Raymond James Institutional Investors Conference

Company Participants

- Bill Simon, Mart Stores, Inc.

Other Participants

- Budd Bugatch, Analyst, Raymond James
- Unidentified Participant, Analyst, Unknown

Presentation

Budd Bugatch {BIO 1504748 <GO>}

Good morning, again. My name is Budd Bugatch. I am with Raymond James and it is my pleasure to welcome you to the Walmart presentation at our 34th Annual Institutional Investors Conference.

With us today from Walmart and we have Bill Simon, President and CEO of Walmart U.S.; Brett Biggs, he is EVP and CFO of Walmart U.S.; and Carol Schumacher, Vice President of Investor Relations for Wal-Mart Stores, Inc.

We are happy to welcome Bill back to the state of Florida where he served as the secretary of Florida's Department of Management Services during Jeb Bush's tenure as governor. He joined Walmart in 2006 from Brinker International. Bill was named President and CEO of Walmart U.S. in 2010.

Bill, without any further ado, the floor is yours.

Bill Simon {BIO 15112481 <GO>}

Thank you, Bud. Appreciate it. Glad to be here with you today.

It is an opportunity for us to talk about our business, which we like to do, particularly given we just released our earnings on the 21st. Not too long ago. I'm going to take a moment, if I can, to recap some of that for you and then spend some time talking about some of the initiatives that we have. Give you a little more insight into some of the things that we are thinking.

But first, of course, the forward-looking statement. We will be making forward-looking statements. I think that is why, hopefully, some of you are here so you can hear what we think about the business and how it is going. If you would like more details, it is on our website and you can take a take a look at it.

Just to recap, our business at Wal-Mart Stores Inc., the corporation, is strong and growing. We added $22 billion for the fiscal year that we just completed. Added a Fortune, what, 50 company in a year. Leveraged the business; in fact, all three of the operating segments delivered operating leverage this year and this is the third consecutive year.

Free cash flow of about $13 billion. Returned about $13 billion to shareholders in part with a fairly substantial dividend increase. A great result for the year and part of it, for me, representing the Walmart U.S. team is a bit of pride because the Walmart U.S. team was a contributor to that great result.

If I can I will really just bring you up to date on the strategy in the US. You have you had seen this; it is our productivity loop. That is the business model that we operate, that is the business model that has been successful for us, that is the business model that delivered a great result in the US this last year. And for us it starts with leverage.

If we can leverage our expenses. And this year we drove down our expenses by 27 basis points, it frees up cash for us to invest in price. We did very broadly invest in price, primarily in food and consumables because we know that is a traffic driver in our business. And the result was a growth in our sales. And we are back around to the beginning with initiatives and prepared to drive leverage for the year.

Just a little bit more detail. The US segment finished the fiscal year at $275 billion in sales. Very, very strong, a 1.8% comp. We added about $10 billion in top line for the business. You all may know that we recently began to re-subscribe after about a 10-year hiatus to Nielsen and IRI point-of-sale data. And that data is indicating that we grew 50 basis points in food consumables and the health and wellness over-the-counter areas that we measure. 50 basis points on a strong share. So a great performance driven primarily by traffic.

Facilitating all of that, as I said, was operating expenses and our operating expenses increased by 2.5% on just under 4% sales growth, the net of which is $22 billion in operating income. $1 billion increase in the US in operating income for the year. Profit growing faster than sales in each and every quarter, a very good result for us.

We, in the company, have a history, established by our founder, of sharing that success with our associates. In addition to the normal wages that we pay our field and management teams we paid this year nearly $1.5 billion in field-level incentives. Every hourly associate in our store is eligible for a bonus, a quarterly bonus. And we paid out $1.5 billion in bonuses this year just to the field-based folks.

Additionally, they have access to discount cards. About $550 million that they took advantage of discounts in our stores and over $800 million in contributions to 401(k) and stock purchase plans. So combined, in addition to regular base pay, nearly $3 billion given back to the people who made this happen for us and we are proud to be able to do that particularly at a time where the economy remains challenging.

One of the questions we get asked and so I thought I would address this upfront is what's on the top of mind of our customers. Our proximity to the customer base that we serve with about 140 million customers coming into our stores every week and the polling and Walmart Mom groups that we manage give us a pretty good window into what folks are thinking. Now more than ever they are telling us that they rely on us for that low price, Every Day Low Price promise, particularly as things get a little bit uncertain.

The customer continues to be pressured by jobs, jobs, jobs, jobs. Unemployment and security they tell us is top of mind. They started to mention the payroll tax increase. They noticed that 2% in their paycheck.

Most of them say they are adapting to it and are figuring out how to work their way through that. Maybe a lesson for those in certain parts of the government. If our customers can figure it out, well, maybe there is hope.

Gas prices are also -- they are very sensitive to that. Rapid run-up in gas prices that we have all seen is something that is on their mind.

What we know, though. And what they tell us is they continue to rely on us in difficult times and we are well-positioned really in any market place to serve the customer. The strategy of Every Day Low Prices fueled by that productivity loop is what runs our business.

It is really pretty simple. It is the program that Sam Walton developed and was expounded on over the years and now has evolved into grocery for us. If we can invest in price on food and consumables, we drive traffic to our stores, which will give us leverage, which then allows us to continue to invest in price.

And those price investments -- and lots of folks are out there and they do price surveys. We do well in most of them, some of them better than others.

Our price investments are very, very broad based. They are not KVI, or known value item, driven. Not milk, bread. And eggs particularly. But more broadly against items that drive a basket savings. They can be sometimes difficult to read if you are out there doing a survey on 50 items or so.

And the unique position that we have in the marketplace has showed up in the market share increases that we have. We are also talking to the customer about that.

Many of you would have seen the ad campaign that we are running now. There is a national campaign that is more broad in its claim and then we will be expanding into 50 markets in the First Quarter with direct market-specific basket claims. And I brought one of those.

(video playing)

Those ads, as I said, running in 50 markets. You will notice that was a neighborhood market and I will talk a little bit more about that later. We are increasingly rolling out that format and it has been very successful for us.

But those challenge campaigns are real baskets, real customers taking and shopping in the same list. So we don't pick the items. There could be anything from milk, bread, eggs, in there are to black shoe polish. Whatever they bought we run the comparison against and we do very, very well.

We also have made a lot of progress this year in anytime anywhere shopping, driven by our online business. We occupy a unique position in e-commerce. Based on the 4,000-plus store infrastructure that we have in the place and our logistics infrastructure, we have the ability to do things that the customer finds a lot of value in.

A couple of examples of that I will give you because they are very top-of-mind given the recent holiday season. We are able to stay in stock and in business through Walmart.com really all the way up till Christmas Eve when most traditional e-commerce players are out of business because of the shipping deadlines. Because of the 4,000 stores we can fulfill the orders from our business on the ground, either through a fulfillment from store or a pickup in store opportunity that others might not be able to do.

Another great example was many of you would have heard about the one-hour guarantee that we gave our customers on the most sought-after items on Black Friday. We were able to oversell what we had in the store and fulfill it within days through Walmart.com. So the customer who came in and wanted that 32-inch TV for $148 we sold about 600,000 of them in about an hour in the stores. But we actually sold more than that. Another 100,000 or so and then to fulfilled them through Walmart.com.

So that integration of physical and digital retail is a place where we believe we have a huge opportunity and we will continue to expand on that. We have also online been innovating to deliver the customers' needs. You would have hopefully read about our new Polaris search engine, which, by the way, was completely developed internally. So we now have the engineers or the capability to develop a world-class search engine that is resulting in conversions from Walmart.com and all of our e-commerce businesses are at a much higher rate.

We launched this past year Pay with Cash and had some really interesting results with it. Pay with Cash was a way for customers who we thought without credit to participate in e-commerce sales. And low and behold, we found out that a substantial portion of the pay with cash business was actually paid with a credit card.

Pay with Cash, you go online and you order the product and then you go to a store and you pay. Well when they showed up in the store to pay a substantial number of them use credit cards to pay in a store, which will give you the idea about there is still some people out there who aren't quite sure about that whole Internet credit card thing. At least that is what we believe.

Site to Store has been expanded for us with pick up as early as today we call it. So now you can order online and get it now in the store.

We were very, very fortunate and pleased to be named mobile retailer of the year. Some of the activity we have been able to generate through our mobile application, things like Scan & Go that is in pilot now where you can mobile self-checkout on your smartphone. As you all know, you heard we launched a same-day delivery pilot and are very, very interested in that as a concept to service for our customer.

The bottom line is anytime, anywhere. And we are able to do that. The idea is that we can expand our reach and deliver our low price, Every Day Low Price promise to customers wherever they might be.

I am going to transition a little bit and talk to you about our real estate portfolio and how we think about supercenters and small formats. It is important because you will see us, as the chart on the bottom indicates, increasingly moving into smaller formats. Just to be clear, when we talk about smaller formats we are talking about anything below, say, 50,000 or 60,000 square feet, non-supercenters. So Neighborhood Markets and Express Stores would fall into that category.

Just so everybody is aware as well, 90% of our fleet are Supercenters and Supercenters are still a great growth vehicle for us from a dollar perspective. And we will continue to build those where we see the opportunities. We have given you those real estate numbers and they are on this chart as well. We will add about 125 new supercenters this year.

You can see the rate at which we are expanding our small formats and it is a very -- a rapid ramp up. I'm going to explain to you in more detail why and why we are so excited about that. We will build as many as 115 small formats this year. And we have seen that fleet grow to, as I said, to be about 40% of our new openings.

We are excited about it because they compete really well against multiple channels. You may think of Neighborhood Market as a drugstore or a grocery store competitor or Express as you have thought about it as a dollar store competitor. Well they are not really.

They are more hybrid stores than you would think, because they have, obviously, our low price promise but they all have fresh food and pharmacy and the Walmart Every Day Low Price promise. They are enabled with dot-com capabilities, Site to Store capabilities. So you have that endless aisle that we can offer that others might not be able to offer.

So if you sort of put it up against each of these channels that they compete with, against the dollar stores while the prices -- dollar stores we still have a price advantage against them. They are known for their price as well. But we can deliver price and assortment and fresh food and Rx and the Walmart EDLP promise. And then give you anything that we can get online in the store. That digital capability is a deal breaker.

Against grocery our prices are -- traditional grocery our prices are much, much better. As you see in the advertising campaign that we are running, our Walmart brand is also very important.

Then, again, enabled with e-commerce capabilities that most traditional grocers can't and don't compete against. Then against drugs obvious price advantage, fresh foods. And then the dot-com piece. So we have seen our small formats compete very well against every one of these channels and deliver sales that we are very, very proud of.

Just as an example, in pharmacy and over-the-counter we have high single-digit positive comps in these small stores with strength in OTC and Rx. Rx driven by our $4 generic program. Grocery, on the grocery side the small stores are mid-single digits with strength in fresh and deli, bakery, exactly where you would think they would be.

And our GM business, in the consumable parts of GM, like light bulbs and air filters and things like that, we are able to fulfill the order right then and there. But some of our stores, these small stores have a very, very high percentage of Site to Store sales.

There is a store in downtown Chicago, a Neighborhood Market at the bottom of a tower, that has at times of the year up to 20% or 25% of its sales are done through Walmart.com and Site to Store. In fact. So much volume is done there that we had to rent more space from the landlord just to be able to store the products that were shipped to the store through Walmart.com. It is a terrific story for us that has resulted in very, very good growth across our formats.

The Neighborhood Market for fiscal 2013 delivered mid-single-digit positive comps against the competitive set that you would think as good as or better than everybody in the traditional grocery space. Traffic is up 2% every quarter. Strength in every one of the categories.

And for those who know the history of Neighborhood Markets we started in the late '90s with Neighborhood Markets and built them in year groups, for example, all the way through this recent year. The growth and the positive comps that we have been delivering this year were in every single year group. So even if you go back to the '99 year group they had positive comp. In the 2003 year group they had positive comps.

Of course, the more recent ones, because of the velocity and build up, had better comps. But we are really pleased with the entire fleet and the comps that they have been able to deliver.

Walmart Express double-digit positive comps. And while there are not a lot of them on comp yet, we are very, very pleased with the result that they have been delivering. Positive traffic every single quarter.

The Rx portion of this has been very, very important. If you can deliver prescriptions to markets, access to low-price prescriptions into markets that haven't had access to them before it is very, very compelling from a traffic and a customer perspective.

The assortment in these stores is really interesting, too, if you think about it. If you are at a 12,000 or 15,000 square foot, say, drug or dollar chain and you have the ability to assort your store based on your distribution network, which might be two times the number of SKUs. So say you carry 10,000 SKUs in the store, you may have 20,000 or 25,000 in your distribution system. So when you go through your assortment calculations and you try to figure out how you should assort that small store you are limited to what you carry in your system.

At Walmart we can assort a 12,000 or a 15,000 square foot store with the entire assortment from a supercenter, a 600,000 distribution system. So the best-selling items at an adjacent Supercenter can be assorted into a Neighborhood Market or an Express store. And that is a capability we have that others don't. Then when you take that to the next level with the digital capability through Walmart.com that has been a very, very powerful customer proposition.

Neighborhood Markets, we are in a rollout mode on this. We have direct line of sight to 500 by fiscal 2016 and we have been able to decrease the building costs. We are seeing, as I said, improved sales trends. Productivity, because as we scale these things has built the return so that they are now in line with approaching Supercenter-level returns. So we are very, very pleased with this.

You can see geographically where they are. We will be building out penetration in many of these markets and there is a few new markets that we will be going into this year as well. This is a great opportunity for us. 500 is by no means the end; it is merely just the beginning of what we think the opportunity might be for this format.

With Express we are in the middle of a density test. If you have been in any of North Carolina recently around Raleigh-Durham you would have seen us building a lot of these. What we are trying to understand here is what happens when you put a lot of these in close proximity.

Again, these are not dollar stores as you would think of them or drugstores. They have a volume, a sales volume that is fairly substantial compared to a dollar store -- 5 to 8 times what a dollar store might do. But only, say, 30% or 40% of what a Neighborhood Market might do.

And so the density test for us is to try to decide where and how many we can put these. Do you use them as a filler strategy or a penetration strategy? One of the things that we want to make sure that we don't do is put a 15,000 square foot store where we should have put a 35,000 square foot store. And so we are learning a lot from this.

We are actually learning a lot from Express that we are now applying to Neighborhood Markets about building costs and discipline with capital. And that is making us better on all of our small formats.

While I have you as a captive group, I am going to take the opportunity to talk to you very briefly about some of the things I am most proud of with our company and that is the things that we are doing to lead on issues that matter to our customer.

In January, we announced that we are going to step up our commitment to US manufacturing by adding $50 billion over the next 10 years in US-manufactured products. The equation is changing very, very rapidly with higher oil costs, transportation costs. And emerging demand in markets that are outside of the US. So that manufacturing equation is changing. There are categories of products that are ready to come back to the US.

With our access and visibility a lot of the manufacturers in the US and in the world and a lot of the state and local governments, we believe we are in a position to make some commitments, longer-term purchases, working with state and local governments to bring this manufacturing back. In fact, later this week we will be at a summit with our suppliers where we are going to be discussing this in detail. It is a very, very exciting opportunity for us. And we are focused on it.

We also talked about veterans jobs initiatives. We believe, like everybody in this country, that if you fought for your country you shouldn't have to fight for a job. Veterans are great workers; we know that. They deserve an opportunity. We are going to give them that.

But we believe that -- if you think back along the history of our company, every single time we have had a conflict the veterans have been the ones that lead an economic boom after the conflict was over. Happened after World War I, happened after World War II, happened after Vietnam. We have 10 years' worth of veterans right now and they are one of our best hopes for the next phase of growth in the US.

So if you have left active duty within 12 months with an honorable discharge and you want to work for Walmart we are going to give you a job. We have also called upon the top 50 employers, many of whom are already very heavily engaged in this. And we're going to see if we can't get a broader commitment from America's businesses to employ our veterans. Because that is one of the ways that we are going to get the economy growing again.

Of course, we are still very, very focused on sustainability. We are very proud of the zero waste initiative, our journey towards zero waste. We are at about 85% and we have been able to divert 85% from landfills today. We are now the largest on-site user of renewable energy and solar fuel and wind.

Of course, we are still focused on women's empowerment, our ability to attract and retain internally top female talent. Then the establishment and the development of women and women-owned businesses all around the world is something that we are focused on as a company.

Briefly wrapping up, we had a great year, both for the corporation and the Walmart U.S. segment. Our strategy in the US is right on and working. We are very pleased with the productivity loop and how it continues to move forward.

We think whatever the economy does we are the best-positioned retailer in the US to serve our customers. And we are very, very excited about the opportunity to reach more customers with our Everday Low Price promise that these small formats give us.

So with that, Budd, let's see if we got any questions.

Questions And Answers

Q - Budd Bugatch {BIO 1504748 <GO>}

We do have time for some questions from the audience. Who would like to start us off? Anybody? Bill, let me ask you a question on (multiple speakers).

Let's start at the end of that last comment about you were the biggest user of renewable energy sources. How do you calculate that? Is that just by virtue of your size or is this energy that you generate on-site?

A - Bill Simon {BIO 15112481 <GO>}

I guess, if I understand the question, we have solar installations at well over 100-plus of our stores today. We just expanded our solar installations in Ohio. The roofs are big spaces where we can gather a lot of solar.

We are one of the initial customers of a company called Bloom Energy, which is fuel-cell technology in the Bay Area where we have now got I think more installations than anybody does. And that is a fuel cell sort generation of power on site.

We are business people. So these are great business opportunities and returns for us. While they are great for the environment, we believe in the long term we will result in a cleaner planet, it is good business for us. We generate this power on site.

They are in different forms and fashions with power usage agreements with the owners of the products. So there is not a lot of capital outlay. Some of the deals are slightly different. But by and large we have solar wind and fuel cell installations on our properties, stores, clubs. And distribution centers.

Q - Unidentified Participant

I presume these are generating returns. This is cheaper than buying off the grid?

A - Bill Simon {BIO 15112481 <GO>}

Yes.

Q - Unidentified Participant

Just curious, going back to the slide where you were showing the evolution of what percentage of your stores are going to be under the large versus smaller format, do you foresee your square footage in total staying about flat or do you think that it will be in decline?

A - Bill Simon {BIO 15112481 <GO>}

I think what we are trying to do is to do more with less. So we are trying to become more efficient in the use of capital. So the square footage will roughly stay the same. But you will see more doors open because we are going to be opening smaller stores instead of Supercenters.

Q - Unidentified Participant

Can you talk a little bit about the impact to labor costs over the next, say, three years from Obama Care and will that be significant to the Company?

A - Bill Simon {BIO 15112481 <GO>}

The Affordable Care Act, like it or don't like it, it is the law of the land. It has been argued all the way to the Supreme Court and we are prepared to implement it. Our healthcare benefits were well above what was required by the Act anyway. And while there is some bulges that are not where we were spending the money, we feel like we can absorb that in our business.

Q - Unidentified Participant

On the other side of that is there any way you can benefit either from minute clinics or Rx from the healthcare reform?

A - Bill Simon {BIO 15112481 <GO>}

They are probably is and we are working towards figuring what that is. But I don't know if it is a benefit from the change in the legislation so much as it is the opportunity to benefit from the increased demand and relative scarcity and high cost of healthcare in general.

If you think about our business model, any time that there is an inefficiency in the system. And there is no better poster child for inefficiency than the US healthcare system, we believe there is an opportunity for Walmart. So I am not sure that I can answer your question that as a result of the law there is a big opportunity for us. But there is a huge opportunity for us in that space and we are pursuing it.

Q - Budd Bugatch {BIO 1504748 <GO>}

You were instrumental in the $4 prescription. What is the progress of that now? It has been in place for, what, five or six years?

A - Bill Simon {BIO 15112481 <GO>}

Yes. We launched it in the fall of 2006 and you know our market share in Rx increased substantially with that. I don't have the latest dollar amount. But we have saved billions of dollars in healthcare costs.

If you really think about it. And if you are really, really honest, it is the only thing you can point to that has actually lowered the cost of healthcare in the US. Everything else just moved it around; the Affordable Care Act and changes to Medicare or Medicaid and everything. This just lowered the cost of healthcare because we did this and then about 30,000 other locations in the US matched us. And that is great, that is a wonderful thing.

2006, before 2006 the timeframe, if you recall people were talking about having to cut pills in half and going and importing drugs from Canada because they were too expensive in the US. Not talking about that anymore. We just lowered the price. And by the way, we still make really good money at $4. The cost of goods of those things it's not all that complicated.

And so there is an opportunity for us to take that same mindset into the healthcare space and, frankly, other services as well where there is a disjointed nature and inefficiencies.

Q - Budd Bugatch {BIO 1504748 <GO>}

One last question, there was an article I think in one of the reporting services yesterday about your doing something with Amazon or trying to get through the partnership. Is there anything you can talk about on that at this point in time?

A - Bill Simon {BIO 15112481 <GO>}

No. That article and that particular publication and that particular reporter got a hold of something that is now about six weeks old that I think she is just trying to continue to write about. That was the same story that you read about about an e-mail that got out of our company.

By the way, just for perspective, we generate -- and this is shocking to me when I found out -- about 10 million e-mails, external e-mails, not even the ones that I send to Carol or Brett, 10 million a week. So since that person got a hold of that e-mail we have had 50 million more e-mails than that. That was a snapshot at a day and time that isn't even really relevant anymore.

So the Amazon story, I would tell you, is probably an interpolation of an interpolation.

Q - Budd Bugatch {BIO 1504748 <GO>}

Okay. Thank you very much. We will continue at the breakout. Thank you, Bill.