

Greetings and welcome to Walmart's Fiscal Year 2018 Fourth Quarter Earnings Release. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

I'd now like to turn the conference over to your host Steve Schmitt with Investor Relations. Please go ahead.

**Steve Schmitt.**

Thanks, Rob. Good morning, everyone, and thank you for joining us today to discuss Walmart's fourth quarter and fiscal year 2018 results. Joining us on today's call are Walmart President and CEO, Doug McMillon; and CFO, Brett Biggs. Doug and Brett will have some opening remarks in a minute, and then we'll take your questions. We'll do our best to get to as many of you as possible.

We're excited to be hosting this call today. You may have seen in our press release announcing this call that we've made a process change to have a live earnings call with executives in conjunction with our fourth quarter results going forward.

It feels appropriate that we share our thoughts as we wrap up one year and begin another. Also, this timing is well spaced from our June and October meetings. We plan to follow our typical earnings release process for other quarters during our fiscal year.

Now before I turn the call over to Doug, let me remind you that today's call is being recorded and will include forward-looking statements. These statements are subject to risks and uncertainties that could cause actual results to differ materially from these statements. These risks and uncertainties include, but are not limited to, the factors identified in our earnings release and in our filings with the SEC. Please review our entire safe harbor statement and non-GAAP reconciliations on our website at [stock.walmart.com](http://stock.walmart.com).

And with that, it's my pleasure to turn the call over to Doug McMillon.

**Doug McMillon**

Good morning, and thank you for joining us today. We just completed an exciting year with solid fourth quarter results and continued momentum in the business. On a constant-currency basis, total revenue grew approximately 3% both in the quarter and for the full year. We reached more than \$500 billion in revenue for the fiscal 2018 for the first time as a company.

For the quarter, Walmart U.S. delivered strong comp sales growth of 2.6% due primarily to improved comp traffic growth in stores of 1.6%. Strength was broad-based across merchandising categories, formats and regions, and holiday sales were solid. In addition, comp store inventory declined again for the 11th consecutive quarter so we're well positioned as we begin the year.

Sam's Club comps improved to 2.4%, and in International, 9 of 11 markets posted positive comp sales. So overall, we were pleased with most aspects of the quarter and confident in the foundational aspects of the business as we enter this new fiscal year.

Walmart U.S. eCommerce sales growth in the fourth quarter was 23%, down from 50% in the third quarter. The majority of this slowdown was expected as we fully lapped the Jet acquisition, as well as created a healthier long-term foundation for holiday. A smaller portion of the slowdown was unexpected as we experienced some operational challenges that negatively impacted growth.

Overall, we finished the year with eCommerce sales growth of more than 40%, so we feel better about the year than the quarter. Looking ahead, we expect eCommerce growth to increase from the fourth quarter level as we enter the New Year with about 40% growth for the year.

We're confident in our strategy to transform the company, and we continue to be guided by four key objectives: make every day easier for busy families, change how we work, deliver results and operate with discipline and be the most trusted retailer.

We're accelerating innovation in the business to make shopping faster and easier for our customers. Creativity, decisiveness and speed are priorities. We made good progress this past year to save busy families time and money, and we'll do more.

By becoming stronger at mobile and leveraging digital capabilities, we improved in-store experiences, including our pharmacy and money services areas. We enabled Easy Reorder online. We're making the checkout experience easier with Scan & Go and also digitizing the returns process.

We made acquisitions to improve our online assortment, and we're partnering with others like Google and JD in new ways. We're expanding Online Grocery in the U.S. and around the world and broadening our delivery capabilities in the U.S., China and other international markets.

It's really all about providing more convenience for customers. Customers that shop across all channels are important to us. As we said in October, U.S. customers that shop us in-store and online spend nearly twice as much

as customers that only shop with us in stores. Their loyalty to Walmart strengthens overall.

Online Grocery customers are a great example as they spend more with us in total once they start using the service. So we'll lean in this year by nearly doubling the number of Online Grocery locations in the U.S.

We're also becoming more efficient by changing the way we work, including leveraging technology to equip and empower our associates to be successful. They now have better information, tools and training.

Finally, we're always striving to earn and maintain trust. We're focused on not only helping our customers save money and live better but also on creating shared value for our business and the communities we serve.

In his remarks, Brett will go over the financials and guidance. This will include an overview of the benefits of tax reform and the strategic choices we're making to further strengthen our business.

Tax reform gives us the opportunity to accelerate plans for the U.S. You may have seen our announcement last month about investing some of the proceeds in better wages and benefits for more than 1 million U.S. hourly associates. We'll also continue to lower prices for customers, improve technology in our business and accelerate grocery delivery in the United States.

Now let's get into more details for the segments, and I'll start with Walmart U.S. We had a strong year of top line growth, and we're seeing signs that the productivity loop is turning. In our stores, we're making shopping easier and equipping associates to serve customers more efficiently.

In the fourth quarter, we took steps to restructure our store leadership teams and corporate support areas to be more nimble. We're becoming more efficient, and it's contributing to the expense leverage that physical stores have delivered all year.

Beginning this week, we increased the U.S. starting hourly wage rate to \$11. We're also proud to announce adoption benefits for associates that went into effect earlier this month in addition to expanded paid parental leave for all associates that will take effect in March. Investing in our associates will help us attract and retain talent in the future.

In addition, we've invested in nearly 200 training academies that have further developed the retail skills of more than 250,000 associates. So our stores are executing better. We're innovating more. We're lowering prices and customers are responding with higher sales and traffic. As I mentioned

earlier this has also been a year of good progress in ecommerce. We launched free 2-day shipping on Walmart.com, and customers continue to love Online Grocery pickup. We're expanding our test of same-day and next-day delivery, and our Walmart.com assortment has grown to nearly 75 million SKUs.

Acquisitions like Bonobos and ModCloth bring unique, private-branded products to our shopping experience. In addition, partnerships like the agreement with Lord & Taylor will help create specialty experiences that complement our own assortment with more brands customers want.

Jet.com complements Walmart.com nicely. Walmart.com, including Online Grocery, is and has been the key driver of our eCommerce growth and that will continue. The Jet brand over indexed with higher-income, urban, millennial customers when we made the acquisition, and we intend to build on that strength going forward.

The cost to acquire a new customer on a nationwide basis is cheaper with the Walmart brand so we've been investing more in Walmart.com on a national basis and reducing marketing investment in Jet, except in certain urban markets.

Due to this change, Jet will not grow as quickly as it did in early days but it will be well positioned where we've chosen to focus the brand. We'll continue to evaluate ourselves on the total U.S. eCommerce growth number.

Moving to Sam's Club. You'll remember that we made a decision to close 63 Sam's Club locations in the U.S. We've talked about transforming the Sam's business, and part of this transformation means managing the club portfolio to include clubs that are both financially viable and that fit within the strategic framework for the future.

Closing stores and clubs is difficult. It's obviously difficult for our impacted associates, and there is never a good time to do with. John and the Sam's team are working to place as many of them as possible at nearby locations. These closures will help us run a healthier business.

We also took additional steps recently to align resources around the initiatives that are most important to our members. We enhanced the value of the Plus membership with a free shipping proposition. We also made the decision to remove tobacco from certain clubs.

In addition, Sam's Club changed its merchandising structure to encourage more expertise and continuity in buying roles. The strategy continues to come to life, and we're already seeing progress.

Our International team continues to deliver consistently solid results. While Walmex led the way this year, our good performance was broad-based. In fact, 10 of our 11 markets posted positive comp sales for the year, and 5 of those markets grew comp sales by more than 5%.

To give a little more detail, Walmex comp store sales increased 6% this year, and we're really proud of how the team is combining our stores with eCommerce to deliver a convenient, seamless shopping experience.

As we mentioned in our October Investment Community Meeting, there's more work to be done on the portfolio. We've set priorities, focused our - on our North American core and key growth markets, including China and India.

During the fourth quarter, we made the decision to wind down the Brazil first-party eCommerce business. We always want our resources aimed at winning in the most strategic places.

So overall, the International segment continues to make steady progress as we find new ways to serve customers more effectively through stores and eCommerce.

In conclusion, we have a plan that leverages our unique assets and strengths to benefit customers and shareholders. It's resulting in momentum. We're being disciplined about cost and capital, and we're acting faster as a company but are pushing to increase our speed.

Thank you for your interest in Walmart. Brett, you want to pick up there?

### **Brett Biggs**

All right. Thanks, Doug. Good morning, everyone. We're pleased with the company's performance during the fourth quarter and for the full year. We've made progress on several fronts, and we have good momentum across the business as we enter the new fiscal year.

Adjusted EPS for the quarter was \$1.33 and \$4.42 for the fiscal year. GAAP EPS of \$0.73 for the fourth quarter and \$3.28 for the fiscal year was negatively impacted by a number of discrete items totaling \$0.60 and \$1.14, respectively.

Most of these items position the business for more efficient growth going forward, including closing 63 Sam's Clubs locations to create a more viable fleet and healthier business.

In addition, we discontinued real estate projects in the U.S., following our decision to open fewer stores and clubs, with greater emphasis on comp sales and eCommerce growth.

We also completed our third bond tender of the year to take advantage of more favorable interest rates. A full reconciliation of GAAP EPS to adjusted EPS is included in today's earnings release.

During the quarter, we had additional EPS headwind related to some smaller unplanned items and expenses we incurred as we pulled forward initiatives in order to take advantage of a higher tax deduction. These were only partially offset by slightly more favorable currency exchange rates.

Before we get to the results, I'd like to highlight some accomplishments for the full year. Total revenue surpassed \$500 billion for the first time and increased \$15.1 billion or 3.1% in constant currency.

Walmart U.S. comp sales grew 2.1%, the highest growth rate since fiscal 2009, led by traffic growth of 1.4%. Walmart U.S. eCommerce sales grew 44%, reaching \$11.5 billion. We made good progress on expenses, especially in Walmart U.S. stores and International. Without the discrete items mentioned in arriving at adjusted EPS, we would have leveraged expenses.

Adjusted EPS increased 2%. Operating cash flow was \$28.3 billion. The company returned \$14.4 billion to shareholders through dividends and share repurchases, and strong working capital improvements continued.

Let's move on to the quarter. We delivered a solid quarter to finish out the year as constant-currency revenue grew 3.1% to \$135.1 billion. Comp sales were positive in all 3 segments with growth of 2.6% and 2.4% at Walmart U.S. and Sam's Club, respectively.

On a 2 year stack basis, comp sales accelerated for the third consecutive quarter for both of these segments at 4.4% and 4.8%, respectively. Even more encouraging is that these results were driven by strong in-store traffic. International grew net sales 2.8% in constant currency, led by strength at Walmex.

Consolidated gross profit margin declined 61 basis points. Approximately two thirds of the decline was driven by price investments in certain markets and the mix effect from our growing eCommerce business. The remaining one third was driven by Sam's Club inventory markdowns associated with closures and other International items, including the wind down of our Brazil first-party eCommerce business. Looking ahead to fiscal 2019, we'll continue

to make investments that will pressure the rates some but not to the extent of this quarter.

Similar to our full year results, SG&A and operating income were significantly impacted by charges for discrete items. Excluding these items, we would have leveraged expenses in the quarter and operating income would have decreased less than 1%.

Let's move on to U.S. eCommerce. As Doug mentioned, the slowdown in growth during the quarter was a bit more than we planned. Looking ahead, we have a number of new initiatives planned for the year. We expect eCommerce growth to increase from the Q4 level as we enter the New Year, with about 40% growth for the year.

Now let's discuss the results for each operating segment during the quarter, beginning with Walmart U.S. The U.S. team continued to produce strong top line growth. Customers are responding well to our everyday low prices and the convenience we're providing through a variety of initiatives. All store formats had positive comps, and we saw strength in key categories with increased customer traffic and units.

During the fourth quarter, comp sales increased 2.6%, led by traffic growth of 1.6%. Comp sales performance on a 2 year stack was the best in 8 years, and eCommerce contributed approximately 60 basis points to the segment.

Gross margin rate declined 50 basis points in the quarter due primarily to price investments, higher transportation expenses and mix effects from our growing eCommerce business.

Also, the team leveraged operating expenses slightly even when considering adjustments for discrete items in both current and prior year periods. Overall, we like the momentum we see in Walmart U.S. Our strategy is working, and customers are responding.

International had another solid quarter. The teams around the world have done a nice job of delivering top line growth through a focus on price as well as strength in fresh and private brands. Growth was broad-based across the markets, and results at Walmex were particularly strong.

Overall, net sales in constant currency increased 2.8% and grew 6.7% on a reported basis. Changes in currency rates benefited net sales by approximately \$1.2 billion. It's also important to note the divestitures of Yihaodian and Suburbia created a headwind to sales of about \$400 million when compared to last year.

From a profitability standpoint, fourth quarter operating income decreased 16.1% in constant currency and 10.9% on a reported basis. As detailed in this morning's release, restructuring and impairment charges in certain markets negatively impacted operating income. Without these items, operating income would have increased year-over-year.

Overall, we're pleased with the consistent performance we've seen from our International business, and we feel good about the year ahead.

Sam's delivered solid top line results. Comp sales without fuel increased 2.4%, led by traffic increase of 4.3%. Tobacco negatively impacted comp sales by 120 basis points. ECommerce growth was solid and contributed 80 basis points to the comp.

Also in the eCommerce space, the team recently announced the free shipping offer from SamsClub.com for Plus members. The team is moving quickly and making decisions that we believe will benefit our members and the business over time.

I'll close today with guidance. As always, we have a number of assumptions on our guidance, including the economic conditions and the tax and regulatory landscape, and our largest markets remain generally consistent.

You'll recall that we issued fiscal year 2019 guidance last October at our meeting for the investment community. Since that time, we made some decisions and assessed other potential opportunities to accelerate investments, particularly - primarily as a result of tax reform.

Let me start with our expectations related to tax reform. Our estimates are based on available information and our current analysis regarding the application of the new law.

We expect our effective tax rate for fiscal 2019 to be 24% to 26% compared with our previous guidance prior to tax reform of 32.5%. Our global blended rate is higher than the new U.S. federal rate due to state taxes and taxes we pay outside of the U.S.

In terms of cash flow, in addition to the income statement benefit from a lower U.S. tax rate, we expect an additional cash tax benefit due primarily to accelerated depreciation.

Including all aspects of tax reform, we currently expect a cash benefit of around \$2 billion for the year. Additionally, we are reviewing our cash positions overseas in light of the new law but have not made any decisions regarding potential repatriation.



Our priorities for capital allocation remain unchanged. We'll focus first on investing on our business and other growth initiatives. We also remain committed to our dividend, as evidenced by the increase we announced today. And we announced a \$20 billion share repurchase program back in October.

We've consistently talked about investing in the business for the long term while balancing near-term results. As tax reform is taking shape, we took the opportunity to step back and assess various aspects of the business, including potential investments. We will continue to be aggressive but thoughtful to ensure we win long term.

We recently announced some additional investments related to increased wages, training and benefits for our associates in the U.S. In addition to that, we'll look to accelerate investments in our customers through lower prices, and we'll make investments in technology, supply chain and eCommerce to better position the company for the future. We'll also continue to prioritize winning with customers in our grocery and fresh business, ensuring we make shopping with us simple and at a great value.

At the October meeting, Doug talked about some decisions we had in the Q, but it was too early to comment further at that time. During the quarter we took several actions, including: a wind down of the first-party eCommerce business in Brazil, the closure of 63 Sam's Clubs locations in the U.S. and the decision to remove tobacco from certain locations at Sam's. These decisions impact the guidance we gave in October, particularly in regards to total sales growth, so I'll quantify the impacts and compare back to the October guidance.

Let's first talk about Brazil eCommerce. We expect a headwind to sales of approximately \$500 million related to the wind down of the first-party portion of the business. In terms of profit, the benefit of fewer operating losses will be largely offset by onetime costs associated with the wind down.

As for Sam's, we anticipate a negative impact to sales of about \$6.3 billion related to the decisions to close clubs and remove tobacco from certain locations. Additionally, recall that we sold our Suburbia business in Mexico in the second quarter of last year, and this will create a headwind in the first quarter of this year.

The combined top line impact of these items will negatively impact consolidated net sales growth by about 140 basis points. And as a result, we now expect net sales growth to range between 1.5% and 2% in constant currency. Adjusting for these changes, this growth compares to the guidance of at or above 3% that we provided in October.

As for comp sales, we expect growth at Walmart U.S. of at least 2%. Sam's Club comps excluding fuel and tobacco should range between 3% and 4% and flat to negative 1% when including the impact of reduced tobacco sales. We expect International total net sales growth to be around 3% in constant currency.

Our October guidance for fiscal 2019 also included expectations for expense leverage, relatively steady operating income margin and EPS growth of around 5%. The incremental investments mentioned earlier will pressure operating expenses more than anticipated in October.

On a consolidated basis, we still expect to slightly leverage expenses but not to the extent we originally planned. Excluding the impact of the reduction in Sam's Club sales, leverage would be stronger. Overall, cost management is continuing to improve across the business, and we remain pleased with the progress.

As for operating margin, we expect consolidated operating income as a percentage of net sales to be approximately 4.3% to 4.4% in constant currency, resulting in a low single-digit percentage decrease in operating income versus operating income this past year, adjusted for the discrete items.

Considering all of these items, we expect full year EPS to be in a range of \$4.75 and \$5, an increase of 7% to 13% compared with adjusted EPS of \$4.42 in fiscal 2018. This range represents an increase from the guidance given in October.

Additional guidance is included in the materials we issued this morning, so please reference these documents as you analyze our outlook. Going forward, we're moving to an annual guidance framework with quarterly updates as warranted.

We considered a number of factors when making this decision, including management's long-term view of the business, the transformation of the business, the investment time horizon of many of our shareholders and the uncertainty of the timing of investments during the year.

There could be fluctuations within the quarters, but we believe EPS growth will be relatively consistent across the year. We look forward to updating you on our progress throughout the year.

So with that, I'll close by saying thank you to our shareholders for your support of Walmart. And now I'd be happy, along with Doug, to take your questions.

## **Question-and-Answer Session**

### **Operator**

Thank you. [Operator Instructions] Thank you. And our first question comes from the line of Simeon Gutman with Morgan Stanley. Please proceed with your questions.

### **Simeon Gutman**

Thanks. Good morning, guys. And thanks for doing the call. My first question is on the e-com growth in the fourth quarter relative to next year. You mentioned some operational issues. Can you elaborate and then talk about what gives you confidence that the e-com run rate will accelerate heading into next year?

### **Doug McMillon**

Hi, Simeon. This is Doug. Happy to elaborate a bit more. First of all, I would say that, as we try to communicate in our remarks, most of that was expected and planned. As we came around the fourth quarter and looked at what we did last year promotionally, realized we're lapping Jet for sometime now, we've expected a lower growth rate.

The minority of the miss that was more operational in nature that we're referring to is related to the fact that, during the seasonal spikes, seasonal inventory, think electronics, toys, gifts, things like that, came into our fulfillment centers and there was enough cube that it harmed our basic in-stock on more everyday items, and our basic in-stock for eCommerce suffered as a result.

So we're learning how to deal with higher volumes and learning how to deal with a higher peak than what we had previously. But again, that was the minority of the issue. Most of this was planned and in our numbers.

### **Brett Biggs**

And Simeon, just to remind -- this is Brett. As a reminder, in October, we've guided to \$11.5 billion of revenue for Walmart U.S. eCommerce, and that's just about where we came in for the year.

### **Simeon Gutman**

Okay. And then if I can ask my follow-up. Brett, you mentioned you were doing the comparison with pre- and post-October guidance. So I think at that point, EBIT was supposed to be up maybe low single digits, and now it's going to be down a little bit.

Can you just tell us if the entirety of that change is tax reform spending? Or is any part of it reflective of higher cost in the business in some form or another?

**Brett Biggs**

Yes, Simeon. I still remain -- feel good about the cost management in the business, and we're making progress there. When we've given guidance back in October, we've talked about an operating income range that would be similar to where we had kind of been.

So as we step back and we looked at everything, we've decided to make these investments that we talked about, and that's all included in the guidance that's there today.

And so it's -- that one is a little bit tougher to compare pre and post, but when you look at the investments that we're making, that is the difference. But I feel good about the overall cost management side of the business.

**Steve Schmitt**

Thanks, Simeon. Rob, next question please?

**Operator**

Our next question comes from the line of Robbie Ohmes with Bank of America Merrill Lynch.

**Robbie Ohmes**

Good morning, guys.

**Doug McMillon**

Hey, Robbie.

**Robbie Ohmes**

So a follow-up on Simeon's just - and then on gross margin. So I just wanted to get clarity on the eCommerce growth outlook. So the first question is just, where -- the confidence in the eCommerce growth going back to roughly 40%, are you seeing that already in the first quarter? And sort of what is the difference to get back to the 40% versus the fourth quarter?

And then could you tie that into the gross margin outlook you gave? Maybe some thoughts on where you might be investing in price. And also, I think

the guidance, Brett, was that gross margin rate would be down less in fiscal '19. So if eCommerce is going to reaccelerate to a sort of 40% type growth rate, why wouldn't we see more pressure on gross margin? Thanks.

### **Doug McMillon**

Thanks, Robbie. This is Doug. I'll start with the eCommerce question, and Brett can elaborate on it too if he would like to. We're not expecting the first quarter to go all the way to 40%. We think it'll start to ramp up from the fourth quarter to approximately 40% for the year. We're going to continue expanding our eCommerce business as it relates to food. Online Grocery's ramping up.

As we've said, we're going to almost double the number of locations that do Online Grocery. That will drive eCommerce growth to a certain level. And then on top of that, we've got the activity planned for both Walmart.com and Jet. So we've got an investment plan there.

We have an assortment plan and other innovations, as you saw last year, that will be occurring as we go through the year. So we think by the time we get to the end of the year and look back at the number for the total year, it will be approximately 40%.

### **Brett Biggs**

Yes. Robbie, I'll comment more on gross margin. As we've talked about before, there's a number of things that impact gross margin. Price, shrink, transportation expenses, all of that go into that. And so as we've said before, it's tough to look at gross margin quarter-to-quarter. I think you have to look at it on a longer base. And what I'd said in my comments is that we expect that next year's decrease won't be what we saw in the fourth quarter.

And if you look at where we've guided operating income and the comment we've made about slightly leveraging expenses, you can kind of back into what -- a bit of what we're expecting from a gross margin perspective. So we do take into consideration the mix of the business.

We'll continue to be aggressive but thoughtful on pricing, where we invest, how we invest, both in stores and eCommerce, but we'll be thoughtful about those investments.

### **Steve Schmitt**

Thanks, Robbie. Rob, next question please?

## **Operator**

The next question is from the line of Karen Short with Barclays.

## **Karen Short**

Hi, thanks. Just two clarifications and then a bigger picture question. So on the gross margin, the comment that you expect next year's decrease won't be where you were in the fourth quarter, is that including or excluding Sam's? So is that the 61 basis points or around 40?

## **Brett Biggs**

That's all in next year as far as gross margin rate.

## **Karen Short**

Okay. And then I know you kind of said that your comments on earnings growth will be - the cadence growth rate will be similar throughout the year. Is that fair to say, for U.S. comps, you don't really expect a lot of volatility throughout the year?

## **Brett Biggs**

Yes. I don't expect a lot of volatility throughout the year. Overall, for the year, we expect it to be 2% or higher, but I don't expect a lot of volatility during the year, Karen.

## **Karen Short**

Okay. And then I guess I wanted to just turn to the color in terms of acquiring customers on Walmart.com versus Jet.com. Is it -- I guess, is it fair to say then, since you're switching to, I guess, a lower-cost customer to look to acquire, is it fair to say that eCommerce losses have kind of bottomed? Is it still consistent with what you previously said that eCommerce losses have bottomed in '18?

And then I guess, bigger picture, is there any color on Jet? Like do you feel as good as you have always felt in terms of the prospects for Jet and this is just pure math, it just makes more sense to go after the Walmart.com customer?

## **Doug McMillon**

Yes. Karen, this is Doug. Great questions. I think as we look at this year, we're trying to preserve flexibility as we go through the year to decide what level of investment we want to make in eCommerce as we go month to

month and quarter-to-quarter. It's possible we may choose to lose a little more in eCommerce this year than we did last year, but generally speaking, we think it'd be about the same level of losses.

Our visibility into picking costs, shipping costs, margin rates, the cost to acquire a customer and how the different cohorts are behaving as we make the marketing investments is really improving, and I'm excited about all the levers that are there. And we're -- we again are trying to preserve some flexibility to make choices as we go through.

As it relates to the brands, Walmart is just a really well-known brand for value throughout the country. And when you get into Oklahoma and Texas, in the middle of the country, it just makes a lot of sense to invest in that brand rather than investing higher incremental dollar to introduce a brand that's less familiar.

Now on the other hand, if you take the New York metropolitan area as one example, not the only one, the Jet brand is really well known, has a lot of traction, has appeal, as we mentioned earlier, to urban, millennial, higher-income customers. So it's really just a positioning choice, and that choice was made before we made the acquisition.

I think we wanted to leave our minds open as we acquire Jet to make the best choices about how we use the brand and where we position it. But our thoughts before we bought it that basically become confirmed, that Jet plays a great role reaching parts of the country and selling, in some cases, some brands that are not ready to sell on Walmart.com.

So I think what you'll see is Jet will go through a period of adjustment and then it'll start to grow again in the future but focused on specific markets and opportunities, whereas Walmart will be the broad-based, big part of the business, and growing it will be a priority.

**Karen Short**

Thank you.

**Steve Schmitt**

Rob, next question please?

**Unidentified Analyst**

And if I could just ask...

**Steve Schmitt**

We're limited to just one question, just to get through as many as we can, please. Thanks.

### **Operator**

Thank you. Your next question comes from Oliver Chen with Cowen & Company.

### **Oliver Chen**

Hi. Thank you. Regarding eCommerce and the road ahead, what are your thoughts on profitability and the smart baskets and pricing and how you're thinking about grocery pickup as well as supply chain in the context of bricks post clicks?

And would love your thoughts on eCommerce M&A and on correlated assets as you've been quite creative about thinking about how to build this business over time? Thank you.

### **Doug McMillon**

Yes. Let's break it into pieces. This is Doug. I'll try to do so quickly. If you look at this business, look at it for the quarter or for the year, I think the first thing to always remember is we've got this really big and now strong business in U.S. supercenters. Our comp traffic's up. We're in a really strong foundation there, playing more offense than before. So the big part of the company is in good shape and foundationally strong.

Now we've got Sam's to a point where it's starting to get repositioned. We'll see more traction and improvement in that part of our business.

Internationally, the big businesses at Walmex, Canada and even the U.K., which is a big part of our International business, has been stronger lately. So kind of those big platforms are there and stronger, and I wouldn't want us to spend this whole call talking about a smaller part of the business, although it's of vital strategic importance.

So now let's click to eCommerce. In the U.S. specifically, and don't forget we've got food eCommerce opportunities around the world, but let's focus just on the U.S. for a second, we've got this tremendous advantage of having the stores and the supply chain that put us within 90% of U.S. customers within 10 miles. So you can build on that to build a strong food eCommerce business, and that's what we're doing.

Learning how to pick in-store enables Online Grocery. Learning how to pick in store enables delivery, which we'll continue to expand and learn more about as we go through the year.



Now let's click to the part of the eCommerce business that doesn't come out of our stores. That's where you get into eCommerce fulfillment centers, the opportunity to leverage smart cart to build an eCommerce basket, not just selling eaches. Like selling a television at cost for Cyber Mondays, not all that exciting as it relates to being a way to make money, but driving baskets on eCommerce is.

So you'll start to see smart cart functionality move over to Walmart. You'll see us continue to make assortment improvements to bring in new brands, be more increasingly open to not only the Jet brand but the Walmart brand.

So as that happens, your mix starts to change, and you're selling a basket and a more profitable basket. To do that, there are times when an acquisition makes sense because it accelerates the improvement that you can make in your assortment.

It might take us longer, for example, to do it organically. There's so many suppliers and so many brands to acquire to get on the platform. So some of the acquisitions we've made have been specifically aimed at assortment, and I would expect that some of that will continue.

**Steve Schmitt**

Thanks, Oliver. Rob, next question please?

**Operator**

Next question is from Chris Horvers with JPMorgan.

**Chris Horvers**

Thanks. Good morning. A follow-up question on gross margin. So can you talk about the 60 basis point decline in the U.S.? Where was that relative to your expectations going into the quarter?

And then what aspects of those buckets moderate as you look to the upcoming year such that the gross margin degradation improves? Thank you.

**Brett Biggs**

Yes. Chris, this is Brett. As we mentioned earlier, so the 60 basis points you mentioned was total company, and there is about third of that, that was related to the Sam's Club closures as well as the Brazil eCommerce shutdown and a couple of other things inside of International. So it was -- about third of that was onetime type items.

In the U.S., again, there's just so many things that go into margin in a quarter, pricing, shrink, transportation costs. And so quarter-to-quarter, I think, gross margin is challenging to look at and try to compare it on a quarter-to-quarter basis. We're going to continue to invest in price. We've been investing in price.

As you know, we always invest in price. But we've been investing in price over the last couple of years, and so we're now 2 years into that. So there's just different pieces of it. I don't want to get into specific pieces from a competitive standpoint, but we feel confident that the gross margin decrease that we will see next year will be less than what we've seen in the fourth quarter.

### **Doug McMillon**

Chris, this is Doug. I'll just add that I think we're getting better at managing our price investment considering all the other investments that we're making. So Brett and I and the management team are watching eCommerce growth rates, eCommerce profitability, store traffic counts and making decisions in a relatively fast cycle on how much price to invest and where to invest it, and we're monitoring what happens when we do that.

So we're just going to calibrate this thing as we go through the year. It's one of our big levers, and we're excited about the fact that the investments we've made in the past are driving traffic and starting to get this productivity moving, which is ultimately what we're after.

And one of the metrics that I get excited about and have been for some time now because the team's doing such a good job is inventory. For us to be down in comp store inventory again for the 11th consecutive quarter while shelf in-stock is going up is awesome and remarkable.

And the cash flow benefits and the other benefits are flowing through to the overall business. So on price, we're being thoughtful, we're being strategic. And we'll manage margins just like we do the other parts of the P&L, a quarter at a time, balancing short term and long-term.

### **Steve Schmitt**

Thanks, Chris. Rob, next question please?

### **Operator**

Your next question is from the line of Michael Lasser with UBS.

### **Michael Lasser**

Good morning. Thanks a lot of taking my question. Several years ago, Walmart was ahead of the curve, investing in stores, e-com, in price, and you really saw a gain in terms of market share and your outperformance relative to a lot of other retailers. Now it seems like some of those share gains may be slowing a bit.

So do you think you're seeing diminishing returns on your investments and you'll have to make even greater investments in order to outperform at the rate that you have been versus others?

**Doug McMillon**

No. Michael, this is Doug. That's not my perception, and the data doesn't support that. When you look at our share numbers, we feel really good about them, and not only the dollar share numbers but also units. I'm specifically thinking of the U.S. business in my comment. But the tonnage moving through our stores is increasing, and I don't feel a trend shift there.

**Steve Schmitt**

Thanks, Michael. Rob, next question please?

**Operator**

Next question is from the line of Scott Mushkin with Wolfe Research.

**Scott Mushkin**

Hey, guys. Thanks for taking my question. And before I ask it, I concur, our data does show you guys continue to gain a lot of market share, particularly in food. But that's kind of where I want to go with my question. If we fast-forward, guys, 5 years from now and we see a substantial, I think about 60% -- 67% of your sales are either pharmacy or food, and a good portion of that becomes click-and-collect or even maybe delivered to the home, how should we think about Walmart's profitability? And have you guys done a lot of thinking on that? Thanks.

**Doug McMillon**

Yes. Why don't we both -- I mean, you can go first, Brett.

**Brett Biggs**

Yes. I think as, Mike -- I mean, Scott, as Doug was saying, we do spend a lot of time as a management team thinking ahead, obviously, next quarter, next year, 3 years out, 5 years out and how we manage all the pieces of our

portfolio, and that includes International portfolio, Sam's Club, eCommerce, Walmart, and thinking about how we will manage as this business changes.

We know it changes. The customer is changing, and we're going to stay out in front of the customer. And the great thing about our business is we have so many different ways to do that, and we -- and the diversity of our portfolio gives us more options in which to do that.

And I think we sit back and we say we know where we want to be 5 years from now, 10 years from now, and there's a lot of different ways to get to that versus just one direct path. And so there's different things that we can do to manage that over time.

### **Doug McMillon**

I think the only thing I would add is that we're learning kind of the activity-based cost aspects of different paths. And I think, over time, if we could, and I think smart cart causes us to believe we might be able to, we'd like to bring the customers into this conversation and help them understand through our pricing and our communication that if you want to buy a single can of corn for under \$1, there's not going to be a better, more efficient path to you than a supercenter visit.

As the shape of a basket changes, food and non-food, and it goes up, and remember, Jet had a much higher units per order and still has a much higher units per order than the Walmart brand does, you can start to change the economics of eCommerce to be profitable with a unit per order that looks more like 7 than 2 and a blended basket margin that helps you to have basket economics rather than eaches.

So part of what we're trying to build with eCommerce, and I think you can see it, frankly, in the fourth quarter choices that we made around pricing on eaches, is that we're really focused on building a basket business because that's a big key to profitability.

### **Steve Schmitt**

Thanks, Scott. Rob, Next question please.

### **Operator**

Your next question is from Matt Fassler with Goldman Sachs.

### **Matt Fassler**

Thanks a lot. Good morning. I think I have a different way of asking the eCommerce and profitability question. Understanding that this is a year in

which you're probably making some investments that you may not have made because of tax reform, is there anything that you learned since you spoke with us back in October that suggests it would be more expensive due to market conditions to get to 40% annual eCommerce growth than you had previously thought?

**Doug McMillon**

No, I don't think so. Matt, my head, when you asked the question, started dividing it into food and non-food. There's nothing new on food. I think if you go back and listen to or watch our October analyst presentation where we walked through the strategy for food, all of that, even more convicted, still holds.

On the non-food side, we're building a business. It's -- non-food eCommerce is -- has not been our historic competency over the last few decades and the history of the company, and so we're learning something new.

We're trying to build an assortment that enables a margin ultimately, and that's got components to it like attracting brands, being able to execute from a fulfillment point of view during a busy season.

We've got some exciting things coming out with site redesign and other things this spring, I think, that will help us make more progress in that area. So I don't think it's that we've learned something new. I think it's a question of pace. And are the operational improvements and merchandising improvements happening? And are you investing marketing to kind of coincide with those improvements.

**Steve Schmitt**

Thanks, Matt. Rob, next question please.

**Operator**

The next question comes from the line of Kate McShane with Citi.

**Kate McShane**

Hi. Thank you for taking my question. Just to drill down a little bit more on some of the questions that have been asked. I think apparel has been highlighted by several media outlets over the weekend.

Can you walk us through what the overall apparel strategy is in store and online and how you're balancing national brands with private label?

**Doug McMillon**

Sure. I'm excited about -- later this week, I'm headed down to Houston because we've got all of our store managers there and these new apparel brands that have been mentioned in the media are on the sales floor, and I hear they look great. We're focused on improving quality; still managing good, better and best; protecting opening price points, which we do such a great job of; reducing our SKU counts in apparel to improve our presentation.

And we have some new fixturing in some stores that we're expanding on this year so that everything fits together, the quality of the product, the value of the product, the brand presentation of it, the ability to present it well because you have fewer SKUs and then a presentation in terms of fixturing that enables that to look fresh and new.

We've got a big apparel business. It has been growing, but we have even more opportunity to grow it in store. And then online, there are numerous opportunities for us to build private brands, leverage the DNVBs of the world like Bonobos and ModCloth and maybe more in the future and attract other brands to both Walmart and Jet that will help us drive our apparel business and manage the mix. So apparel is a pretty big focus at the moment.

### **Steve Schmitt**

Thanks, Kate. Next question please.

### **Operator**

Next question is from the line of Dan Binder with Jeffries.

### **Dan Binder**

Hi, thanks. You've talked about accelerating certain investments, so I'm just curious if you could be a little bit more specific on what those are and whether or not there'll be any lumpiness by quarter that we should consider. I know you're giving annual guidance, but just want to make sure we consider the quarters as well.

### **Brett Biggs**

Yes. Dan, this is Brett. The investments that we're going to make are going to continue to change how we work as a company, help us continue to stay ahead of the customer, and those are going to be in the areas of technology. They're going to be in the areas of supply chain, pricing.

And you can imagine, for competitive reasons, we're not going to get into a lot of things that we plan to do, and we'll be talking about those as we go

throughout the year. We mentioned we think EPS growth will be pretty consistent throughout the year quarter by quarter.

There could be a quarter or two where we make an investment that's different than the other quarters. And if that's the case, we would talk about that when we release earnings. But right now, I don't anticipate major changes quarter-to-quarter.

**Steve Schmitt**

Thanks, Dan. Rob, next question please.

**Operator**

Next question comes from the line of Paul Trussell with Deutsche Bank.

**Paul Trussell**

Good morning and also thank you for doing this call. Just wanted to circle back on margins. The guidance for 4.3% to 4.4% for the year, obviously, a lot of moving parts and some acceleration in investments. So just want to confirm that your thought process is that there is an ability to find further leverage over time and expand from those levels as we look forward.

And also, more specifically, for the current quarter, if you can just touch a little bit more detail regarding the transportation cost impact that you saw and what your expectations are on that particular line item going forward.

**Brett Biggs**

Sure. Paul, appreciate it. I'll start with the operating income question. We're only giving guidance for this year coming forward. We did leverage expenses. Excluding discrete items for the year, leverage got better as we went throughout the year. So I am optimistic about the expense leverage that we're seeing in the business, particularly in International and Walmart U.S. stores, and I expect that we'll continue to see that progress.

So that gives us -- we've always talked about that being better with expenses gives us more flexibility and more ways in which to hit the P&L that we would like to and do what we want to do for our customers. So that's the only guidance we're going to give, is we'll be this, this year on operating income.

On transportation costs, those vary from quarter-to-quarter. As you know, gas prices -- fuel prices have gone up a little bit. In this last quarter, I think we're maybe \$0.30 versus last year roughly. So that has a bearing on what

we do year-to-year, quarter-to-quarter, but that was the main mention of that in the fourth quarter.

**Steve Schmitt**

Thanks, Paul. The next question please.

**Operator**

Our next question is from the line of Ben Bienvenu with Stephens.

**Ben Bienvenu**

Hi, thanks. Good morning. Thanks for taking my question. Could you talk about the working capital opportunities that you see for FY '19? Obviously, you've done a great job in inventory in the U.S. Can working capital continue to be a source of cash for Walmart? Or have you harvested all the opportunity that you can?

**Brett Biggs**

Thanks, Ben. Yes, there's always more opportunity. If Greg Foran were sitting here, he would talk about, as he goes into store by store, he still sees opportunity for us to be better, to be more efficient. Some of the technology that we've talked about and investments will continue to lead to easier ways for our associates to move goods, stock goods.

So all of that helps, and all of that matters. I don't think there's ever an end to what we can do on working capital. The last 2 years have been -- to be fair, have been pretty impressive, the last couple of years, particularly on payables and the inventory side.

So I think there's more room to go. I won't quantify what I think that could be, but I do believe working capital can continue to be a source of cash for Walmart going forward.

**Steve Schmitt**

Thanks, Ben. Rob, next question please.

**Operator**

Your next question comes from the line of Peter Benedict with Robert Baird.

**Peter Benedict**

Hey, guys. You've shown signs of being willing to rationalize the asset base here more recently, but, obviously, continue to invest in eCommerce. So



how do you see the ROIC profile evolving over the next few years? Just curious how important stabilizing that metric is to you as you guys think about your broader priorities? Thanks.

**Brett Biggs**

Yes, great question. And Peter, as you know, we've talked a lot about ROI. It's important to us. Returns are important, along with a number of other metrics that we've mentioned this morning.

If you pull out the discrete items, ROI would have been in a much better place in this last year, and we've seen improvements in our asset base and rationalizing that operating income being where it is. Returns short term, long term are really important for the company.

We are going to make sure that we win long term. And as we've said before, there may be times year-to-year where that has an impact on ROI that is different than we would want on a long-term basis.

But we will make those decisions when we need to do that. But returns are very important for us, and we talk about it a lot as a management team, as you would imagine.

**Steve Schmitt**

Thanks, Peter. Rob, next question please.

**Operator**

Next question is from the line of Bob Drbul with Guggenheim Securities.

**Bob Drbul**

Hi, guys. Good morning. Two quick questions. The first one is, did you give a number on inflation and sort of the trends that you're seeing on -- especially on the food inflation?

And then the other one is, on fulfillment centers, you're converting, I think it's, 10 of the Sam's Clubs into fulfillment centers. Can you just give us an idea of where you think you are with your ability on the fulfillment center proposition in the business?

**Brett Biggs**

Yes. Bob, on inflation, we didn't see a meaningful impact in the quarter. And going forward, probably a modest impact -- slight impact next year, but nothing meaningful really next year.

**Doug McMillon**

And on the fulfillment side, I would say we're in pretty good shape in terms of square footage and where it's placed. We had these 6 fulfillment centers with Walmart, the 3 we picked up from Jet. And Marc and the team are learning how to mirror inventory in certain places to improve customer service levels and to lower cost. So that's underway, but the physical plant is in pretty good shape generally. It's going to be fun to watch what happens with the Sam's Club efforts here.

If we're going to take Memphis as a place to learn, we basically use the same facility, same steel that we use when members shop in the club and pick from those. That's going to help us with speed. It's going to help us reduce transportation costs. And once we have the wrinkles ironed out there, we'll use more facilities over time. Generally speaking, I think we're in pretty good shape. Over the years, looking ahead, as we grow the business, we may open a fulfillment center here and there, but that's where we stand today.

**Steve Schmitt**

Thanks, Bob. Rob, next question please.

**Operator**

The next question is from the line of Greg Melich with MoffettNathanson.

**Greg Melich**

Hi, thanks. I wanted to tie it back a little into the reinvestment of the tax benefits. I think you guys have invested about \$750 million in labor that was announced about a month ago. When you think about the magnitude that would go back into price, should we think about it being similar to what was in SG&A?

Or how would we even frame that? And you can answer to this year or even over the next couple of years. Thanks.

**Brett Biggs**

Yes, Greg. As I said earlier, we're not going to get into a lot of detail about how we're going to invest. The wage amount you mentioned, about \$400 million of that was the onetime bonus. The other part would be going forward into next year with the increase in the start rate.

And I'll say what I said before, which is we're going to be thoughtful about these investments. And we have a lot of levers that we can use to satisfy that customer, and we're going to be thoughtful about which levers we pull.

**Steve Schmitt**

Thanks, Greg. Rob, next question please.

**Operator**

Next question is from the line of Edward Kelly with Wells Fargo.

**Edward Kelly**

Yeah, hi. Good morning. I would just like to talk about - or ask about investment in grocery at this point, just in terms of price investment, how you're thinking about the returns that you're getting on that investment, how you balance that against investing in the digital experience for the customer. I would think that, at this point, you're getting to an area, given your price perception and competitive marketplace, that maybe digital is the better return.

And then you did mention grocery delivery. Could you just give us an update on where you stand there at this point?

**Doug McMillon**

Sure. As you think about price investments in store, think about grocery, consumables and the fact that, across the store, there are some items, windshield washer fluid in the automotive department, tennis balls in sporting goods, that are high-turn, price-sensitive items to a degree. And when we think about the price investments in the store, we're not singularly focused on dry grocery. We're thinking about this in a broad way.

The supercenter assortment is a big advantage, and we want to deliver low prices across the store, which also helps us drive traffic to the store and manage margins across the entire store. So evaluate the price investment through that lens rather than just grocery. And the returns we're seeing there are attractive. You can see it in the store traffic.

And we're going to continue our strategy as it relates to those. We're not cutting short the eCommerce investments. I think part of what we're doing now is just letting the business mature and learning how to become stronger operationally in eCommerce.

There may be a point this year and looking ahead where we want to be even more aggressive on eCommerce marketing, if we feel like those operational

improvements are on the right path. We kind of watch that very continuously basically.

As it relates to grocery delivery, we've had this small pilot going on with our own associates, and we'll continue to play around with that and learn what works there. But the expansion will happen through a variety of platforms. We'll use, depending on the spot in the country, different providers to get the product to the customer, and we'll be keeping an eye on NPS scores in particular.

Our Online Grocery business has a really high Net Promoter Score, and we want to, as we start to grow delivery capabilities, ensure that the customer experience is as good through delivery as it is for pickup. So we've got some things to learn there, and it'll happen at a pace based on the customer experience.

**Steve Schmitt**

Thanks, Ed. Rob, we have time for one question.

**Operator**

That final question comes from Chuck Grom with Gordon Haskett.

**Chuck Grom**

Hi, thanks. Good morning. Doug, from a capital allocation standpoint, could you discuss a little bit about closing the 63 Sam's stores earlier? And then should we expect to see continued closings both in the U.S. and International? And then for Brett, on the digital side, could you shed some light on the growth between 1P and 3P for the e-com business? Thanks.

**Doug McMillon**

Sure. I'll take capital allocation first. If you go back a couple of years, you'll remember that we closed quite a few stores around the world, including the 100-some-odd Express stores in Walmart U.S., the smaller stores that we have been testing as a pilot -- as a format. We discontinued those and closed those.

At that moment in time, we had been through all of the 11,600-plus units around the world, sitting through real estate, meeting, Brett, country by country and making choices about the portfolio. So we did a lot of that cleanup then. We didn't do Sam's Club at the time.

We were still working through a number of things, pacing things out, trying to put them in the right sequence. So the way I was thinking of it is let's

make sure that the U.S. store business is strong. What do we need to make that work? That's where we made wage investments, price investments and cleaned up the portfolio. We've been focused on -- focusing on building an eCommerce business. That's still underway obviously. And then now we've turned our attention to Sam's Club.

We've got a strategy we believe in, a leadership team we're excited about, and we're investing in that business to drive comps up there. So it's just been a sequencing, and the bottom line is we've been through the portfolio. I can't tell you there will never be more closings. A store here and there, I think, makes sense, but we've been through the majority of that big work for now anyway.

### **Brett Biggs**

Chuck, on your question of 1P and 3P, obviously, first part, they're part - they're both important to us. We want to satisfy that customer need. Sometimes, it's better done through first party; sometimes, it's better done through third party. As you know, we have about 75 million SKUs now on our Marketplace site.

And it's another one of those levers that we've talked about -- I was talking about earlier that we have in order to determine how we best fulfill that customer need in a way that makes sense for both top line and bottom line.

### **Steve Schmitt**

Well, thanks, guys. We certainly appreciate you joining our call today. And have a great day.