very good returns with supercenters. So no, any type of significant activity like that, it wouldn't be in the cards because we have good returns, and it would be silly to close a lot of stores with good returns.

Sid Cavale: Hi there, just one question, this is for Neil. Neil, I'm wondering can you give me an idea of how much has actually been spent already and how much is expected to be spent this year on online business?

Neil Ashe: Charles, do you want to take that or do you want me to take it?

Charles Holley: You go ahead.

Neil Ashe: So we've consistently talked about a few cents per share that we're investing in e-commerce. When you think about the opportunity that's in front of us, we're viewing this as a long-term change in customer behavior that we're benefitting from. So we're investing to that to continue to grow faster than the market. So it's a few cents per share, but we're pleased with where that's going.

Charles Holley: Yeah, our original incremental investment was two to four cents. And what we announced in this release, we'll invest in an incremental increase of five to seven cents per share for the year.

Sid Cavale: Anything other than total investment that you're actually going to make or the amount you set aside? I'm just trying to get an idea of how much has been spent totally?

Charles Holley: We haven't released that in total. We've just been talking to the street about, in the last two years, the incremental investment. We will have more on our Global eCommerce businesses at our October analyst meeting.

Sid Cavale: Ok. Thank you.

Randy Hargrove: We appreciate everyone's time today. If you have any follow-up questions, please give me a call or send me an email and we'll get back with you. Thanks for your time. We'll see you in October and in November, when we do our next earnings announcement.