Barclays Global Consumer Staples Conference

Company Participants

- Brett Biggs, Executive Vice President and Chief Financial Officer

Other Participants

- Karen Short, Analyst, Barclays Capital

Presentation

Karen Short {BIO 7215781 <GO>}

All right. Well, good afternoon, everyone. My name is Karen Short, and I'm the staples and hardline retail analyst at Barclays. We're very pleased to once again welcome Walmart to the Barclays Staples Conference. Obviously, to state the obvious, with close to $550 billion in global sales, Walmart is the largest global retailer, at this point, cannot be emphasized enough, but equally important, the list of successful global brands is very short and clearly Walmart would be at the top of the list.

With us from Walmart, we're very pleased to welcome Brett Biggs, Walmart's Chief Financial Officer. As I think all of you know by now, the format will be fireside with no Q&A this year. You should see Walmart's Safe Harbor slide on the screen momentarily. Please refer to this and their latest SEC filings for forward -- any forward-looking statements that are made this morning.

On Tiktok, I would just like to point out and remind investors that Walmart is not elaborating on the topic beyond the public statement the company made on August 27th. So if anyone is listening and thinks that I'm not interested in asking about it, that's not the case. It's just we have 30 minutes. So we want to get as covered as possible.

So this is obviously a very unique time for any essential retailer. Again, we thank you very much for your participation and insights. So as the largest global retailer, you're obviously in a very unique position to get the pulse of the consumer. So I wanted to start off a little bit on whether or not you have any comments to make in general on the state of the consumer, and then I do want to ask this in the context of top line and market share in the US because this seems to be the biggest point of contention, I guess, as it relates to whether you are or are not losing share. And then I'll jump into some other questions.

Brett Biggs {BIO 17414705 <GO>}

Yeah, you bet. Thanks for having me. Looks a little different than last year, obviously, again, to state the obvious. As we think about the consumer, so much has changed in the last six months, so many dynamics. It's tough to peel through everything that's going on. You've had such disruption end of our first quarter, start of the second quarter, but in the same way, you had stimulus, a large stimulus, particularly in the US. And so understanding -- even in our second quarter results, I mean, some of that was stimulus; some of that was people spending money on things. They are not spending as much on vacations, gasoline, things like that, and so they would spend more in a place like Walmart. So it's tough to peel all those things apart.

The economic numbers over the last few weeks have seemed to look better than they have over the past. Again, it's hard to know how much of that is stimulus related and we'll be watching like everybody else what happens in Washington in the next several weeks around stimulus. But it's been a very interesting five or six months certainly from a retail standpoint with certain retailers closed; certain ones like us open.

When you look at the period of time overall, we feel really good about our business. We have got a lot of questions about market share. We know we've taken market share in certain categories, general merchandise, which is very good for us from a customer perspective as well as from a margin perspective. Grocery and consumable market share is a little tougher for us to read. There's a lot of things that have gone on. We'd say there's a lot of noise around the numbers.

We significantly pulled back on our operating hours, which you know. We started closing around 8:30 for most of the second quarter. Now we've taken those operating hours back to 10 o'clock. We know that impacted us some in the second quarter not having those operating hours like we had them, metering stores, things like that.

Price is still really important, but with the stimulus dollars that were in the market, convenience became even more important. We think during the quarter now, we've made a lot of inroads as far as convenience over the past several years and that benefited us, but I think people probably became a little less price sensitive maybe in the second quarter. And from an out-of-stock standpoint, we had some struggles as did a number of retailers in that second quarter. We're in better shape than we were a few -- certainly a few months ago and we're getting better every week, but there are certain categories that will take some time still to get back to where we want to be from an overall in-stock perspective.

Karen Short {BIO 7215781 <GO>}

On that note -- and I'm probably going to jump to Walmart+ fairly quickly, but on that note, in terms of the actual hour reduction and then in terms of the inventory, I think people may underestimate how much and how great the percent of sales are actually done at Walmart, say, from call it 8:30 PM to 7:00 AM and most are probably really understating the basis point impact on your sales. So maybe can you -- any color you could give on that?

And then on the inventory and the out-of-stocks, I mean, as you said in one of your earlier meetings, you obviously have become unbelievably efficient with inventory and you have probably basically just-in-time inventory, while you have all algorithms completely run out of whack. So is there -- could you talk a little bit about that? And I guess the ability to override the algorithm that you've obviously been operating under for so -- for decades?

Brett Biggs {BIO 17414705 <GO>}

Yeah. On the operating hours, I mean, we didn't -- we haven't quantified it externally, but it was important enough that we mentioned it quite a bit in our second quarter release. And I know there are times even as a customer, it's 8:30 and I wanted to go to Walmart, and for a few weeks there, we weren't open past 8:30. And so you really had to change your minds a little bit as a customer. I think we've got customers back now to where it feels a little more normal for customers.

The other thing to mention too would be pricing. And our price gaps in a number of categories actually widened in the second quarter. And so when you -- number of our competitors weren't as promotional in the second quarter or actually raised prices. We really didn't and that created some noise as well around on the market share side would be on the dollar -- the dollar basis.

On inventory, store managers do have some ability to override, but it -- there's two kind of large buckets of inventory. One will be short lead time. That would be food and consumables. And we can make adjustments on that pretty quickly, but you've got to have supply down the chain with our suppliers to be able to do that as well. And that was a challenge for a little while, even though they're doing the best they can as well. And there is longer lead time; think about holidays, Halloween, Thanksgiving -- not Thanksgiving, much Halloween and Christmas, where we're going to have to make bets a little further out. It's tougher to change those, so merchants have to make some assessments there.

The store managers do have some ability, but we're -- our systems are such that they can look at the demand by store and pretty quickly adapt to a shorter period of time. Now, the algorithms over the last few months -- you're not going to -- want to repeat those all the time, but they do learn pretty quickly.

Karen Short {BIO 7215781 <GO>}

Okay. So jumping to Walmart+, because that seems to be the number one topic, maybe talk a little bit about -- sorry, I actually want to take a slightly different angle than some of the things that you've been asked in prior meetings. I frequently get the comment that Amazon didn't break even until it reached a certain number of like -- whatever hundred -- I guess, call, a billion in sales. And so the comparison is that introducing this is going to only exponentially increase your losses. So I wanted to maybe see -- get your framework on that a little bit. I guess, I would argue that the Walmart behavior as a shopper is just very different from how people shop Amazon, but is there a risk that you train the customer to start shopping Walmart like they shop (inaudible)?

Brett Biggs {BIO 17414705 <GO>}

Yeah. I mean, there is a number of things that we considered as we looked at Walmart+. One, it's really important, we think, for us to offer this for customers, and now, members in Walmart+. Though the world has evolved -- customers evolved a lot over the last several years. And we've had a membership, whatever at Sam's Club, but people have got more used to using memberships, whether it's movies or streaming or other things that they do and we felt like this was the right time to give customers that option.

There is a number of things that we can do with this over time. So we've announced three main benefits at this point, but there'll be other things that we do over time. It was important to get the membership at the right price point where we thought would be good for our customers, which is under $100. So we feel good about that.

Customers are going to -- they're going to shop however they want to shop and we know that and we've been setting ourselves up for that for several years. We still love customers coming on to our stores and we think that's going be a big part of what we do forever. And so having the opportunity to pick up in stores, making sure that the Supercenters in particular, are a great place to shop. Those things are all going to continue to be important.

Basket size matter. We think we'll continue to have basket size. We think basket size will get bigger. We've seen that in grocery pickup where basket size are bigger than they are in the stores. And so that part is very different than what some of our other competitors might have. And now the ability to get increasing mindshare with that customer on the grocery and consumable side, and then be able to get more of their general merchandise business, which is great for us from a mindshare perspective and market share perspective as well as margin perspective, is a really important part of this.

Karen Short {BIO 7215781 <GO>}

So when you think about the demographics that this would appeal to, obviously a question has come up that -- and I have had this question asked, why would people -- why would a customer pay a fee when there's a minimum of $35. So maybe can you just talk a little bit about the thought process behind that, but also just talk a little bit about why you think this is something that will appeal to all demographics because I think the perception is that it's only a higher income demographic.

Brett Biggs {BIO 17414705 <GO>}

Yeah, it's what -- yeah, we wanted to appeal broadly. I mean, Walmart has always been kind of democracy for shoppers. If you look at the US population, we tend to mirror, from an income level, racial, gender, we kind of mirror America, and that's what we like and the same as we do in other countries. But getting that bigger basket, the baskets we're seeing with most of our customers for delivery or pickup have the $35 minimum wouldn't have seemed to have made that much of a difference, and it is a way for us to differentiate what we do from the way that we fulfill as well. So it does help us from a fulfillment standpoint, but we think we give the customers still what they want. So that, we think, is a win-win.

And it just -- we want to do things that fit our customer base, and we don't think this appeals one way or another to lower income or higher income. We do think it is really broad reaching, and that's what we like so much about it. We think we've got something in there for everybody and the price point is really attractive.

Karen Short {BIO 7215781 <GO>}

And when you -- I guess, you obviously started testing this before you consolidated the apps, but is there anything you could talk to in terms of the behavior and attachment rate pre the consolidation of the apps from a general merchandise perspective to currently? And then anything you could talk to in terms of what you're seeing on the behavior -- now that the consolidation of the apps is done?

Brett Biggs {BIO 17414705 <GO>}

Yeah. We won't talk about it specifically from a competitive standpoint, but you can imagine anything you can do to make it easier for that customer to go across the isle, so to speak, and buy general merchandise, the better. And that's why the Supercenter was such a great retail invention. It's because it brings people on to the store for food and consumables, but then as everything they need from a general merchandise side and it mixes out in a way that makes sense.

I don't think online is going to be that different actually, and as we continue to get people in for top of the funnel with food and consumables and things like Walmart+ will help us do that, we will become more top of mind on general merchandise. And we have really good, strong general merchandise business. We can make it stronger. The second quarter was a great reminder to all of us of what that flywheel really looks like when it works. And so what we've seen so far is we have made it easier for the customer to do that. There are things we'll continue to do that will make it even easier. I feel certain it will become I think a year from now that where we've made that easier than it is today.

Karen Short {BIO 7215781 <GO>}

Okay. And then you've commented a couple of times on the gap in price and our price checks at least in grocery definitely show widening of the gap. So I guess the question is, how do you think about when that gap will actually matter again? It just feels like consumers are selfless with cash on all things that they're not spending on. And if you're not necessarily getting credit where -- when do you think you will, I guess?

Brett Biggs {BIO 17414705 <GO>}

Yeah. There are some things that are a bit counterintuitive right now. The price gap always matters and the customer, they notice it is not as formulaic as we make it with the customer, the customer notices it. It still matters for sure. If we don't get another stimulus package, which all of us are monitoring like you are, price probably matters even more. We will get back to something at sometimes it feels a little more normal than this, I mean, price will matter.

Convenience matters more than it used to, and I think that's here to stay. We've seen some trends accelerate over the last five months that are here to stay; more people on e-commerce, probably more people eating at home, things like that. Some of those work and I think working to our benefit now, but the price gap is always going to matter and we're going to be thoughtful about it. There are price -- we want to find that optimal point where we're doing what we need to for customers, but also ensuring that shareholders get the benefit that they should see as well.

Karen Short {BIO 7215781 <GO>}

So on that cash topic, I don't know if you could answer this or not, but -- it seems that there may be a tax though coming for our many customers or many consumers who got the $600 stimulus weekly, meaning that there wasn't withholding taken out of that. I don't know if you've done any analysis on this at all, because it kind of -- I would venture to say if there is a tax though on that, it will just be subject to regular tax withholding, there are going to be a lot of shock to consumers in March. Do you have a view on that?

Brett Biggs {BIO 17414705 <GO>}

Nothing to specifically discuss. I think there are so many things right now that are unusual or that could have impacts down the road, as you say, first quarter, second quarter of next year that we'll just continue to monitor. How they all work together in aggregate to have an impact on the customer, I think we're just going to have to -- just to make our way through things like that as soon as that becomes an issue.

Karen Short {BIO 7215781 <GO>}

Okay. And then when you think about the 2020 holiday season, maybe talk a little bit about how you're thinking about that from a competitive perspective because on one hand, I could argue that the consumer is going to do anything and everything they can to make it as special as possible because everyone's so bored.

Brett Biggs {BIO 17414705 <GO>}

Right.

Karen Short {BIO 7215781 <GO>}

On the other hand, I could argue that you have Prime Day, combined with no real Black Friday, obviously no Black Friday really. So how do you kind of think and weigh those two factors?

Brett Biggs {BIO 17414705 <GO>}

Yeah. Our merchants -- we've -- basically the only thing we know so far is we'll be closed on Thanksgiving Day, which is something new for us. Glad we're doing that. And then we'll announce more as we get closer to the holidays. Thanksgiving is still two and a half months away, which in, today's world, seems like a long time, but there -- our merchants have -- on some of the long lead-time items we talked about a minute ago, they've made bets of where they think the holiday will come out. It will look -- holiday is going to look a lot different than prior years, as you said. How promotions from competitors workout over that period of time, I think, remains to be seen, but we feel good about how we're positioned for the holiday. I'm with you. I think people want to make this special and so I would expect things like -- I'm not head merchant, but I would expect things like trim a tree and other things like that, people want to decorate their homes, will probably be pretty big this year. We've seen that in other times when there's been a downturn in the economy that people really want to go all out for the holidays. And there'll be some places where it will be more conservative. And our merchants haven't been through something exactly like this, but we've had periods of time that have been either good or bad for the holidays from an economic standpoint. They're pretty good at knowing how to work their way through that.

Karen Short {BIO 7215781 <GO>}

Okay. And then maybe turning to e-com becoming less unprofitable, I guess, I think people are trying to -- struggling a little bit with what you think is about - in terms of what's structural in nature, in terms of more permanency or less unprofitable e-com business. Maybe can you kind of talk a little bit about the puts and takes of how we should all think about that going forward?

Brett Biggs {BIO 17414705 <GO>}

Sure. I think really over the last, I'd say, 12 months even, we've been talking about some positive things we were seeing on the profitability side from e-commerce. And there is -- there are just several levers within there. One is sales growth obviously. Two is increased -- or the increased rate of fixed cost; then there is variable cost of fulfillment, there's contribution margin. Those are four things that we watch really closely. A lot of tailwinds for the e-commerce business in the second quarter, but we have already seen some of those things in the first quarter, which makes us feel good that structurally we're making progress. Obviously, when you almost double the size of your business in the quarter, that helps from a -- helps leverage expenses all the way down the line. But the work that we've done over the past several quarters on getting more brands online, particularly in home and apparel and higher margin categories, it helps a lot with contribution margin, which, as you grow sales, and that actually just starts leveraging your fixed cost at a pretty rapid rate. And so that -- we were seeing that already last couple of quarters, but it certainly showed up in the second quarter. So it's those kind of things that structurally I feel good about where we're going that won't maybe all look as good as the second quarter did, but it was a demonstration to us that the way we're thinking about that e-commerce model is right and we saw what that looked like in the second quarter.

Karen Short {BIO 7215781 <GO>}

Okay. And maybe on that, can you just elaborate a little bit in terms of what capital, if any, would be required going forward with respect to Walmart+ fulfillment centers in general? And also maybe an update on how many SKUs you have on Walmart+ and e-comm, and whether or not those are all actually mirrored at all your FCs because I think that was the -- one of the two big points pre-COVID for you.

Brett Biggs {BIO 17414705 <GO>}

Yeah. We've made a lot of progress on mirroring. We have about 160,000 items that would be next-day eligible on -- I mean, same-day eligible on delivery and a little more than that on next day. So mirroring has come a long way over the last year. We haven't updated -- we'd said 200,000 plus. We haven't really updated that number in a little while and probably won't from a competitive standpoint, but that -- we feel good about the ability to get the customer what they want when they need it.

As we've talked about what capital could look like over the next couple of years, we've been kind of in this $10 billion to $12 billion range for a period of time. And I think, most years, that's probably about right, and there's some assumption there about increasing fulfillment capacity. Now what we've seen in the second -- first and second quarter, we can really get the e-commerce business ramped up if we wanted to. Maybe we add capacity faster than we had anticipated; maybe a year or two, that number goes up, but overall, I feel good about our ability to add capacity at a rate that makes sense from a financial standpoint.

Karen Short {BIO 7215781 <GO>}

And with respect to the FCs that you have now, those all have the capability to fairly meaningfully broaden the marketplace SKUs, correct, without incremental -- increasing the actual capacity or size of the facilities? That's my understanding.

Brett Biggs {BIO 17414705 <GO>}

Yeah. That'd be accurate. I mean, if -- as we continue, we had triple-digit growth in marketplace in the second quarter and we're also trying to ramp up Walmart fulfillment services, which would be taking third parties and running at their own fulfillment, but to the extent that that grows dramatically, that will be a good thing for us from a top of mind standpoint as well as profitability when you can get 3P and marketplace going more rapidly. So if that continues to grow like that, we'd be just fine adding fulfillment space. We'd be glad to do that.

Karen Short {BIO 7215781 <GO>}

Okay. And then I guess in terms of overall margin structure, I mean, I think it's obviously known and documented with every investor that we should always kind of expect US gross margins to be down, and that's certainly what you get credit for. How do you think about that though going into the second half just, again, given that your price gaps are so wide and you're not really getting credit for it at the moment? Maybe a little color on how to think about that.

Brett Biggs {BIO 17414705 <GO>}

Yeah. We got a little bit of a shift in the second quarter of gross margins going up, and a lot of that was mix, as I talked about. Yeah, I think -- you know what, I think I've said to you before even, Karen, that we need to be able for margin -- gross margins to go down over time. To some degree, markets and customers will determine where that margin rate goes. And that's why I've been so focused on expenses, is being able to get our expense and cost structure in a point to where gross margins could come down some over time and our operating profit margin maintain where we're at or even potentially go up a little bit. That's -- that model works because if we can do that and grow the top line, you get that -- you've seen we can do it at 3% and 4% growth. It's just such big dollars that it leverages dollars. Even if the rate stays the same, the dollars grow pretty dramatically.

Could margins go up? If we -- our general merchandise -- I mean, if our general merchandise business performs like we hope it can over the next two to three years, there's room for that to happen, but that also would give us the opportunity to invest back in some other things that would help the business longer term. So there is a lot of optionality, I think, we create with the focus we've had in expense leverage, and it's still there, and that optionality is important.

Karen Short {BIO 7215781 <GO>}

And maybe with respect to expenses, I guess, can you just remind us how we should be thinking about COVID-related expenses into the third quarter or back half? And then how are you thinking about wages obviously in light of Target's announcement and just broader wage pressure?

Brett Biggs {BIO 17414705 <GO>}

Yeah. So on the COVID-related expenses, we had $1.5 billion roughly in the second quarter and about three quarters of that were related to pay and benefits. So we had two special bonuses that were in that number, and then also some things we've done around sick pay and time off for people who either are concerned about COVID or have COVID emergency leave time. So there'll be some expenses that continue, I think, probably for quite a while. Things around sanitation, maintenance, anything we need to do for customer and associate safety, we'll continue to do that. So there's some level of that that's going to continue probably for a period of time, but not the level you've seen at Q1 and Q2. On the wage front, we're just always, always watching it. We have to be able to recruit good talent. We have to be able to retain people, really have to look at it geography by geography. I don't think looking at a rate across the nation is -- firstly, I don't think is the right way to look at it. I think you've got to look at it by geography. And so there are places that are hotter than others from a wage perspective, and we're being competitive in those markets. There are certain types of positions where we're going to make sure that we are really competitive to ensure we're getting the right talent in those areas, but it's something that just -- it takes constant minding and paying attention to.

Karen Short {BIO 7215781 <GO>}

Right. Okay. And then I guess, thinking about capital allocation, I can think of one retailer so far in this coverage -- my coverage that has announced resuming buybacks, and I know where you stand currently, but maybe how should we kind of think about that? Is that something that we should not expect until we're back to whatever normal it is?

Brett Biggs {BIO 17414705 <GO>}

Yeah. We haven't talked specifically about buybacks. You saw -- I mean, you have seen that we didn't do any buybacks in the second quarter, but it's not something that you're likely going to ever say we're off or on. It's -- we want to be more nimble than that. The way we think about capital hasn't changed. We're going to continue to put significant amounts of capital into the business. And when you look at our operating cash flow over the last five years, there have been $25 billion to $30 billion in cash flow. And when you look at the capital we spend of, say, 10 to 12, and the dividends of around 6, which we're very committed to that, still leaves you a lot of room from a cash flow perspective. We've been buying back significant amount of shares. And there's a number of things that go into that decision on a quarterly basis. I still feel really good about the value of the company. So share buybacks is something that is certainly mid to long term. We're -- I feel like it's an important part of how we spend our capital.

Karen Short {BIO 7215781 <GO>}

And just remind us, in terms of that, if there were a decision where you resume the buyback, you have a grid in place in terms of how you proceed or maybe just to remind people how that would work.

Brett Biggs {BIO 17414705 <GO>}

Yeah. That's typically what we do is we always have a share repurchase grid based on buying at certain levels of price on the stock, which is pretty typical of what most companies do.

Karen Short {BIO 7215781 <GO>}

Okay. And then maybe a last question just in terms of e-comm. Obviously, you've indicated in the past that you're definitely willing to look at larger scale acquisitions on e-comm that are transformative, but you've also been divesting some of the e-comm assets. So I think Shoes.com, (inaudible) Bare Necessities. Obviously, Jet --

what happened with Jet. Maybe just -- maybe end with how you think about that from a strategic perspective.

Brett Biggs {BIO 17414705 <GO>}

Yes. I think there is -- certainly, if we have opportunities to -- from a brand perspective or from a technology perspective, people perspective, those are the types of acquisitions that would -- they're enabling-type acquisitions, we will continue to look at those. And we're just making decisions more quickly than we used to. And so in the example of Bare Necessities and Shoes, both of those acquisitions helped us make significant progress in those categories from a brand perspective, in stores, online. And so we benefited a lot from those acquisitions. And there is times where we're going to get the value that we think we need out of acquisitions and it makes sense for someone else to own them going forward, and to continue to focus where we want to focus, we'll make the decisions to not focus in places where we don't want to focus, but those categories are critically important to Walmart.

Karen Short {BIO 7215781 <GO>}

Well, I think maybe we are close to the 1:10 -- well, we are on the 1:10 mark. So this is news to me in terms of how we get cut off. I don't want to suddenly get cut off and (inaudible) Zoom Meeting. So thank you very much...

Brett Biggs {BIO 17414705 <GO>}

Thanks, Karen.

Karen Short {BIO 7215781 <GO>}

...for being with us, and I'll see you again shortly in the next meeting.

Brett Biggs {BIO 17414705 <GO>}

Yeah. Thank you. Take care.

Karen Short {BIO 7215781 <GO>}

Okay. Everyone.