Walmart's Fiscal Year 2014 Q3 Earnings Results
Media Call Transcript
November 14, 2013

Charles Holley: Good morning everyone, and thanks for joining us. As we've done in the last few quarters we have a guest with us today, and it is Bill Simon, the President and CEO of our Walmart US business.

After I make a few comments, I will turn it over to Bill so he can make a few comments. I will break down the quarter for you with our financial priorities: growth, leverage and returns. As for growth, you saw that we had $114.9 billion in sales. That was up $1.8 billion from the prior year, but if you dig a little deeper, which I think it is important to, there are two things that affect that.

First of all, if you look at our constant currency performance, and when we talk about constant currency we exclude the effects of foreign currency and we exclude the effects of acquisition. So when you take those two in to account, our revenues would have been up about 2.7 percent. Still, it was a tough sales environment but the sales were probably underlined a little stronger than you would have seen from the reported numbers.

When you break it down into segments as you saw, Walmart U.S. had a 2.4 percent increase in net sales with a relatively flat comp at -0.3 percent. Sam's Club had a 1.1 comp and 2.1 percent increase in net sales overall, excluding fuel, and Walmart International had a .2 percent increase in net sales but when you take into account the items that I just mentioned on constant currency, their net sales are actually up about 4.1 percent.

Turning to leverage, we did not lever. When I talk about leverage, I mean we grow our expenses at a slower rate than sales; however, we did make improvement.

We didn't leverage by about 8 basis points, but that's 22 basis points better than the prior quarter. So we feel encouraged by our progress. We are still very focused and very committed to a goal of leveraging our expenses more than 100 basis points improvement over a 5 year period starting last year, and we are very focused on that.

And finally returns, we had $1.5 billion in operating income. That's up about 1.7 percent, but again when you exclude the effects of currency and you exclude the effects of acquisitions, that would have been up around 8 percent.

I think we're very pleased how we managed the business. Again we know the sales were tough.

Let me turn to guidance for a minute. We did provide guidance for the 4th quarter of $1.50 to $1.60, but there were two distinct items included in that, that are important to note. The first was ending the franchise agreement with Bharti in India. That's dilutive of about 4 cents per share -- that's our expectation, and that's subject to regulatory approval. The next would have been that we plan to close around 50 stores in Brazil and China. That will be dilutive to our earnings per share by about 6 cents per share, for a total of 10 cents per share. We believe the adjusted or underlying EPS forecast, would be, then, between $1.60 or $1.70. You would take that same 10 cents per share and apply it to our estimates for the current year, the full year; and the full year guidance was $5.01 to $5.11. Adjusted for that 10 cents, obviously, it would be $5.11 to $5.21. With that, I'd like to turn it over to Bill. Bill, if you'd like to make a few comments.

Bill Simon: Thank you, Charles. It's great to be with everyone this morning. Walmart U.S. finished roughly where we thought we would from a sales perspective, at -0.3 comp, while delivering very strong bottom line results.

We were able to draw operating income 5.8 percent to over $5 billion.

Stores and logistics teams did a terrific job, as they have been recently, managing expenses and serving customers, and we were able to leverage by about 16 basis points.

Overall the quarter started a little more slowly than we would have liked, but we gained momentum through the quarter, and actually the last two months of the quarter were positive comps.

So we're seeing, we saw, an improvement throughout the quarter both in sales and in traffic. That was driven by some events that we ran, a Stock Up and Save and the October savings event which featured a lot of items that customers needed in the consumables area at great value.

We continue to invest in price; we also had some really good sales in our soft lines categories of home and apparel which helped the margin.

We're ready to serve customers in the fourth quarter, and we're excited about what's happening with what we believe to be our best holiday plan ever. We're pretty heavily invested in marketing and we believe we'll have the number one share of voice of retails each week during the season. We estimate about 25 billion impressions this year – that's a big number.

We also launched holiday specials on Walmart.com that you would have seen, earlier than we did last year. And this week you would have seen, we announced our plans for Black Friday and we're going to have nearly seven times the number of our one-hour guarantee items compared to last year. And some great, fantastic items including 32" LED TV for $98, and a 16 GB iPad Mini for $299 with $100 gift card. So we've got some great things and robust plans in place to help the customers during the holiday season. And we're encouraged by some of the momentum we've seen coming out of the third quarter.

Having said that, we know the customer will continue to be focused on their personal expenses and ongoing uncertainty about their personal finances in areas like health care and payroll taxes that happened earlier in the year. Most recently, we've seen the reduction in SNAP benefits – and I would tell you that it's too early for us to tell how that might impact our business going forward. And so we're focused on offering low prices to our customers every day. That's what we do, so they can stretch their budgets even further. And we're currently forecasting, because of some of the combinations of headwinds and tailwinds, a relatively flat comp in the fourth quarter. And now, Charles, I'll turn it back to you.

Charles: Thanks, Bill. Why don't we turn it over for questions.

Shelly Banjo, Wall Street Journal: Great, thank you. Good morning. I just wanted to ask about lower gas prices and basically flat to lower grocery prices. Whether or not that is helping, for the customer, offset any of the other weakness in the payroll tax and other kind of economic issues?

Bill: Thanks, Shelly. That's a great question. There's a lot of things happening in the marketplace today -- combinations of headwinds and tailwinds. And they're more difficult to forecast than they have been in quite some time because most of them we haven't seen before.

So the reduction in gas price will certainly help consumers. Flat to deflationary prices in dry groceries certainly would help customers stretch their budgets. On the other hand, everybody's still sort of trying to absorb the 2 percent payroll cut that happened before. SNAP customers are now trying to digest what might be a change coming there. Uncertainty out of Washington, and kind of a lack of clarity around what personal healthcare costs will be are also potential headwinds. So the combination of these things, I think, will make it more difficult to forecast the quarter. But I would say as we see customers and we talk to customers I continue to be amazed at their ability to process it all and figure out how to serve their families; and so we continue to try to be a part of that solution.

Shelly: And the weakness that you said started the quarter, that then picked up in the last couple of months, was that due to – can you quantify the effects of the government shutdown?

Bill: Again, it's really hard to do that. I can tell you that I don't believe we benefitted from it. I can't imagine any perspective that would have led us to do that. We did see a decline in sales around military bases, for example, as the civilian workforce there was furloughed. But again, it's really hard to process the data and give you a clear view on it. But I would say the continued noise and angst and arguing that goes on in Washington isn't good for consumer confidence, and so we'd strongly like to see those situations – budget and issues – resolved.

Anne D'Innocenzio, Associated Press: I wanted to follow up on Shelly's question: since there's so many different factors you cited for hurting sales, how would you rank them right now in terms of the biggest concern for your shopper? Is it the payroll tax, is it jobs, or is it – how worried are you about SNAP?

Bill: We do pretty consistent polling with the customers and the issues that they're telling us remain number one are around jobs and employment. Rising costs – food costs – I think that's more of a value thing, rather than inflation. Their income is going down while food costs are not. And then third, gas and energy prices, while they're abating, I think they're still eating up a big piece of the customer's budget. It's also one of the things I said earlier to Shelly's question – consumer confidence is an important aspect to retail, and I think until the issues are resolved that are making news these days, we're not going to see a very large rebound in the middle of the economy in consumer confidence.

Anne: Ok, and then can you just address the SNAP. I don't know if you can say – you said you've seen, or in surveys they're talking about it, or you've seen them pull back?

Bill: It doesn't come instantaneously, so that everyone's aware. The benefits are distributed at different points in the month depending on the person and their geographic location. And they're distributed in a lump sum typically, so that if they were reduced by some percentage, we may or may not see the impact of that until the end of the month, rather than the beginning of the month. So I'm not able to give you a view on whether or not there's an impact at this point. We look at historical data, and to be quite honest with you, when the benefits were expanded in 2009, our market share percentage of the SNAP benefits actually went down. So we look at that and we understand that when price is more important to the customer we have to be prepared to serve them. And so that's what we're doing.

Courtney Reagan, CNBC: Hi, good morning to you both, Charles and Bill. I just had a quick question: Bill, I typed out that you said just before you ended your comments, that you were encouraged by the momentum coming out of the third quarter. Are you able to explain that a little more? Does that mean you felt as if it was getting better towards the end? I just kind of want to understand, as recent as a quantifier or trend as you are able to help us with.

Bill: We did see improvement through the quarter. The month of August was the worst month of the quarter, and we saw positive trends, positive comps, in the last two months of the quarter and improving traffic. So the plan for us -- we said we're going to continue to be focused on price and invest in price. We have a terrific holiday program in place, so we're going to try to build on the closing success of the quarter.

Phil Wahba, Reuters: Good morning, everyone. Just a quick question on the layaway program. If you can give us a quick update on how that's going, and how many people have taken advantage of it so far and if it's more than last year?

Bill: The last number I saw was, as of the sixth of November, we had over 2 million customers take advantage of layaway – or 2 million transactions, I should say. Maybe somebody did it twice. It's hard to gauge the program versus last year because this year we have two new game systems – XBOX and PlayStation – that we're pre-selling, and the way we're physically pre-selling it is as a layaway item. They haven't been released yet, so we've been selling them as part of our layaway program. So it isn't really apples to apples to compare it, so I couldn't give you that.

Phil: And, how about in-store pick up? Are you starting to see people taking to that?

Bill: You mean site to store or redeeming their layaway?

Phil: Not about layaway, but ordering online and picking up in store. Do people like it so far?

Bill: We've been doing it for years. Site to store, and pick up in store, pick up today are essential portions of our e-commerce business. At various times of the year they can be well over half, and in certain stores they can make a big, big difference in the store's economics. It's a very popular program.

David Tovar: Our Site to Store program is not a new program, and we can get you some additional background on that, and some of the results we've seen in the last couple of years on that.

Christine Romans, CNN: Hi, everybody, and good morning. Bill, I wanted to ask you real quickly – you and I talked before about SNAP, and how you could conceivably see more of a customer's shopping basket filled by Walmart. It could end up being a slight positive, maybe, for you guys. But then at the same time, by the end of the year we have 1.3 million people who are going to be rolling off their unemployment benefits, and then that keeps happening through next year. How, as we're seeing, kind of the ramp down from the stimulus, some of these stimulus measures, how is that going to play out on balance among Walmart shoppers, your core customer?

Bill: You're asking the questions that we ask ourselves, with all of the economic noise – and these are sort of once in a generation things. We have historical data on almost anything, but most of these things haven't happened before. And, you know, I guess that's the difficult news. But the good news is, our actions are not any different regardless of what the issues are. We've got to be sharp on price. We've got to serve customers. We've got to focus on investing in price where we can to make our products more affordable for customers. And that's what we've been doing. And we think that when price matters, customers will turn to Walmart. I will say, and I have said publicly before: we'll do better and we'll perform better if GDP were growing at four or five percent. But we serve customers. And we have to serve them when there's growth, and we have to serve them when there isn't growth, and we're prepared to do that.

Ashley Lutz, Business Insider: I noticed that the Neighborhood Market format did really well this quarter, and I was wondering what the success of the Neighborhood Market format means for the company's strategy going forward. Will we see more of these? And what does this kind of say about the consumer and their mindset right now?

Bill: Our Neighborhood Market format's doing very well. We opened about 35 of them this quarter and we continue to open them. We'll have – for the first time next year we'll open more small stores than we will large stores as we continue to expand that format. The comp sales at our Neighborhood Markets were 3.4% for the quarter, and it's been very consistently in that range for us. And it's probably the best measure of how we're performing as a company against the rest of the grocery industry, because the mix in those stores are pretty typical grocery store mixes. So that's been a good format for us and you'll continue to see it expand. The customer likes it because of the size and they like it because of the access. It's in their Neighborhood – obviously, the name of the store – so it's closer to them, and it serves a different need than the big stock up trip that they take to the supercenter.

Andria Cheng, Marketwatch: Hi, Bill. So, we saw Macy's numbers yesterday, and then also today. Are you seeing a dichotomy in terms of the lower income shoppers versus the more average middle income class shoppers? Are you seeing a difference there in terms of the way your customers are spending and feeling about things?

Bill: You could interpret that and I could see how you could get there. But, frankly, Macy's – they're a great retailer and they had a great quarter. Our success, we had pretty good success in apparel and home, which are fundamentally the categories that Macy's operates in as well. So, there's a point of comparison. But I do think there's the opportunity for us to really talk about how we rebuild the middle class and focus on middle class jobs. And one of the reasons we've been so aggressively focused on U.S. manufactured products is we think about how to build that middle back. We believe that's a big opportunity. The economics of U.S. manufacturing right now are, again, once in a generation tipping point in the U.S.'s favor with low energy costs here in the U.S. and higher transportation costs overseas. The opportunity for manufacturing closest to the point of consumption is like it's never been. And plants and factories in Asia will continue to grow because the demand of consumers closer to those factories will begin to suck up capacity.

Andria: Ok, and then another quick question. Obviously every quarter and every holiday season we talk about competitive landscape. So how would you say for this holiday season, are you actually seeing more – or you know, is there any way, how it's different for this holiday season?

Bill: This is the time of year that we get our most fun. It's going to be about as competitive of a market as we've ever seen, I would think. Kind of a convergence of a lot of issues: the shortened selling season and the economic condition that the customer is under. You have retailers who are doing very, very well and want to press that advantage. You have retailers who need to do well in order to continue to serve, and so they'll be very aggressive. And we decided to take this opportunity to go very aggressive and support the customer in line with all those things. So you know, it's going to be very exciting.

Barney Jopson, Financial Times: Yeah, hi. Good morning, everyone. You said that your market share in the U.S. grew in the categories of food, consumables, health and wellness. What proportion of your total sales does that represent?

Bill: The categories that we measure that way represent about 55 percent of the sales in the U.S.

Barney: Ok, and were there any categories where your market share declined?

Bill: There were, yes.

Barney: Can you tell us what they were?

Bill: I believe we reported an area in our OTC business was down. I don't have that data, we'll follow up with you.

Barney: Ok, and then a broader question on the structure of the business. Can you conceive of a time when smaller stores and internet sales would be able to offset a decline in sales at supercenters?

Bill: Absolutely. I don't expect supercenter sales to decline, so that's kind of a hard question to answer. We do believe that there's still an opportunity to serve customers in a stock-up occasion and in a fill-in occasion, and that's why we're building small stores and continuing to build large stores. And then the connection of our digital platform to our physical platform, we believe creates an incredible advantage for us. And you'll see us testing pilots of some real exciting programs in that area next year.

Kim Souza, City Wire: Hi. I was just wondering if you would give us any color on the grocery delivery that you rolled out in Denver, and if you'd give us any indication on what the average basket ring is for your grocery delivery.

Bill: Yeah, I don't have that data with me, but we rolled out grocery delivery in Denver recently. We have had it in the Bay Area for a couple of years now, and we have the capability of rolling it out, really anywhere in the U.S. when the demand is there. We're just going to continue to pilot test and we're ready to go when the demand is there.

Shelly Banjo, Wall Street Journal: Thank you. I just wanted to ask a few more questions about holidays, in general. You know, ads, you guys started Nov. 1 online and others have started well before Black Friday. Can you talk about what the extension of the holiday selling season means for Walmart?

Bill: You know, that's not unusual. Several years ago we started earlier in November with promotions both online, programs online, and in stores. We're responding more to customer demand in a competitive retail environment. As I said, the compression of the season, the competitive nature of what's happening in the marketplace today, combined with a customer who's more value-focused than ever – it's a retailers' response to those activities. Our programs this year are very, very sharp. And very, very hot. We bought very deep on things like televisions and iPads, items that sold last year and have been selling all year. Tablets and consumer electronics, we're very deep on, and we'll sell a bunch of them on Black Friday and beyond.

Shelly: What about this idea, the managers' specials and localization? Is that to kind of offset some of that competition?

Bill: Yeah, that's exactly right. You know, managers will have the opportunity to take items, working with the buyers here in Bentonville that are relevant to their local communities and provide the customers with an opportunity to save on those items as well. So that's going to be pretty exciting. It's the first time we've done that.

Shelly: And one more question that I can squeeze in, if it's ok. In terms of online this year – obviously, you mentioned, there will be holiday specials on Cyber Monday. But will there also be online specials on Thanksgiving and Black Friday? And has that become a bigger part of the source of Black Friday, not necessarily just the stores?

Bill: We're an integrated retailer. So when we run an event, we run it online and we run it in stores. So we'll have activity online on Thanksgiving and Black Friday and we'll have activity in the stores on Cyber Monday. And we believe that is a competitive advantage for us.

Phil Wahba: I was never really good at algebra, so maybe you guys can help me. I'm trying to sort of figure out, if you guy's think that the ecommerce comp for the period – I thought that was a little low, and I'm just wondering, can you tell us more about how ecommerce grew during the quarter in the U.S.? Are we talking about 10 percent growth? I don't know what percentage of your overall sales come from online, and that's sort of the missing thing here, otherwise I could do the algebraic problem myself. But just wondering if you can give us a sense of how much better ecommerce trends were than the same-store sales were.

Charles: Hi, this is Charles. I think globally, what we said was it's grown over 40 – around 40 – percent globally. But that had the acquisition of Yihaodian in it; without Yihaodian, it grew about 20 percent globally.

Phil: Ok, and in this country do we know?

Charles: We haven't broken that down by country. We provide more detail when we print our 10Q.

Phil: Ok, great. Thank you very much.

David Tovar: And Phil, keep in mind that we've said that by the end of this year our ecommerce business will be about a $10 billion business, so you know – it's small relative to the size of the overall company.

Charles: And next year it'll grow to about $13 billion.

Phil: Ok, great. Thanks.

Randy Hargrove: Alright, thanks everyone for your time. If you have follow-up questions, please reach out to our corporate communications department. Have a good day.