Walmart's Fiscal Year 2014 Q4 Earnings Results
Media Call Transcript
February 20, 2014

Randy Hargrove: Thanks. Good morning, everyone. Thanks for joining us for our earnings announcement recap with Charles Holley. We're going to have about thirty minutes with Charles today; he'll have some brief opening comments and then we'll get to your questions. As usual, there's going to be a queue in order to ask your questions. We'll try to limit questions to one or two starting out and then we'll try to cycle through everyone and get back to you if you have an additional question. You should have a copy of the transcript; you should have copies of all of our press releases. There were three press releases issued today: earnings, there was a release on our dividend increase for the coming year, and then a release on the accelerated growth of our small store formats. So you should have all of those. I would like to keep the discussion today really focused on the business and if you have questions afterwards, Dave Tovar or I can help you out. So with that, I'll turn it over to Charles.

Charles Holley, Wal-Mart Stores Inc. CFO: Thanks, Randy. And good morning to everyone. Thanks for joining us. With me today is Bill Simon, President and CEO of our U.S. stores. And Bill's going to say a few comments after me and he'll also be available for questions.

First of all, just a reminder: we reported earnings of $1.34 today, EPS. That included 26 cents of discrete items. And what we mean by discrete, those are items that we may not have anticipated, nor do we anticipate would occur in the next years. And we stripped those out; we would call our underlying earnings per share of $1.60. Just a reminder, we had a pre-release where we talked about these items a few weeks ago. We said that we felt like our earnings per share would be at the low range of our original guidance of $1.60 or slightly below, and we actually came in at that low range of $1.60.

I'll say a couple of comments of highlights for the year. Obviously, currency for the year provided some headwinds for our sales. In fact, it was over $5 billion. Despite that, we still were able to increase our sales to $473 billion. eCommerce sales, I think, were a real highlight. They increased 30 percent to $10 billion. Now that includes acquisitions. Although that's a small number when compared to the $473 billion, it's the fastest growing part of our business and it's embedded in all of our operations.

Also, if you look at the U.S. – and Bill will comment further – we had a lot of impacts during the year and in the quarter, and they were negative obviously. If you remember, at the beginning of last year we had the reversal of the 2 percent payroll tax cut, we had the sequestration overhang, and then fourth quarter you saw the Supplemental Nutrition Assistance Program (SNAP) benefits reduced and then the very severe weather which we would not have anticipated.

You know, we did not leverage our expenses. Which means we grew our expenses a little bit faster than sales – we like to grow a little less than sales. The slow sales actually made it a little bit difficult to do that; however, I will highlight that the Walmart U.S. business continued a very excellent track record of leveraging and having very good productivity at the stores.

Our inventories were up about 2.6 percent on a consolidated basis. We feel, overall, pretty good about inventories. So we finished the year well and I think we're staged well going into this new year.

Also, as Randy mentioned, we put a dividend release out. We increased our dividends to $1.92. And just as a point of note: that's the 41st consecutive year that we've increased our dividend. As far as returning to shareholders, still a very large goal for us to make sure we have good returns to shareholders, we returned $12.8 billion this past year to shareholders in the form of share re-purchases (which were $6.7 billion) and dividends (which were $6.1 billion).

Looking ahead in our guidance, in October at our analysts meeting we had put out guidance of sales increases for this new year of three to five percent. Right now, we think it may be towards the low end of that, and one of the primary reasons is currency. The U.S. dollar continues to strengthen against other currencies in the countries that we're with, but that's always subject to change. At the same time, we had some headwinds that we didn't anticipate: healthcare costs in the U.S. (which Bill can talk about in a minute) and then some increased investments in our eCommerce business – between two and four cents per share. The guidance for this quarter is $1.10 to $1.20 and then for the full year, it's $5.10 to $5.45. A little bit wider range. And I think the primary reason is, in the short-term, given a lot of the headwinds we incurred in last year and in the fourth quarter, we're just trying to be prudently cautious. I think in the mid-term and the long-term, though, we're still very bullish on the consumer and where the economies will grow. And we do think we have great growth opportunities, whether it's our small stores in the U.S., our international growth or our eCommerce.

And with that, I'll turn it over to Bill Simon. Bill will say a few remarks and then we'll open up for questions. Bill?

Bill Simon: Walmart U.S. CEO and President: Thanks, Charles. Good morning, everybody. You know, as we finish the fourth quarter, I won't need to recap some of the challenges. I think you all are aware of them. We did grow top-line sales by about $1.8 billion. Comp was down about 40 basis points, as you would have read. About 30 to 40 basis points impact was from the change in the SNAP benefits we felt impacted us during the quarter. As well as the storms, which isn't an excuse but merely an explanation.

Given all that headwind, there's a whole lot to be proud of as well. As Charles said, we were able to leverage our expenses again. We had a very, very good holiday period. In fact, during the six weeks that ran from Thanksgiving to Christmas, we were positive comp and delivered very well for the customer. Really great integration on Black Friday weekend between our online businesses and our offline businesses, and terrific growth on Cyber Monday at Walmart.com.

I hope you would have seen the news, and Charles mentioned it, we had the opportunity to really begin to accelerate our small store program. We announced that in October, and since then we've been working at getting even better – more efficient with capital and speed to market. As such, this morning we've upped the guidance for our small store builds to 270 to 300 stores. These stores are really performing well. They compete really well against all the small store formats that are out there – from drug to dollar to small grocery and convenience. They, by and large, will be equipped with gas, fresh food. Even more powerful because they're connected to our eCommerce business digitally, so that you can get anything you want even at a small store.

We're pleased with some of the pilots that we have ongoing in that convergence of physical and digital retail that we talk about. Site to Store, Ship From Store, Pay with Cash, Lockers. You would also have read during this quarter that we expanded our grocery delivery pilot to Denver and more recently announced pick-up locations in Denver. You'll increasingly see us get more aggressive in that space.

We're optimistic about the business. As we said in the release, the first week or so of February was severely impacted by weather, but the underlying business – that is, markets that weren't impacted by weather and markets since the weather has cleared – gives us cause to believe that the rest of the quarter will be positive and that for the quarter our guidance would be relatively flat.

I'm going to kick it back over to you, Charles, and then we'll take questions.

Charles Holley: Alright, Randy, let's take it to questions.

Barney Jopson, Financial Times: Hi, good morning everyone. Let me be the one to ask you just to clarify your position on the minimum wage. Both in terms of whether Walmart supports an increase in the minimum wage, and in terms of what affect that would have on your business.

Bill Simon: With respect to the press that came in yesterday, I'm not really sure how that got to be news. Our position hasn't changed on minimum wage. We think that it's a good debate to have in the country and we have, where it's been equally applied in states and in jurisdictions, we haven't opposed it. The issue for us isn't really – and by the way, I do need to say this every opportunity I get: we're not a minimum wage payor, less than 1 percent of our associate base gets paid minimum wage. But the issue for us is, and you've heard us talk about this this year, it isn't so much where you start – and as the officials and politicians debate minimum wage, they need to keep this in mind. We need to have opportunity. It's really about how far you can go and less about where you start. So the start rate should be what the economy and the politicians believe the start rate should be. We're focused on opportunity and growth.

Barney Jopson: Can you tell me what you've learned from your analysis about how the benefits, of a perhaps increase in sales, would be offset by the increase in costs if the minimum wage did go up?

Bill Simon: We have. Looking back historically at when minimum wages went up, were able to absorb the minimum wage increases on our business because there is compression as those who are not at minimum wage would also get an increase. The lift from sales is something that is really hard to quantify. We'll be able to absorb an increase in minimum wage should it occur. We have in the jurisdictions where it's happened and – again, it's more of a political solution to an economic problem. The economic problem is opportunity and growth.

Shelly Banjo, Wall Street Journal: Hi, Bill. I wanted to ask you about the grocery. So it looks like grocery decreased for the first time in quite a while. I was wondering what the decrease stems from.

Bill Simon: Probably two or three things. How are you by the way? The first is, our mix of fresh to dry – because of the supercenter and the discount store mix in our business – is different than many other grocers. The dry and frozen areas of the business have had flat to slightly deflating prices, while our fresh business – much like everybody else's fresh business – had some slight amount of inflation and actually had pretty good comps. Our mix of fresh to dry, and our overall grocery business as we report it, is what drove that. So it's a combination of deflation in categories where we're large and strong, and then of course the impact of the SNAP and 2 percent over the course of the year.

Shelly Banjo: And then, I wanted to ask you about the increase in stores. So this quarter, Walmart has the second straight year of negative or declining traffic in U.S. stores, and I'm wondering why Walmart is one of the only retailers adding more stores even those less and less people are coming through your current doors?

Bill Simon: It's interesting. Good question. You know, our stock-up trip – which is what the supercenter does so very well for the customer – is actually pretty robust. The basket size is growing and the customer still comes to us for that large shopping occasion. Where we've slipped in traffic, and it shows up in the supercenters, is the fill-in occasion: the mid-week trip or the smaller basket size. Because of the increased competition and availability of products at competitors. We see the exact opposite of that in our small stores. Traffic is up, you know, very robust traffic increases. Our Neighborhood Markets had around a five comp in the fourth quarter and 4 comp for the full year, which is really in the top-tier amongst grocery competitors. That's why we're expanding and really stepping on the pedal on the small stores, because we believe we can complement the real powerful stock-up trip in a supercenter with a fill-in trip to these small stores.

Anne D'Innocenzio, Associated Press: Hi. Bill, can you clarify a little more about the economic headwinds? It's interesting that the payroll tax, which was implemented a year ago, is still having an effect on shoppers. And then the reduction in food stamp benefits – of course that's new. But can you clarify a little more about the economic headwinds for us, and then what you're doing in response to the reduction of food stamp benefits? How are you getting shoppers to spend more?

Bill Simon: Sure. The 2 percent payroll impact that happened a year ago January is largely in our base today. So we know that will be with us forever, it's built into the overlap. So it's less of a headwind than it was. The change to SNAP benefits is really interesting because of the way that it's delivered on the particular card, it's very measurable. So we can see what happened there – it's a reduction in the customers' subsidy on food. And we can track that. We believe we've got one quarter behind us, one quarter already in the base, and we'll have a little bit of a headwind with that for the next three quarters.

You know, weather is what weather will be. Sometimes it's in front of you and sometimes it's behind you. It's been, as we all know, a particularly unusual winter. I think we've done as good a job as we could of staying in stock and keeping stores open as long as we could. We did have 200 to 300 stores closed at various points between November and February because of the storms. They're all open today, thankfully, serving customers. But it's a challenge, and it continues to be.

The customer remains resilient. We're able to serve them by taking advantage of the offerings and the features that reflect what their changing spending habits have been: smaller pack sizes, change in proteins – we've talked about some of this stuff before. But I continue to be impressed, and I've said this before, the customer figures out a way to take care of their family, how to have a good Christmas, how to celebrate Valentine's Day. They know what they're doing and how to manage their money accordingly and we try to help them with that.

Anne D'Innocenzio: Ok. Thank you.

Phil Wahba, Reuters: Hi. Good morning. Ok, one question I have for you has to deal with the omni-channel. Can you tell me a little bit about what you guys felt was – things that you've tested that are still on a small scale or you may still role out – which found the most favor with customer. And which do you think still need more tweaking, like in-store pickup. What would you say was the omni-channel homerun for you guys during the holiday season?

Bill Simon: Oh gosh, there was some really good progress. Probably the most impactful that many would not have recognized was an omni-channel play was the One Hour Guarantee program on Black Friday weekend. We filled orders from stores until we ran out of stock at the store, and then we flipped instantly – seamlessly – the customer to online to Walmart.com and fulfilled the balance of the orders from our Walmart.com fulfillment network. That's the only way you could really deliver that sort of a promise because you can't balance your inventory to make sure it was at every store in the right quantity. So we sold what we had in the store and we instantly were able to flip to Walmart.com and that's a capability that I think will serve us pretty well going forward.

The grocery delivery test – the pickup in Denver – while still very small and in early stages, has 90 percent customer approval, so we're pretty encouraged about that. Lockers in the D.C. area for pickup have been met with pretty high customer satisfaction. Site to Store, which is not a new program, but Site to Store combined with Pickup Today (meaning you can get the item available almost immediately in the store) has really had an impact across the fleet, but particularly in the smaller stores. We see some stores over the holiday season where the Site to Store or Walmart.com orders picked up in stores could approach 50 percent of the sales of the store. So we're able to do things and learn things that I think will benefit the customer as we go forward, and you'll see us continue to experiment and then you'll also see us start to roll some of these things out.

Phil Wahba: And, if I may, just a quick question about the accelerated expansion of the smaller formats. Do you think there will be push back from communities in some of the areas that might not have a Walmart about the smaller format? Or is the idea that the smaller stores are generally close to supercenters? Is there any risk of pushback from communities?

Bill Simon: I can't answer that question. Typically, small stores are easier to site. Their land is not particularly huge, their sites are available – many are already entitled because they're in development. So placement is typically easier. From a customer perspective, our customer experience stores are significantly higher in the small stores than they are in the large stores, which indicates that the customer likes them better. If the customer likes them better, then typically the community likes them better. But I can't tell you that there won't be a place somewhere where somebody might not.

Phil Wahba: Thank you.

Courtney Reagan, CNBC: Hi. Thanks for taking my question. Good morning, everyone. Bill, I'm wondering if you're able to provide us just a little bit more color on what you're seeing in regards to tax refund activity? When you're seeing it, what impacts you might think it's having, and potentially the outlook going forward. I know that was something that was considerable at this point last year. Thanks.

Bill Simon: It was. Thank you, Courtney. It's a big number for us. It started out late, I think the IRS would confirm this, but we started seeing checks come about a week later than we did last year, which was part of the issue in the first few weeks of February that I talked about already. Since the checks started flowing – and right now they are still slightly behind where they were last year – sales have been pretty good for us. So year on year we're neutral – we're behind, but on a day to day basis we're neutral to slightly behind in the disbursements. And we project that if things continue on the trend from last year, it'll probably last a week or so longer and we'll catch up. So I think we're seeing customers spend slightly less – I read a release from the National Retail Federation this morning that would support that – slightly less of a percentage of their check when they cash it and save or pay down debt on slightly higher percentage. But it's too early for us to say what sort of impact that will have on the business. Right now, we're slightly behind in total and right on on a day-to-day basis as we see the disbursements relative to last year.

Courtney Reagan: Thank you.

Julie Hyman, Bloomberg TV: Thanks for taking my question. Bill, you had mentioned that you did expect comps to improve in the current quarter given what you're seeing so far. At the same time, the forecast for earnings came out a little low for what analysts had been looking for. And I'm just curious, if you guys are increasing your aggressiveness on price and that is driving some of the traffic and that's also responsible, maybe, for a little bit of the earnings miss. In other words, how willing are you all at this point to give up margin in order to drive traffic and sales?

Bill Simon: Thanks for the question, I appreciate it. As you can see form our fourth quarter, we invested about 40 basis points in price. We grew market share in the fourth quarter, in fact for the year, in most categories that we measure. So we're focused on making sure that we are taking care of the customer and building market share. Some of the headwinds in the business are, from an earnings perspective (on the U.S. side anyway), related to healthcare costs and just a sort of reset to par on the incentive that underpaid in the previous fiscal year. I think if you would take those things out and adjust for that, you would find us still to be in a leveraged position in the U.S.

Randy Hargrove: And I think we'll have time for just a couple more questions. We've got some in queue.

Andria Cheng, Marketwatch: Hey, Bill. So regarding the expansion of the small format stores – obviously it is still kind of a drop in the bucket compared to the big dollar store chains. So what's your thinking regarding, maybe, time for Walmart U.S. to acquire for growth?

Bill Simon: Well, we always look at opportunities to acquire. And don't be so sure it's a drop in the bucket compared to the dollar chains. Our small stores are approaching total size, in dollar sales, of those chains and we'll aggressively add to that this year. Our stores, from a location and from a physical footprint, aren't exactly what we see in some of those dollar chains. For example, we believe fuel is very important in all of those locations. And so as we roll them out, virtually all of them will have fuel. Fresh and frozen are really important to us as well and need to be a part of it, as well as pharmacy. And so you'd have to take the premium that you'd pay for locations that are not perfect, and then the cap ex that you would then have to plow into retrofitting fuel and refrigeration, and then assess whether the speed to market – what you could keep from a regulatory perspective and whether the math works. And to date, we've found we can open 300ish a year or maybe more, we can build those formats pretty aggressively. Keep in mind, now, our smallest format – Walmart Express – probably does four times what a typical dollar store does in sales, three to four. And our Neighborhood Market format does six to seven times what a dollar store would do, maybe even more. So we're able to build the sales with fewer physical footprints if we get the box that we would like. And that's why, while we look at acquisitions, it's really hard for us to find one that might fit what we need.

Andria Cheng: Ok, thank you. And then can you guys talk about what the comp performance for the Express is? I know it's very small, only 20 stores right now.

Bill Simon: Yeah, there are 20 of them. There are only 12 that are on comp, and they've ranged throughout the year from double digit to mid-single digit.

Andria Cheng: Great, thank you.

Shelly Banjo, Wall Street Journal: Thanks so much, I just wanted a quick follow-up on the healthcare costs. Can you just clarify that a little bit? I was having a hard time understanding why the higher than anticipated enrollment in your health plan, how it relates to the Affordable Care Act?

Bill Simon: That's a great question, too. So are we, I guess would be the answer to that. Our benefits package, in all the time that I've been here, changed the least in this fiscal year. From fiscal year to fiscal year. We had already, and we had told you this, our benefits offering far exceeded what was required by the Affordable Care Act. So we weren't anticipating any significant cost increase because of the Affordable Care Act. What surprised us, I suppose, was that, relative to the other offerings associates had – and you could argue whether this was Affordable Care Act-driven or not – they realized that they were now going to be required to enroll, our benefits to the cost were relatively better than anything else they could get. And we saw a significant spike in enrollment. So the largest portion of the healthcare cost headwind is related to healthcare enrollment by our current associates in our health plan, which hasn't changed. So I think it's just the relative value of our health plan compared to the other options that they may have had or may have been buying in the past.

Randy Hargrove: And this will be our final question.

Kim Souza, City Wire: Hi. I've enjoyed watching your commercials featuring Mike Rowe during the Olympics, and I just wondered if you might give us a little color on any feedback you've gotten from that, and if we can expect any more ads like that coming from Mike Rowe – even if he's taken a little bit of flack from that from the entertainment community (it doesn't seem to bother him though). And also if you could give us any color on the traction that program is getting and what we can look forward to in the coming year.

Bill Simon: The U.S. manufacturing program has gotten a real good start, and a fair amount of momentum. We've been pretty pleased with our suppliers' reaction and the customers' reaction to the products when they're in the stores. This isn't a PR thing, it's a math thing. The economics are very favorable right now for manufacturing certain products in the U.S. And sort of related back to the first question on minimum wage, the ability to build opportunity and growth jobs in the manufacturing sector is so key to the economic recovery in this country. And we're so happy to be able to participate in it. With respect to the ads, we do plan to continue that campaign for a while. Mike Rowe is a terrific person and did a good job as a voiceover for that ad. He's not a paid spokesperson, he just really cares about working people in this country and agreed to do the ad for us. Whether he'll be on future ones, I don't know. But we will continue the campaign for a while, it's been very well-received.

Randy Hargrove: Great. Thanks, everyone. We appreciate your time. If you have any follow-up questions, reach out to me or to Dave. And we'll look forward to seeing you next quarter.