Goldman Sachs Global Retailing Conference

Company Participants

- Dave Cheesewright, Mart Stores, Inc.
- Matthew Fassler, Analyst

Other Participants

- Irma Sgarz, Analyst, Goldman Sachs
- Rob Joyce, Analyst, Goldman Sachs
- Unidentified Participant, Analyst, Unknown

Presentation

Matthew Fassler {BIO 1509751 <GO>}

Good afternoon, everyone. I am Matt Fassler from Goldman Sachs and it is my privilege today to introduce Walmart. From Walmart today our special guest is Dave Cheesewright. Dave is the President and CEO of Walmart International overseeing obviously all of Walmart's businesses outside the US.

He had been President prior to that of Walmart's EMEA business, Europe, Middle East and Africa as well as Canada since September 2011. He had been CEO of Walmart Canada appointed to that role in 2008 prior to that had spent time both in Canada and at Asda and he joined Asda in 1999. So 15 years in the fold if you will.

Most of the time I have spent with Dave I have spent in stores which I think speaks to his focus and the fact that he is a detail-oriented and insightful retailer as well as the leader of this massive global business and I think is going to be terrific in terms of our conversation today.

Walmart as an enterprise, I know we say every company needs no introduction, this company certainly needs no introduction; the world's largest retailer not to mention the largest retailer in the US. Certainly with a stellar long-term track record and I think a very aggressive realistic approach to retail today with all of its opportunities and pitfalls with a very aggressive push overseas, a very aggressive push online and then the omni-channel arena.

David is going to speak with prepared remarks and slides today for a number minutes and then I have with me on the podium my colleagues, Irma Sgarz, who covers retail in the Lat-Am region. And Rob Joyce, who covers Europe and we thought what better way to engage the CEO of Walmart International in a conversation than to have regional specialists as well as myself running that dialogue.

So with that, I'd like to turn the podium over to Dave.

Dave Cheesewright {BIO 7334339 <GO>}

Okay. Thanks very much, Matt. I reckon this is by a long way the poshest venue I've ever done a Walmart presentation in. Particularly impressed by the private boxes over at the side. I don't know what you have to do deserve to one of those spots. But is it just me or is cold in here. It is cold isn't. You know you hear the normal fire warnings, I think I'm kind of inclined if there is a fire, I'm going to huddle around there, I don't know about you but never mind make it to the exit.

Okay so I was going to talk about probably five broad areas today. Give you a bit of background on Walmart International. I know most of you will know some of it so I apologize if it is repetition but a brief bit of background on the business. Give you a very quick update on the half-year performance. Some encouraging signs but certainly not where we want to be as a business.

I will talk a little bit about strategy and how we started to look at the portfolio in a much more practical way across international. Give you a quick whistle stop tour through our five biggest countries. I won't go through all the countries and then finish by talking a bit about e-commerce.

So before I start, I know your favorite part of the presentation, the obligatory forward-looking statement. So I am sure you all have read that. Not everything I say will come to pass unfortunately. I wish it weren't the case but you can get full details on our websites.

So let's talk a bit about Walmart International. I think and I would be biased wouldn't I, I think I have the best job in the world. Walmart International is a big business. We will do around about $140 billion worth of sales. That would make us in our own right the second largest retail business on the planet, somewhere in the top 15 of businesses generally on the planet in terms of sales revenue. So it is a big business.

It is an incredibly diverse portfolio. We run around 6300 stores. We have over 800,000 associates, we operate in 26 countries with our core retail operation but have a number of franchise operations and vertically integrated sourcing operations across a number of other countries.

We run about 15 core formats so we are a multi-format business but because we have grown primarily through acquisition, we actually have over 70 different fascias [ph] around the world. So the names above the doors. So a very broad portfolio both in terms of geographic reach, number of associates, different markets.

And I think in there comes the fascination for the business. In some ways it can be very frustrating because having grown up as a very different portfolio, working on how you get things to be common and how you leverage that degree of scale can be a challenge. On the other side of it, it is fascinating. And one of things you find with Walmart is it is very rare that you come across a problem where someone across our enterprise and international hasn't already gone some way to solving that solution. So a lot of my job is knowing the markets well enough to connect all that innovation and start to try and find common themes that bring us together.

Certainly you have got some numbers there for the last 10 years. We have been a growth engine for Walmart. You can see our sales over the last decade increased threefold. We have added about $90 billion worth of growth. It has ebbed and flowed. It is not a dissimilar profile in terms of where that growth comes from other businesses. Obviously comp growth is very high up our priorities. We like that because it is our most profitable source of growth. That is probably been the most consistent through that period of time. It slowed down more latterly as we've seen economies slow around the globe.

The biggest chunk of growth in there is new store growth and we have been very aggressive in real estate expansion certainly over the middle part of that period and then dotted through there is a series of M&A acquisitions and some disposals, Korea and Germany in 2010.

So -- but very much a growth engine for Walmart and final thing just to point out on this slide and we are about one-third of the total business on sales, less than that on profit. I know we would get some questions on this, we always think of this in two dimensions. Clearly we are a very different business in the US. They are a single format, single country, $280 billion business. We are a 72 fascia, 26 country, much more complicated business. It is difficult to compare the profitabilities but we will often get referenced against them, we are not as profitable.

If you look at against our benchmarks of global competitors, the Carrefours, Casinos of the world, people with similar coverage, we are actually pretty good on profit versus those benchmark. So somewhere between those reference points is the right answer.

We've certainly got opportunities to improve our profitability. But about a third of the sales of the moment.

Okay so start of this year I think you have heard the announcements, we described the start of the year as solid. We are seeing a -- I'll start with sales, we are seeing a reasonable sales performance around the world. We are seeing mostly the same trends, we are seeing economies whether they are developed or developing under stress. Particularly in the middle and lower affluent customers, the top end tends to be a bit buoyant but that is not typically where we are playing.

Marketshare-wise, we are broadly satisfied with our performance. We have taken share in the majority of our markets. The ones where we are not taking share are typically the ones where we have taken some proactive activity on the portfolio and we have closed stores. But in the comp markets, we are doing pretty well.

And I think on the bottom point in terms of comp share, I do believe we are now starting to turn a corner. I think the best measure of comp for me is looking at a 12-month rolling average. So you take out all the variations of timing and after more or less two years of seeing that track down as economies have come down, half year quarter two actually was the first time we've seen that 12-month average move upwards. And I would anticipate that we will continue to see that improve during the course of the year.

Pleased with the operating income growing faster than sales. I am pleased with the way that this has been balanced in the half year. If you dig in the details, you will see that our gross margins have come down slightly. That is where we have been very aggressively going after price positioning in some of the markets where we don't believe that our GAAP is big enough. That has been one of the fuelers to comp growth. And we are covering that with leverage on SG&A. So we have got that formula nice I think in the first start of the year.

And key to some of the growth albeit a very smart part is we are expanding e-commerce very quickly in our markets. So across our business we are in significant double-digit growth on e-commerce. We have some sort of operation. I will talk a bit more about this later in all of our markets but a very, very good organization in the UK on the grocery home shopping business. Then very focused on Mexico and Canada in terms of more of our general merchandise businesses.

So I think overall, a satisfactory start to the year. We set solid progress but under no mis-illusions that there is a lot more to do as far as international performance is concerned.

Our strategy, relatively straightforward. We think of our business in two dimensions. We want to be in good businesses and then we want to run them well. And good business is really about the portfolio. So in the first couple months in the job spent quite a lot of time looking at the portfolio we have both in terms of countries we play in, the formats we are in within countries and the categories that we prioritize on and try to get a feel for what is good.

Some broad conclusions for us on that. I think we are broadly in the right markets. So if you look at the markets we are in and I include the US in this, based on the various projections you can get your hands on, we have got access to a bit over 50% of global growth projected in retail in the next 10 years. And that is very good coverage versus any competitor set. So that is good. And I think you can take from that that I will be very, very focused on improving the businesses we currently have rather than being too preoccupied with going to too many new places.

It doesn't mean to say that if the right opportunities come up, we won't look at them but we will be very focused on the portfolio that we have.

I think within that portfolio from countries, you can see that we have very big businesses typically in the markets that are much more slow growing like Canada and the UK. And particularly in the large store formats in those markets. We are bit underdeveloped in the markets so they are going to grow faster in China and Brazil in particular. So you will see another theme that will run through our strategy is that in the market you will start to see us move investment into the markets where we believe there is more growth. But only when we believe we have built a solid foundation for our retail operations.

So we will talk about some of the country strategies but turning around Brazil, which is fixing a lot of the integration issues that we've not managed to sort out in the past. And building a solid platform in China, are really about slowing things down for now. We are getting a very solid base in place so that as we start to look for more growth in those markets we can do it in a controlled and profitable way.

So the balance between the fast and slow-growing markets is something we will look at. I mean in terms of the formats within those categories, we are very strong in large formats and slightly different definitions around the globe. Obviously large means bigger in the US but typically we think of stores in three broad bands. So anything above 40,000, 50,000 square feet is a big store, 15,000 to 40,000 is a supermarket. Below that is a convenience store. So we are very well represented in those big stores.

And typically what you're seeing around the globe and it is not bearing too much by market is traffic ticking down in those big stores but ticket going up. So you will see a big strategy about reinventing our big stores. They are still a big growing and I think potentially vibrant part of the market but we will have to move much faster than we have done in the past at looking at what offer is going to bring customers to those stores.

Now it is always an evolutionary process. I mean if you look at the way our big stores have developed, Canada would be a great example. If you want back five years, we were building 200,000 square-foot stores. Our largest prototype now is only 140,000. And within those boxes you will have seen some substantial changes in mix as we move more into food. We have moved away from some of the hardlines areas that are moving online. Really chased off the soft home or areas where fabric and touch and feel is more important.

And so it's always been an evolutionary process for Walmart. But I think we're realizing now the customer is changing so fast that we are really going to have to step change our level of innovation in protecting those big stores.

So that is one part of the format portfolio and in terms of growth, we are seeing good growth around the globe in smaller formats and in particularly for discount and smaller formats. You see them predominately in Latin America through Bodega, (inaudible) in Brazil and through e-commerce.

So I think as a rough shape going forward, you will see our allocation of CapEx moving towards the countries that are going to grow, protecting the big boxes we already have but not be over excited about building lots of new big boxes. But particularly focusing on growing e-commerce aggressively and chasing smaller stores where we believe there is more long-term benefit.

In terms of performance, you can see there is a very simple wheel there that we tend to operate across the countries. I think you could take this and probably pretty much overlay it to any retail business. We are focused on all the things that are good in retail. So driving a healthy core which is all about pricing and assortment for us and we are still very focused on price leadership across our markets. Focusing on new growth through controlled real estate expansion where it matters. Our enablers are typically through the productivity loop so driving every day low cost out of our business and I will come on and talk about that in a bit more detail as we cover the countries.

But also really upgrading our talent. And we were delighted -- and slightly sad to see Greg Foran move from our business to run the US business. And you can see the style of leaders that we are looking for in our latest appointment which will be the CEO of Canada. So Doug VanDenBerg, he is Belgian by background. In his words, speaks five languages fluently and he is dangerous in another five. But a really experienced retailer. Was running (inaudible) Belgiums [ph], worked in Asia, worked in North America, worked in Europe, run across multi-formats. And that sort of breadth of complexity I think is going to be really crucial in our leaders in managing the transformational changes there that are going to occur.

Then in the green boxes at the bottom are really about building trust. So our compliance programs, we have invented a lot of time and energy over the last couple of years. We are seeing an immediate benefits in the maturity and the continuity and our ability to deliver within our businesses. And I think there will be a very good long-term differentiator as well as the world becomes more transparent and the levels of scrutiny that everybody is going to be under goes up and up and up. They are going to pay back for us very well.

Okay. So let's just talk briefly about international priorities and then we will cover a few of the countries and you will see a very consistent message from me through the various places that we talk to this community.

So number one priority, driving comp sales through price leadership. As I said before, we like comp growth. It is our most profitable form of growth. It is leveraging existing assets. And we've seen a slow but continued decline over the last eight quarters prior to Quarter Two and that is something we need to turn around. I think the way the economies are at the moment I don't think we would get back to the sort of levels of comp that we were running three or four years ago but there's certainly room for improvement in there and you would hear the same message from Doug about the US business or Sam's.

It is really about doing the basics well, making sure we've got the right price position in markets, we have got acceptable GAAP versus competition but really working hard on our assortment management in stores and also how our offering integrates with our online offer. So that will remain the top priority as we walk around countries and talk to the teams.

Four strategic priorities that we'll continue to focus on. And I will cover most of these as we go through the detailed countries. So accelerating our e-commerce business. We're going to touch on that at the end. Building a platform for sustainable growth in China, rejuvenating our Mexican business and I know you will have heard a very good update on some of things that we are seeing and particularly some of the progress that we are making already -- at the sessions yesterday. Then turning around Brazil.

The enablers to that, again, no rocket science here. We will be the lowest cost operator wherever we are. That is not the case now and some work to be done in a couple of markets. We will develop genuine world-class talent either by developing internally and in some cases looking outside and we will aim to be one of the most trusted operators wherever we operate through our investment in communities, through the work on the sustainability and particularly through the work we are doing on our broader compliance programs.

So you will see those priorities pretty consistently for trade for us and I think -- I don't think you will see too much of a different agenda over the next couple of years.

So let's talk about a few of the markets and start with China. So build a platform for sustainable growth in China. Any which way you cut numbers, by a long way the biggest growth opportunity in China is China around the globe. It is a real mix so you see all of our formats doing well. Sam's Club which typically targets more affluent customers has been a very strong business. I think we have our highest grossing Sam's Club worldwide in Shenzhen. So a very successful format for us.

But we also seeing there is still a big growth in terms of people moving from informal to formal market which you are going to get fixed a bit through the business-to-business side of Sam's but also through some of our supercenters.

So a few things we're working on here. First of all is disciplined growth. And I think if you looked back four or five years ago with China and looked where new stores were growing up, you would see them pretty evenly spread across the whole geography of China. And I think we have gone back to what Walmart knows best which is concentric circles. So we are very clear now about which regions we want to dominate in. We'll build out stores around distribution capabilities so we're leveraging those assets and you can see from the chart there that the south of China is where we will put most of our resources and lean into. And our aim will be to dominate in one particular geography before we worry too much about going somewhere else on our physical business; e-commerce obviously we can approach very differently. So a much more disciplined approach to growth.

We spent a lot of time working through exactly what formats and layouts of formats will work for us in China because it is very hard to get a nice 200,000 or 150,000 square-foot store at grade with a nice car park out in front. You are typically looking at three; or four-level stores. So we have done some very good analytics now to look at which combinations work for us, which ones don't, what are the key contributors in terms of access and parking that make those stores work. So think very clear, where we grow, what sort of formats are going to work for us.

Delivering value to customers is about the core offer. And certainly the biggest enabler to this is what we have done with the merchandising organization. So over the last 18 months we have taken a very regional buying structure with multiple offices, very different assortment in stores and centralized that. That is given us much more control over our offer, given us much more control with our negotiations with vendors and also taken significant cost out of the business.

So you can start to see that play out in the stores now that price gaps are starting to improve in China, the assortment is much better, the forecasting and replenishment are better for the basic, in stock standards are significantly better.

Investing in infrastructure. So we've now have got a much more robust and coherent distribution network. So particular on the fresh side, that is meaning that the product in stores is much fresher. So big, big improvement in the core offer.

On cost, the chart looks a bit odd. The spike in 2013 was the big investments in compliance but also some investment in restructuring. And I think what you will see in subsequent years is a bit more of a compelling chart that you will see us now start to be able to take costs down in subsequent years. And although the sales have been tough in China this year with a number of the government austerity schemes, we are seeing increased ability to leverage our costs down and still maintain a good level of profitability improvement despite a bit of a sales shortfall. So great progress on the virtuous circle.

And finally then in China, trust is very, very important. We have invested a lot in compliance and particularly on food safety. And you will hear quite a lot of noise in that area. I really do think that the work the compliance teams have set up in the last 18 months is going to pay huge dividends in China. And we are starting to see a bit of a change in sentiment from the policymakers and government. Typically Walmart is under a lot of scrutiny wherever it operates because of our size. But the power and the professionalism and the caliber of our compliance programs are being now viewed as best in class. And rather than being a target, we are now starting to see some light where we are viewed as a partner for someone who can move the whole country agenda onwards rather than being just someone you can use as an example which is a big deal for us in China.

So we will continue to work hard and focus in that area. So pleased with progress there. I wish the sales were a bit better. Some of that I think will unwind as the austerity measures change but very pleased structurally with how we are building the business, have a very talented team in China.

If we move on now to Mexico. And a number of you will have set through the presentations over the course of the last couple of days. But Mexico is a phenomenal business for us. Maybe I will just switch forward to the next slide quickly. Just gives you an insight for those of you who don't know about the track record of that business. So 10-year, 10% CAGR growth on sales, 12% on profit. It is a phenomenal business any which way you look at it. So it is coming off a very high pace.

I guess the challenge for if we can go back one for Scott and the team, is that it is such a big part of international that we really do need that business to continue to fire on all cylinders. So I think the important message when we talk about rejuvenating Mexico is it is a great business but still doing pretty well but we need it to do brilliantly if we want our overall portfolio to work well.

So a couple of things that the team are very focused on there. Most of the concerns we've had had over last couple of years has been the Sam's business. And I think when we reflect on that, the business strategies changed a bit two or three years ago, a bit more assortment went in there, kind of a bit more promotional, targeted a broader set of customer bases. You know I think there is some short wins in that but I think the Sam's business should be a very consistent offer around the globe.

So what you're seeing us do now under Scott's leadership is we brought Todd Harbaugh, who was the COO of the US business in to run the Mexico Sam's business. And we really are getting back to aligning ourselves to the core business. So we will level the platforms, we will take a lot of the new initiatives that Roz and her team are developing but really you will see us move back to focus on the business member very strongly and particularly try and get a bit more excitement back into the assortment around the treasure hunt. So for those business members who are in, trying to find items that they wouldn't have typically expected to be going into buy but are just so compelling that they can't help but put them in their basket.

So I think there will be some quick wins there but it will probably be a year to 18 months before we really see that business start to get back to where it should be. But very confident we can do that.

On the self-service business which is the bulk of the business in Mexico, very pleased with the progress. They saw sales slow down towards the tail end of last year and during the course of this year, we have gradually seen that improve. So again, no rocket science in there. I think two big themes that I would pick out that Scott and the team are leading, a lot of great stuff on the customer proposition. So reenergizing the competitive price position, particularly working hard on a compelling fresh offer, that is what brings the traffic into the stores. Really start to make sure that the core offer is good.

Second part of it is then leverage. One of the things Mexico has done an outstanding job over the last decade is grow very fast. And the faster you grow, the easier that virtuous circle becomes. I think with the way the economy is, I don't think we'll ever get back to those growth levels of five years ago and therefore some of the skills that some of our slower growing markets have learned in terms of getting into the detail of wage planning, efficiencies, logistics efficiency, are now skills that needed to be added to the Mexican business. And very proactive approach by Scott of reaching out to markets where we have got great skills there and start to bring those into the markets and reengineer costs out of the business.

And you can see at the bottom there that we really starting to see some nice gaps grow again in terms of the comp growth for our self-service business versus the rest the market. So a good start.

Sam's Club is probably still the biggest undone in Mexico.

So let's move on to the next one. And Brazil, turning around Brazil. The Brazilian market is a difficult market to operate in. It is not impossible. There are certainly retailers there who run good business and good profitable businesses but whether you're looking at taxation or the labor environment, it is a complex market to operate in.

We have focused on some similar things that the Chinese business there in terms of making sure that we have got this business on solid foundation. It really starts with leadership. And I've put a few of the face up there that we brought into the business over the last couple of years. Gui Loureiro from Unilever. So a longtime experience in Unilever across a number of different markets. A lot of hands-on knowledge in Brazil, good turnaround experience from Unilever in Mexico and the sort of leader that I think really can drive some of these changes through with a lot of experience in stature.

The rest of the team you see there are senior people, they all have a couple of things in common, they all have the knowledge of the Brazilian market. They are a mix. Some are from other retailers, some are from packaged goods but all have got multinational experience, all know Brazil very well, all got some experience of turnaround. So I am pretty confident we have now got a really good leadership team in that business.

Anything to do with Walmart really does revolve around growing sales. So I think the second thing we talk about is we have taken a much more pragmatic approach to how you develop EDLP and price leadership. I think those of you who have tracked our history, we launched EDLP as we had an initiative on turning around Brazil a couple of years ago. The thing about pricing in EDLP, it is a sequential journey. You aptly have to have the lowest cost base before you can contemplate being a price data. And you really do have to have some sort of reputation as a price leader before you can contemplate going to a EDLP.

And if you think back in the history of Walmart, the kind of Jack Shoemaker days, he would say it took seven years to really implement EDLP and that was off a base of a very low cost base in the original Walmart model and certainly a reputation for price leadership.

If you haven't built those foundations, going too quickly on EDLP simply deflates your sales and makes leverage even harder. So you will see us back off a bit from that and focus very hard on the cost basis and try to start broadening our price gaps in a controlled way until we get some sort of reputation of price leadership and then we will come back and deal with EDLP.

As well on comp sales, we've seen very good work on assortment management in there. And again we borrowed some resource from the US in Steve Breen who was one of the Senior Merchants at Sam's. And we found some big gaps in assortment in some of our formats. We've added those back in and we are seeing some nice sales results.

So we are not taking market share yet. We closed 27 stores last year. If you take those out, we are certainly now in line with the best competitors which is a lot better than we have been in the past.

Across the bottom, a couple of things I will pick out. In terms of discipline growth, exactly the same approach with China. Rather than trying to grow everywhere on all formats, we are very clear where our priorities are. We are very strong in the north of Brazil, (inaudible) and Bahia. We understand that our best format is the TodoDia [ph] format. It is very similar to the Dager [ph] in Mexico. That is where we will focus our efforts rather than try to grow everywhere.

And I think the one of the bottom left is probably our key one which is integrating systems. When you're in a country as complicated as Brazil, we still got three legacy businesses. So the original Walmart business, the Bompreco and the (inaudible) acquisitions. Three head offices, three different systems. And we tried a number of times to integrate those. So what would tell you is different this time?

I think we really understand through the leadership team that this is just a nonnegotiable in terms of ever having a successful business in Brazil. So there is definitely a burning platform, the team are committed behind it. And to date, very good progress. So we have converted 106 stores so far this year onto Walmart platform. We focused primarily in the south. We are seeing great results of those convert. So clearly you get all the benefits of common systems, visibility and control. But the associates in stores are immediately seeing much more information that they can use so the last trip Enrique and I had down there, you could feel the excitement as they got hold of tails on guns [ph] and they could look at margins and sales rates in the stores and they were going around all the fixtures and moving things that weren't selling. So you get all that incremental excitement about selling which is what want to get in our stores.

But I think also you then start to get a much more clarity in terms of consistency and control of your process. So 106 done so far. Seeing also improvements in availability of in stock as we are cutting over. So positive impacts of those stores cut over and we will aim to have that finished by the end of next year as we move to northern stores.

So a long way to go in Brazil but I think we are growing in confidence after a couple of failed attempts. We really are going to get that business integrated and create a solid platform for growth there. It is a good progress.

Onto the UK. Very difficult operating environment in the UK. You will know the rough climate there. You have got four main players in the four main supermarkets typically about 80% of the business and sandwiched between a very vibrant discount sector with Aldi and Lidl and at the top end, a very vibrant premium sector with Marks & Spencer and Waitrose. And for the last 18 months or so, the 20% taking share off the 80%.

I think the discount one is a trend that is here to stay. So I am imagining we're going to see that pressure for the foreseeable future. I think the top end is a bit more cyclical. It depends what happens in markets if they start to track down or become a bit more volatile. Typically you see that customer come back to us. But certainly there is going to be pressure on the big four.

I feel very good about our UK business and Andy Clark's leadership. Mostly because we talked about this particular issue nearly 2.5 years ago now. They did a big strategic review and they have been on a program called redefining value retailing in the UK for the last two years. And what you started to see them do is take a long-term structured approach to taking cost out of the business. You would have heard an announcement earlier this year about their store structure. You will have seen them over the last five years build an organization called IPL, International Procurement & Logistics, which is now the largest single supplier to any retailer in the UK. It is owned by Asda. And it does the produce sourcing, it does a lot of very good efficiency driving in the supply chain.

So for example, a wine from South Africa, most people buy bottles of wine from South Africa and then ship in them a lot of fresh air which unfortunately you can't sell one that arrives in the UK. We ship Polytainers of wine, we have our own bottling plant. So we save all those transport costs and take costs out of the chain. And there's numerous examples of that that I think we can deploy around the world actually.

Very innovative Asda on their offer. Very progressive on private label. Just under 50% share in the chosen by you, mid-tier range which is very integrated with customer preferences. It has been a great success. And very innovative on the service end. So you can see one of the rapid scans, auto scanners at the checkout that is on trial in a couple of stores in Asda at the moment.

But more than 50% of transactions in the UK now are going through self checkouts. So very efficient in terms of the way they operate both through the self checkouts you've been used to in the UK but also the hybrid checkouts that allow you to check out the baskets yourself.

Share-wise, you can see how this market plays out. It is going to be a tough market to aggressively take overall market share because of the strength of the discounters. I think Asda is doing a great job at being the best of the four in taking share off the remaining three. There are very focused on the discounters. And the work that has been done on restructuring cost base has allowed us to half our price gap to Aldi over the over the last couple of years. I don't think we need to match, we just need to be at a level where what we offer in terms of service and assortment outweighs any differences in prices and I don't think we're that very far away from that at the moment. So good job in a very tough environment for the UK team.

Then finally, Canada. Want to strengthen our position there. The big story over the last couple of years in Canada has been the entrance of a big competitor and I think the team have done a really nice job there.

The biggest advantage for us was the amount of notice we had at that event occurring. So we spent a lot of time with Duncan McNaughton and the US team. Obviously Duncan was CMO in Canada prior moving to the US. Did a lot of analysis on where we would be strong and weak. And I think the long and short of that competitor's entry is we've just become a much better Walmart. We put a lot of work on our assortment and our style management in both home and apparel and we have seen both those businesses perform very well. And the whole marketplace was very aggressive on food when that entrance occurred.

Second-biggest trend in Canada is the growth of food for our business. We have opened over 260 food stores in the last five years with the roll-out of supercenters and we are very pleased with that program. It is a lower-cost program in the US because of the nature of the marketplace. Quite a lot more stores where we'll put food inside the existing box rather than to go through the cost of expanding. But we've taken the vast majority of food growth in that market over the last five years and we have still got a few more years to keep focusing on that.

Next stage for Canada is really starting to take some of the best practice from both Asda in the UK in terms of modeling their costs. And whether that is benchmarking the DCs or taking the wage planning system from Asda, there is a lot of initiatives now starting to flow into that market which will allow us to restructure costs and then get back to investing even more in price leadership and you can see some of the gaps that we had there which are pretty healthy.

So good progress in Canada. I think it gets very interesting as you get to the final quarter and you annualize out against some of the big openings.

Okay, let's finish with e-commerce, a really, really exciting area for us. And you'll hear a couple of phrases consistently whether it is Neil talking or me and that is excelling at the fundamentals of e-commerce. So the technology side of it. It is a huge advantage for me to have Neil's organization, San Bruno, developing a world-class platform. And Neil and I have kind of developed a hybrid approach that says look, we can't afford to wait for Neil to build a global Pangaea platform. So we have gone fast in our countries on our own. So Canada would be a great example. We put our own platform in. We built it through third parties. But we built it in collaboration with the global e-commerce business in San Bruno. So it is built in part as Neil develops for example the Polaris search engine, we can just unplug our third-party system and put their one in. So they've kind of have been built separately to allow us to go for speed but integrated so we can dovetail and use the technology platforms that they are building.

So we'll end up with a leveraged global platform around the world which I think will be a huge advantage.

Second phrase you'll hear a lot of is winning at the intersection of digital and physical. And there's a lot of misunderstanding about what that means. It operates at a physical level. So as the business is very, very proactive looking at all the various elements that the customer might want to receive product in the future. So lockers, collect from stores, remote collection, automated collection, drive-throughs, all of those we are rapidly now trying to test and work out what the best formats are in themselves and then which ones work best in different countries.

I think the two most exciting areas about the intersection, one is the customer. What being a generally credible player in both physical stores and digital means is that we will have an array of data that no one else will be able to match. Because there is no one else really that is going to operate with credibility on both sides of the physical and digital spectrum. And I think that ability to take that information and interact directly with the customers and either drive loyalty or shopping lists or programs that understand what their behaviors are changing by is going to be a big piece of competitive advantage in the future.

Then the third area of integration which I think is maybe the most exciting, is the two businesses are so different in the way they approach things. Our physical businesses are much more about art. You know we have got a lot of merchants that have been in the business of long time, they use analysis but they use a lot of experience and gut feel to know roughly what customers are doing and how you change assortments.

Neil's team are phenomenally good at the science. They can -- you know where we are doing 100 price changes a week, they can write an algorithm that can do 100 million a week because of the unlimited capacity and algorithmics. I think if you start to think about how those two can impact on each other, our ability from our physical side to give all of those years of experience and gut feel about what customers want, the digital side. And the digital side to take their problem-solving capability to algorithmics and apply it to a physical business I think you get an enormous amount of synergy from those two.

So our focus in international will be to rapidly accelerate grocery home shopping. We have the second largest business in the world already in Asda. A lot of inherent knowledge and experience and you will see us move people whether it is Kieran Shanahan, who operationally around the UK operations for a while and is now in Neil's organization or Judith McKenna, who is running the US small stores operation and again led the e-commerce business.

We will want to use that knowledge to grow our grocery home shopping very quickly. And on general merchandise we will use the generic platforms that are being developed under the Pangaea brand with Neil's organization and deploy those out to the countries as soon as they are available.

So very, very excited about what is happening on e-commerce at the moment.

Okay so summary for us. Lots to do in and international. It is an amazing job, great variety, lots of things to fix which I kind of like. You will hear us very consistent on our priorities. We will always be focused first and foremost on driving comps sells. Always our best source of returns. We have got a very clear view of the portfolio now. You'll hear us talk about those four priorities over the foreseeable future so e-commerce, China, Mexico, Brazil and you'll also hear us work hard in a much more long-term structured way about how we take cost out of our business, how we really do define and bring in what we believe is world-class talent to manage transformation rather than execution. Then finally, continue to build those programs that deliver trust. So a solid start to the year. Loads more to do but I think quite an exciting future for us would be my summary.

Questions And Answers

A - Matthew Fassler {BIO 1509751 <GO>}

Thank you. So much for that overview and those remarks. I'm going to ask you a couple of questions. And the first I will try to wrap two into one and they do relate to your first-half performance.

The first part of the question would be if there were a high level set of drivers that you think would explain the turnabout in the profit trajectory in the International Division in the first half of the year, what would it be?

Then secondly, in the Second Quarter, you had very good performance even though margins were down in I think your three largest markets, the UK, Mexico. And Canada. So were there common factors there that influenced the margin pressure in those markets?

A - Dave Cheesewright {BIO 7334339 <GO>}

So on the first question, the profitability. I would say it is a combination of two things. I think the fact that our sales performance has been stronger through for the first two quarters than it has been certainly through the last year is always very helpful. It starts to make it easier to leverage costs. And that is a combination of two things. We have certainly stabilized some of the declines in some of our problematic countries. But we've also seen some very strong performance in some of our smaller countries. We didn't talk about it in summary but South Africa and Japan in particular, have had very strong first halves to the year versus where they had been running both in terms of absolute growth but also share gain. So sales will be one.

I think the second then is the basics of retailing that we've been very focused on costs and we have seen good cost leverage through the first half which we hadn't seen through last year.

Then probably the third one is that we are benefiting from some of the work that Doug did at the tail end of last year around tidying up the portfolio. So we took out around 17 very poor performing stores in a couple of our countries last year so we will see that starting to flow through now.

A - Matthew Fassler {BIO 1509751 <GO>}

So you talked certainly in your prepared remarks about many of your largest and most exciting markets. You also showed your growth trajectory and to maintain that trajectory there will be a lot of dollars making their way into the system.

If you look across the globe, are there markets where you want to achieve substantially greater scale where you view yourself as underrepresented and profitable share is feasible for Walmart so that when you come back, God willing in 2024, 10 years from now and address this crowd, you can say here is where we did it.

A - Dave Cheesewright {BIO 7334339 <GO>}

Yes hopefully it would warmer in 10 years time. Yes, I think the obvious one is China. When you look at all of the projections, albeit the growth is slowing down there and it's not the easiest of markets to grow freely, we have a very low share in China and we would hope that that would be an area with a solid foundation that we could start to see accelerated growth and accelerated share growth.

You know behind that, in terms of priorities, Brazil would be a second one. We are a reasonably big player there already but I think there is some good growth to be had by at least getting to a stage where we can control (inaudible) grow in line with the market.

Then the dark horse I think would be somewhere like Japan. Where it is -- you know we all went into that market hoping that there would be a degree of restructuring in the supply chain and a bit more consolidation which we haven't seen yet. But you know that is a big market where if we can move a bit, we are seeing some much more solid sales and market share gains this year than we have in the previous years. And if that continues, that could be quite -- .

A - Matthew Fassler {BIO 1509751 <GO>}

Thank you for that. Then the last question I would ask before I share the mic with my colleagues here. If you think across the globe, which competitive formats have been the most disruptive to the marketplace?

A - Dave Cheesewright {BIO 7334339 <GO>}

I think looking back without shadow of a doubt, supercenters over a long extended period have been the most disruptive, the big destination stores. I think in the more developing markets, the compact discount hypermarket has been very disruptive particularly at capturing that migration of traffic from informal to formal shopping. So the Bodega's, the Todo Dias, the (inaudible) in Latin America particularly. Then of late certainly some of the e-commerce formats becoming very disruptive.

Q - Irma Sgarz {BIO 15190838 <GO>}

So in Mexico I think you pointed it out on your prepared remarks earlier that you have been posting for more than a decade a double-digit annual area growth. You've now have significantly scaled that back with the announcement earlier this year and then again yesterday. You know balance sheet is certainly not a limitation. The market is still more than 50% informal. So there seems to be a lot of opportunity still.

Could you just speak to a little bit of what has been driving your decision to slow down growth there? And is it just a question of it being harder to maintain level of returns that you have been posting so far?

A - Dave Cheesewright {BIO 7334339 <GO>}

I think it is a couple of things. Certainly some of it is economic. If the market slowed down you would expect to slow down a real estate program to some degree. Part of it is format driven. We take a long-term view. A lot of our square footage growth has been in supercenters and we think big stores, they are going to be under pressure for traffic albeit there is opportunities in ticket I think that can offset that.

Then I think the third bit is a bit more pragmatic that I think Scott and the team have done a nice job of trying to balance just simply growing very fast with growing fast in a controlled way. And the announcement yesterday I think is a perfect example of that.

So we moved 15 stores out of this year's commitment into next year. Now in reality that makes virtually no difference to our long-term growth because they are moving two weeks from the end of this year to last year but I think the point Scott made to the rest of the business is that it can't be the right thing for either the business or customers to be opening stores in the last two weeks of December. It is your most stressful period. And the last thing you want to do with the unpredictably of a new store is open it at your highest traffic.

So for the sake of two weeks sales, there is a very sensible decision now to start to balance the portfolio and open it in a part of the year where it is much quieter.

I think maybe the final thing and Scott will share if there's anything I missed. But is that a lot of the other growth in terms of square footage has been the Bodega format. Inevitably if that is the format that picks up the move from informal to formal shopping, a lot of that is fueled by remittances for the US. And certainly one of the things that as well as the local economy, the US economy has been subdued. We have seen much less remittance value going from the US to Mexico. If the US recovers and we start to see that go up again, I think you will see the program start to accelerate again.

Q - Irma Sgarz {BIO 15190838 <GO>}

Great. Then just shifting to Brazil in the last years as you have pointed out, the operation has gone through a prolonged integration challenges, repeated management changes and also the implementation of Everyday Low Prices. Could you just repeat or fill us in a little bit more on the details of what are the lessons that you have learned and what is kind of the current stages and then the outlook for that operation?

A - Dave Cheesewright {BIO 7334339 <GO>}

So I think if you deal with the three. So leadership first. You know I think the challenges of integrating a business in a difficult -- you know integrating three businesses into one, in a very difficult country to operate, across that number of sides of the business is about the most difficult challenge you can get. And if you haven't hired a world-class team who have experience in both the market and turnaround, you are likely to fail.

And I think as a business with a history of kind of -- our challenge has been leaders who are great at replication and execution. It is not that they weren't great leaders in the previous two that attempted turnarounds. I just think we put great leaders in the wrong jobs.

So I think our leadership now, we've picked a leader who is designed to deliver what we need to would be the first thing.

On the systems integration, having been through that with (inaudible) in the early days and done quite a lot of work in that, it is much about hearts and minds as it is about technical capabilities and whether it is Enrique or Gui in a country or myself, we are going to integrate those stores and it is not a question of whether we should or shouldn't or how long it is going to take, we are going to do it. And I think as long -- as soon as the team get the mindset, their challenge is not to tell us whether it is the right thing or not, the challenge is how to do it, makes your level of success much higher.

Then I think the third thing that is different this time is we're just being very pragmatic about the commercial side and particularly how quickly you can migrate to EDLP. You know in the virtuous circle, what people forget a lot in EDLP is the single biggest driver of Everyday Low Cost is driving your sales line because it dilutes fixed cost.

So the last thing you ever want to do in a period where you are trying to go through transitional changes is lose sales momentum. So we are first and foremost focused on keeping sales momentum up when we go through this change. That will allow us to build a low-cost base. That will allow us to extend that price leadership and then we got to that stage we might think about EDLP.

Q - Irma Sgarz {BIO 15190838 <GO>}

Great. Rob?

Q - Rob Joyce {BIO 16540401 <GO>}

Thanks, Irma. So moving to the UK, you mentioned the very strong growth we are seeing there from the discount channel. I was just wondering what your thoughts were -- well A, what catalyzed this very strong growth? You mentioned it was a structural move. So B, how far do you think the discounts can go in terms of market share? And is this something you see the threat to other the markets you are in -- is it potentially going to happen elsewhere?

A - Dave Cheesewright {BIO 7334339 <GO>}

So the discounters have been in the UK for a long time, certainly as long as I have been working in retail there. And their first 10 or 15 years were -- they added stores but it was relatively benign share growth. And what was different about them at the time was that they were very much the German hard discount model. So private label, limited assortment, not really focused on fresh. Quite viewed as a down market environment and if you walked those stores you'd typically see very elderly customers or very low affluent customers.

And I think the big supermarkets did a really nice job at developing the discount ranges that gave their customers the option of comparable prices in a much better environment. What has changed then particularly notable having been out of the market and coming back into it is the stores they are building our bigger and the assortment has expanded significantly. So there is brands in there, even on their private label, you're seeing two or three tiers of private label which you have never seen in a hard discounter and a much bigger focus on fresh is one.

So I think the offer is more of a supermarket offer than a hard discount. There is a question about what that does to the cost base going forward. But it is working for now.

Then the second thing that is again surprising is when you look at advertising investment as a % of sales, the two highest advertising investors in the UK, Aldi and Lidl. I mean you had said -- if you asked someone five years ago to tell you about the model of the discounters, in fact they don't have a title, (inaudible).

So I think they have done a very nice job at repositioning themselves as a discount supermarket rather than a hard discounter. And in a very mature market I think that is quite a good strategy. I'm not sure how well that translates to other markets.

Q - Rob Joyce {BIO 16540401 <GO>}

Okay, you don't see them adopting similar strategies in other markets?

A - Dave Cheesewright {BIO 7334339 <GO>}

Well I think it gives them another -- you know is another tool in the armory. If they get to the States, the growth is muted in the hard discount format, there is a way of developing it to the next level. It would work in some markets, it would not work in others.

Q - Rob Joyce {BIO 16540401 <GO>}

Got you. Fair enough. Then just moving on another area of disruption where the UK is quite developed in terms of online grocery, just wondering what Asda are doing to really drive share gains in this channel and what kind of learnings you can take to or from other markets globally on that?

A - Dave Cheesewright {BIO 7334339 <GO>}

Okay. So two main strands. I mean they are consistently focused on basic operations. So it's still primarily a store picks operation. You are then only as strong as the availability in a store. So continued work on making sure that our store availability is good enough so the number of orders that get fulfilled as ordered goes up and up and up. Now that is a fantastic virtuous circle because you know

I would always argue one of the biggest benefits Asda has had from home shopping has nothing to do with home shopping, it is what it's done to the standards of the store. When you get that absolute clarity of what was there and what wasn't there at the time you have to pick it and therefore how you have to engineer your supply chain so that the basic store operation has improved exponentially on the back of e-commerce.

So I think a lot of blocking and tackling on the basic offer. We are certainly plugging in some of the elements of the Pangaea platform as we get them. So the core grocery home shopping in the UK is now on Pangaea. It is got the Polaris search engine. So its basic technology platform is improving all the time.

Then the third area of innovation which you are probably aware is the most transfer is around providing different routes for the customer to access products. So that business grew for the first 10 years simply by delivering to home. And by the end of this year, we will have more than 600 collection points so some of those are at the stores. Those are fascinating because quite a reasonable proportion of customers' collecting from the stores are not store customers. They are new customers. And around 40% of those that come and collect then go in and shop in the store. So that is a big deal of synergy for us.

But there is also then remote collection points. We are trying lockers, we have got gas stations with collection points, we have got a partnership with the London

Underground where we have got six collection sites for transit traffic on the way home. So we are learning very quickly how those modules operate, what the economics are and where the best sites are. And obviously with Judith McKenna now leading the US small stores operation which includes some of the different routes to market, then that best practice is flowing across very, very quickly.

Q - Rob Joyce {BIO 16540401 <GO>}

Thanks very much.

A - Matthew Fassler {BIO 1509751 <GO>}

I want to talk for a moment about China. Can you talk about -- I know you touched on it a bit both in the broader commerce discussion and in your China discussion. Your e-commerce strategy in China and the synergy with the Yihaodian business.

A - Dave Cheesewright {BIO 7334339 <GO>}

Okay. You will see in our three core markets that we probably to a large extent run the physical and the digital businesses separately for now. So US, Brazil. And China with Yihaodian. That is quite a thoughtful move in that although we believe passionately that the winners in the long term will be people who can manage across the whole spectrum of physical and digital and particularly at the interface, we don't believe it is possible to win at the interface unless you are generally world-class at both sides. And they are quite fundamentally different. So letting them develop in some degree of isolation I think is a good strategy.

You are starting to see collaboration between the two. So a good example would be one of the best-selling items in Yihaodian is I believe it or not is Asda Longlife milk. Because a lot of the product security issues in China, foreign brands have a high degree of credibility. So we have given Jin Lee [ph] and the team in Yihaodian complete access to our International buying program. So they have -- they know exactly when all our teams are going out and doing buy trips in certain categories so they can see the product environment prices and if they want to take any of those they are adding those to their assortments. And that is certainly helping them.

We are starting now to move into kind of phase two which is planning how the two integrate. So you will start to see us take a more joined up approach on collection points and so some of the learnings from the UK will start to put collection points on the car parks of some of our stores for the Yihaodian product. And I think we will see the same thing that will bring new customers who shop in the stores and bring traffic to the stores. So making world class in their own right and then start to integrate them would be our approach there.

A - Matthew Fassler {BIO 1509751 <GO>}

Then the last question I would like to ask before I open it up to the audience, the roving mic is coming, please get ready. Canada. So obviously a market you know exceedingly well. How close to saturation is this market? And I ask this particularly really with regard to grocery where there is some terrific indigenous players. And also with regard to Target's recent entry.

A - Dave Cheesewright {BIO 7334339 <GO>}

I think it is a relatively saturated market. Grocery has been very interesting as we have brought it into -- it is rare that you've got two massive impacts in Canada the last two years. You have had other opening from scratch 258 food stores. And you had Target converting 120 odd seller stores and a huge impacts in a market. I mean times by 10 and you get the impact in the US equivalent.

On the food one, what we found is that we are often going into markets where there is a lot of food competition in the area anyway. So we tend not to think of it as saturation. And what we said is there is no one competitor that suffers as we have rolled out. It tends to be the weakest player in any category that is the one that suffers. So I think there will be some consolidation of retail outlets and movement to other areas. But to date, it is dampened the performance of other people rather than led to any restructuring.

You know on Target. And I'll just reiterate what I said before and I think that you have read about some of the trials and tribulations they have had. I think the best thing about their entry was the notice that everybody got about them coming. And it is a good lesson for all of our countries actually. It is one of things we talk about internally is virtual entries. It has accelerated the performance particularly of assortment management of the Canadian business because we knew someone else was coming into our marketplace. And so the challenge throughout the other markets, is well why do you have to wait for someone to come in to have that mindset? Why don't you benchmark against best cost competitor? And if he was going to come in, what would you do about your assortment and why don't we do that anyway?

And I think that is true of every competitor in Canada, Canadian (inaudible) have been very much clear on the back of the (inaudible) entry about the proposition and the acquisition for Zion [ph] is was very -- I think a very good acquisition. Loblaw's and the Shoppers Drug Mart has been an interesting combination. So it just prompted everybody else to be better. That is the problem with somebody comes in.

A - Matthew Fassler {BIO 1509751 <GO>}

Thank you. We have a couple of hands raised through the room. And we have a mic making its way to the front.

Q - Unidentified Participant

Thank you. And congratulations on your relatively new role. You talked a bit about food security but I think one thing that as you expand your e-commerce platform that people are concerned about is Internet security. Given what Target experienced over the holiday and the recent news about accounts at JPMorgan being hacked. Could you share what you are doing versus your competitors to increase that security?. Thank you.

A - Dave Cheesewright {BIO 7334339 <GO>}

I am not sure we go into details about what we're doing. I think I would say a couple of things but it is very, very high up on our agenda. We have seen the impact on other people. Broadly some of the breaches we have seen, we are encouraged by the fact that our protocols would have not allowed that to happen in our business but this area is moving so fast that that is kind of more consolation for now because you never know what the next one is.

I think the other area that we are finding very advantageous is having a pure play e-commerce business in our portfolio. So with the time that we have got in our operations at San Bruno. Probably I think the single biggest achievement Neil Ashe has made is to make Walmart sexy in Silicon Valley, which I would have said was impossible before he did it but he really has got some of the very best brains in technology in that business. And of course they are very focused on how you manage security and so I think that level of competence we are now starting to see apply to our core businesses.

So I think I high up the agenda, we have a unique resource in having a pure play business in our mix which helps us across the rest of the business. But we are certainly not complacent in that area.

A - Matthew Fassler {BIO 1509751 <GO>}

We have a question right there please.

Q - Unidentified Participant

There is a very lively debate about the right model to fulfill e-commerce in food retail. You sort of span the spectrum simply with your (inaudible) and on the West Coast versus store pick in the Asda in the UK. Where do you stand on what is sort of the right model and particularly if we think three years, five years from now rather than utilizing current assets?

A - Dave Cheesewright {BIO 7334339 <GO>}

I think our biggest asset is as in all cases in International is we have an answer to everything. So the store pick model is a really good model to start with a low-cost investment and gradually build up that business and broadly if you look at Asda, it was a -- it is been kind of a 15-year journey to get to a sizable business. And of course there's been investments along the way. But broadly Asda is operating margins are the same now as they were when they started that journey. So by default, they have managed to absorb the investment required and still run a profitable business while they developed an e-commerce business.

I think you can see in Asda's journey that they started with store pick, then moved to dark stores, then gradually started to increase the automation in the dark stores. And they will move towards, in a perfect world, a fully automated picking center that does that. I think the challenge is whether you can put the level of automation that you would need to get pick costs down into a DC where you were close enough to the customers that you didn't give all that benefit back in transport costs because you are shipping picked orders and a lot of fresh air around. That is the ultimate challenge.

But I think the nice thing for us now as we look across the globe, we can pick and choose from a number of different options. So Canada for example, we will look for much more store pick operation because the co-automations [ph] tend to be very centralized with big geographies in between. Mexico is much more of a store picked operations because that works.

So we will play with the portfolio and our goal is to go fast where we can and just use whichever one works for the time being. But we think it will move towards more automation over time.

A - Matthew Fassler {BIO 1509751 <GO>}

Great. Do have any last questions? Any hands raised? Great. We have a 10-minute break after which our sessions continue. But please join me in thanking Dave and the Walmart team for their remarks.