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# Wal-Mart Stores, Inc.—1998

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www.wal-mart.com  
stock symbol WMT

Headquartered in Bentonville, Arkansas, Wal-Mart (501-273-4000) saw its sales rise from \$104.8 billion in 1997 to \$117.9 billion in fiscal 1998. Net income rose from \$3.1 billion to \$3.6 billion during that period. For more than a decade, Wal-Mart has been growing by leaps and bounds, rolling over large competitors such as Kmart and thousands of small businesses. Financial statements are shown in Exhibits 1 and 2.

In 1995, Wal-Mart ended a five-year battle with local leaders of Bennington, Vermont, to open its first store in that state and thereby lay claim to having stores in all 50 states (see Exhibit 3). The Bennington store was Wal-Mart's 2,158th store. To get approval for this store, Wal-Mart abandoned its usual format of a 200,000-square-foot store near a major highway exit and instead located in a downtown building of just 50,000 square feet. Environmentalists in Vermont say the rural character of the state is endangered by "sprawl-mart development." Other chains such as Ames and Kmart had operated in Vermont for years, so some residents were mystified by the controversy. Wal-Mart had three stores in Vermont by the end of fiscal 1997.

Wal-Mart does not have a formal mission statement. When asked about Wal-Mart's lack of a mission, Public Relations Coordinator Kim Ellis replied, "We believe that our customers are most interested in other aspects of our business, and we are focused on meeting their basic consumer needs. If in fact we did have a formal mission statement, it would be something like this: 'to provide quality products at an everyday low price and with extended customer service . . . always.'"

## HISTORY

No word better applies to Wal-Mart than "growth." In 1945, Sam Walton opened his first Ben Franklin franchise in Newport, Arkansas. Based in rural Bentonville, Arkansas, Walton; his wife, Helen; and his brother, Bud, operated the nation's most successful Ben Franklin franchises. "We were a small chain," said Walton of his 16-store operation. "Things were running so smoothly we even had time for our families." What more could a man want? A great deal, as it turned out.

Sam and Bud Walton could see that the variety store was dying gradually because supermarkets and discounters were developing. Far from being secure, Walton knew that he was under siege. He decided to counterattack. He first tried to convince the top management of Ben Franklin to enter discounting. After their refusal, Sam Walton made a quick trip around the country in search of ideas. He then began opening his own discount stores in such small Arkansas towns as Bentonville and Rogers.

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**EXHIBIT 1: Consolidated Statements of Income**

<i>(amounts in millions except per share data)</i>	<i>Fiscal years ended January 31,</i>		
	<i>1998</i>	<i>1997</i>	<i>1996</i>
Revenues:			
Net sales	\$117,958	\$104,859	\$93,627
Other income—net	1,341	1,319	1,146
	<u>119,299</u>	<u>106,178</u>	<u>94,773</u>
Costs and Expenses:			
Cost of sales	93,438	83,510	74,505
Operating, selling and general and administrative expenses	19,358	16,946	15,021
Interest Costs:			
Debt	555	629	692
Capital leases	229	216	196
Income Before Income Taxes, Minority Interest and Equity in Unconsolidated Subsidiaries	5,719	4,877	4,359
Provision for Income Taxes			
Current	2,095	1,974	1,530
Deferred	20	(180)	76
	<u>2,115</u>	<u>1,794</u>	<u>1,606</u>
Income Before Minority Interest and Equity in Unconsolidated Subsidiaries	3,604	3,083	2,753
Minority Interest and Equity in Unconsolidated Subsidiaries	(78)	(27)	(13)
Net Income	3,526	3,056	2,740
Net Income Per Share	1.56	1.33	1.19

Source: www.freedgar.com

**EXHIBIT 2: Consolidated Balance Sheets**

<i>(amounts in millions)</i>	<i>January 31,</i>	
	<i>1998</i>	<i>1997</i>
Assets		
Current Assets:		
Cash and cash equivalents	\$ 1,447	\$ 883
Receivables	976	845
Inventories		
At replacement cost	16,845	16,193
Less LIFO reserve	348	296
Inventories at LIFO cost	16,497	15,897
Prepaid expenses and other	432	368
<i>Total Current Assets</i>	<u>19,352</u>	<u>17,993</u>

continued

EXHIBIT 2: *continued*

<i>(amounts in millions)</i>	<i>January 31,</i>	
	<i>1998</i>	<i>1997</i>
Property, Plant and Equipment, at Cost:		
Land	\$ 4,691	\$ 3,689
Building and improvements	14,646	12,724
Fixtures and equipment	7,636	6,390
Transportation equipment	403	379
	<u>27,376</u>	<u>23,182</u>
Less accumulated depreciation	5,907	4,849
Net property, plant and equipment	21,469	18,333
Property Under Capital Lease:		
Property under capital lease	3,040	2,782
Less accumulated amortization	903	791
Net property under capital leases	2,137	1,991
Other Assets and Deferred Charges	2,426	1,287
<i>Total Assets</i>	<i>45,384</i>	<i>39,604</i>
<i>Liabilities and Shareholders' Equity</i>		
Current Liabilities:		
Accounts payable	9,126	7,628
Accrued liabilities	3,628	2,413
Accrued income taxes	565	298
Long-term debt due within one year	1,039	523
Obligations under capital leases due within one year	102	95
<i>Total Current Liabilities</i>	<i>14,460</i>	<i>10,957</i>
Long-Term Debt	7,191	7,709
Long-Term Obligations Under Capital Leases	2,483	2,307
Deferred Income Taxes and Other	809	463
Minority Interest	1,938	1,025
Shareholders' Equity		
Preferred stock (\$.10 par value; 100 shares authorized, none issued)		
Common stock (\$.10 par value; 5,500 shares authorized, 2,241 and 2,285 issued and outstanding in 1998 and 1997, respectively)	224	228
Capital in excess of par value	585	547
Retained earnings	18,167	16,768
Foreign currency translation adjustment	(473)	(400)
<i>Total Shareholders' Equity</i>	<i>18,503</i>	<i>17,143</i>
<i>Total Liabilities and Shareholders' Equity</i>	<i>45,384</i>	<i>39,604</i>

Source: www.freeedgar.com

## EXHIBIT 3: Wal-Mart Fiscal 1998 End of Year Store Counts

	<i>Discount Stores</i>	<i>Supercenters</i>	<i>SAM'S Clubs</i>
Alabama	50	27	8
Alaska	3	0	3
Arizona	34	0	7
Arkansas	50	27	4
California	100	0	24
Colorado	31	5	10
Connecticut	14	0	3
Delaware	2	1	1
Florida	102	33	31
Georgia	62	25	16
Hawaii	5	0	1
Idaho	9	0	1
Illinois	95	11	24
Indiana	60	15	14
Iowa	43	2	7
Kansas	40	8	5
Kentucky	45	23	5
Louisiana	56	19	9
Maine	19	0	3
Maryland	22	1	10
Massachusetts	27	0	3
Michigan	45	0	21
Minnesota	34	0	9
Mississippi	42	14	4
Missouri	79	30	12
Montana	9	0	1
Nebraska	13	5	3
Nevada	13	0	2
New Hampshire	17	0	4
New Jersey	16	0	6
New Mexico	16	3	3
New York	51	5	18
North Carolina	78	8	14
North Dakota	8	0	2
Ohio	77	4	23
Oklahoma	57	21	6
Oregon	23	0	0
Pennsylvania	49	12	18
Rhode Island	6	0	1
South Carolina	41	12	9
South Dakota	8	0	2
Tennessee	57	30	11
Texas	169	72	52
Utah	14	0	5
Vermont	3	0	0
Virginia	31	21	10
Washington	20	0	2
West Virginia	12	6	3
Wisconsin	55	1	11
Wyoming	9	0	2
<i>U.S. Total</i>	<i>1,921</i>	<i>441</i>	<i>443</i>

*continued*

EXHIBIT 3: *continued*

	<i>Discount Stores</i>	<i>Supercenters</i>	<i>SAM'S Clubs</i>
Alberta	16	0	0
British Columbia	12	0	0
Manitoba	9	0	0
New Brunswick	4	0	0
Newfoundland	7	0	0
Nova Scotia	7	0	0
NW Territories	1	0	0
Ontario	52	0	0
Quebec	28	0	0
Saskatchewan	8	0	0
<i>Canada Total</i>	144	0	0
Argentina	0	6	3
Brazil	0	5	3
Mexico	347 <sup>a</sup>	27	28
Puerto Rico	9	0	5
China	0	2	1
Germany	0	21	0
<i>International Total</i>	500	61	40
<i>Grand Total</i>	2,421	502	483

Source: [www.freeedgar.com](http://www.freeedgar.com)

<sup>a</sup>includes 3 Superamas, 25 Bodegas, 4 Aurreras, 67 Vips, and 7 Suburbias.

The company opened its first discount department store, Wal-Mart, in November 1962. The early stores had bare tile floors and pipe racks. Wal-Mart did not begin to revamp its image significantly until the mid-1970s, and growth in the early years was slow. However, once the company went public in 1970, sales began to increase rapidly. Wal-Mart's stock doubled in value in 1997 alone.

Such retailers as Target, Venture, and Kmart provided the examples that Wal-Mart sought to emulate in its growth. The old Wal-Mart store colors, dark blue and white (too harsh), were dumped in favor of a three-tone combination of light beige, soft blue, and burnt orange. Carpeting, which long had been discarded on apparel sales floors, was put back. New racks were put into use that displayed the entire garment instead of only an edge.

In 1987, Wal-Mart implemented two new concepts: (1) hypermarkets, 200,000-square-foot stores that sell everything, including food, and (2) supercenters, scaled-down supermarkets. Also in 1987, Walton named David Glass as the new chief executive officer while he remained chair of the board. Glass is president and CEO today (see Exhibit 4).

In 1990, Wal-Mart completed the acquisition of 14 centers of McLane Company, a national distribution system in 11 states providing over 12,500 types of grocery and nongrocery products. Also in 1990, Wal-Mart sold its 14 Dot Discount Drug Stores. SAM'S Clubs that year integrated the 28 wholesale clubs of The Whole Club, Inc., c Indianapolis, Indiana, into its operations.



Wal-Mart unveiled in mid-1993 its first environmental demonstration store, a 121,294-square-foot facility in Lawrence, Kansas. This store is designed so that a second floor could be added to allow conversion to apartments if Wal-Mart vacates. The store is exceptionally energy-efficient but costs 20 percent more than the average Wal-Mart, which costs about \$2.4 million or \$20 a square foot. The environmental store features on-site recycling, native plants that make up the landscaping, and solar-powered lights. Planning for this store began in 1990 when Hillary Rodham Clinton served on Wal-Mart's board of directors. Wal-Mart constructed a second environmental demonstration store in Moore, Oklahoma. Companywide, Wal-Mart recycles over 700,000 tons of cardboard, paper, and plastic each year.

Exhibits 5 and 6 provide selected financial information for Wal-Mart in fiscal 1998.

**EXHIBIT 5: Wal-Mart Divisions' Financial Data (in millions of dollars)--**

<i>(Fiscal year ended January 31, 1998)</i>	<i>Wal-Mart Stores</i>	<i>SAM'S Clubs</i>	<i>International</i>	<i>Other</i>	<i>Consolidated</i>
Revenues from external customers	\$83,820	\$20,668	\$7,517	\$ 5,953	\$117,958
Intercompany real estate charge (income)	1,375	349		(1,724)	
Depreciation and amortization	674	104	118	738	1,634
Operating income	5,833	616	262	(208)	6,503
Interest expense					784
Income before income taxes and minority interest					5,719
Total assets	\$22,002	\$ 3,864	\$7,390	\$12,128	\$ 45,384

Source: www.freeedgar.com

**EXHIBIT 6: Wal-Mart Sales Data for Fiscal Year Ended January 31, 1998**

<i>Category</i>	<i>Percentage of Sales</i>
Hard goods	23
Soft goods/domestics	21
Grocery, candy, and tobacco	14
Pharmaceuticals	9
Records and electronics	9
Sporting goods and toys	8
Health and beauty aids	7
Stationery	5
Shoes	2
Jewelry	2

Source: www.freeedgar.com

Sam Walton died in 1992. Bud Walton died in 1995. Wal-Mart's 1995 Annual Report was dedicated to Bud. Sam Walton once said about Bud: "Of course, my number-one retail partner has been my brother, Bud. Bud's wise counsel and guidance kept us from many a mistake. Often, Bud would advise taking a different direction or maybe changing the timing. I soon learned to listen to him because he has exceptional judgment and a great deal of common sense."

## DIVISIONS

### Wal-Mart Stores

Most Wal-Mart stores are located in towns of 5,000 to 25,000. On occasion, smaller stores are built in communities of less than 5,000. As indicated in Exhibit 7, Wal-Mart opened 37 Wal-Mart stores, 97 Supercenters, and 8 SAM'S Clubs in fiscal 1998. Most of Wal-Mart's 1998 \$117 billion in sales came from Wal-Mart stores and Supercenters. International sales grew to approximately 6.3 percent of the total sales in fiscal 1998, up from 4.8 percent in fiscal 1997. SAM'S Club percentage of total sales decreased from 18.9 percent in fiscal 1997 to 17.5 percent in fiscal 1998.

Wal-Mart grouped its smaller discount stores, such as the one in Bennington, Vermont, into a new Hometown USA program. This allows the company to give special attention to customers in smaller markets in rural America. Hometown USA consists of the stores that are under 50,000 square feet and under one regional manager. The idea is to enable these stores to develop locally and with a different mix from the large prototypes. Although these stores represent Wal-Mart's heritage, they had become lost in the shuffle as the company opened 120,000- to 150,000-square-foot stores.

Wal-Mart stores generally have 36 departments and offer a wide variety of merchandise, including apparel for women, girls, men, boys, and infants. Each store also carries curtains, fabrics and notions, shoes, housewares, hardware, electronics, home supplies, sporting goods, toys, cameras and supplies, health and beauty aids, pharmaceuticals, and jewelry. Nationally advertised merchandise accounts for a majority of sales in the stores. Wal-Mart has begun marketing limited lines of merchandise under

**EXHIBIT 7: Wal-Mart's Store Count Data**

Fiscal Year Ended Jan. 31,	Wal-Mart Discount Stores			Wal-Mart Supercenters		SAM'S Clubs			
	Opened	Closed	Conversions	Total	Opened	Total	Opened	Closed	Total
Balance Forward	—	—	—	1,714	—	10	—	—	208
1993	159	1	24	1,848	24	34	48	0	256
1994	141	2	37	1,950	38	72	162	1	417
1995	109	5	69	1,985	75	147	21	12	426
1996	92	2	80	1,995	92	239	9	2	433
1997	59	2	92	1,960	105	344	9	6	436
1998	37	1	75	1,921	97	441	8	1	443

Source: [www.freedgar.com](http://www.freedgar.com)

the brand name SAM'S American Choice. The merchandise is selected carefully to ensure quality and must be made in the United States. Wal-Mart is developing new apparel lines such as the Kathie Lee career sportswear and dress collection, Basic Equipment sportswear, and McKids children's clothing.

Except for extended hours during certain holiday seasons, most Wal-Mart stores are open from 9:00 A.M. to 9:00 P.M. six days a week, and from 12:30 P.M. to 5:30 P.M. on Sundays, with the remainder of the stores closed on Sundays. Some Wal-Mart stores and most of the Supercenter stores are open 24 hours each day. Wal-Mart tries to meet or undersell local competition but maintains uniform prices, except when lower prices are necessary to meet local competition. Wal-Mart stores maintain a "satisfaction guaranteed" program to promote customer goodwill and acceptance.

### **McLane's**

McLane's is the nation's largest distributor of food and merchandise to convenience stores. McLane's offers a wide variety of grocery and nongrocery products, including perishable and nonperishable items. The nongrocery products consist primarily of tobacco products, hard goods, health and beauty aids, toys, and stationery. McLane's is a wholesale distributor which sells merchandise to a variety of retailers, including the Wal-Mart stores, SAM'S Clubs, and Supercenters.

### **SAM'S Clubs**

SAM'S Clubs are membership-only, cash-and-carry operations. A financial service credit card program (Discover Card) is available in all clubs. Qualified members include businesses and those individuals who are members of certain qualifying organizations, such as government and state employees and credit union members. Both business and individual members have an annual membership fee of \$25 for the primary membership card.

SAM'S offers bulk displays of name-brand hard good merchandise, some soft goods, and institution-size grocery items. Each SAM'S also carries jewelry, sporting goods, toys, tires, stationery, and books. SAM'S now has 131 clubs with fresh-food departments such as bakery, meat, and produce.

SAM'S is a \$20 billion business that is starting to grow again. The clubs were never designed to sell merchandise categories, but rather items, and because the number of items is limited to about 2,000 for the wholesale part of the business, which is 60 percent to 65 percent of sales, and to 1,000 to 1,500 for personal and individual use, it is very important for the items to be appropriate for the location. Also, the items have to come and go seasonally, so continuity by category is not appropriate. Thus, there is a problem for buyers who have to be item merchants and compete for space in the clubs.

Operating hours vary among SAM'S, but generally are Monday through Friday from 10:00 A.M. to 8:30 P.M. Most SAM'S are open on the weekend from 9:30 A.M. to 7:00 P.M. on Saturday and from 12:00 noon to 6:00 P.M. on Sunday. SAM'S attempts to maximize sales volume and inventory turnover while minimizing expenses.

During fiscal 1998, Wal-Mart opened 8 new SAM'S Clubs. This division of Wal-Mart lags behind other divisions in financial performance, but the company feels the warehouse club business has promise.

## Supercenters

Wal-Mart's Supercenters combine groceries with general merchandise, giving customers one-stop shopping. Wal-Mart opened 97 Supercenters during fiscal 1998, bringing the total of Supercenters to 441 in the United States as shown in Exhibit 7.

The number of Supercenters grew from just five in 1991 to six in 1992, 30 in 1993, 68 in 1994, 143 in 1995, and 235 in 1996.

Supercenters constitute the company's fastest-growing division, and management is extremely pleased with them. Currently, the limitation is distribution, and Wal-Mart is working hard to expand its captive food distribution capabilities. Most of the Supercenters are replacements of Wal-Mart stores, so they had a jumpstart on the general merchandise side of the store, while food has tended to build a little bit more slowly. However, the company has gained market share faster than planned. Wal-Mart likes to locate Supercenters near the strongest food retailers so those facilities will "either get better or be run out of town."

The Wal-Mart Supercenter is the most important retail concept on the landscape at this time. As with the discount stores, their real competitive impact does not come the year they open, but in the third year, because they have a maturation curve that's more like a Wal-Mart store than a food store. Also, the one-stop convenience aspect of the stores has such broad appeal that it is drawing a larger customer audience on a regular basis. Supercenters are continuing to get better in many categories and are attracting a higher-income audience, in addition to their traditional customers. Supercenters provide mart carts and are on one floor, so the stores are handicapped-accessible. The company's broad assortments and everyday low prices are very compelling; extensive advertising is not needed. This represents an enormous saving over the competition. Furthermore, as Supercenters move into food distribution, they gain a major cost advantage over Super Kmart and Super Target.

## International

In 1994, Wal-Mart acquired 122 Canadian Woolco stores. Wal-Mart revamped these stores in less than a year. Wal-Mart Canada already has become that nation's number-one discount chain, and is on the verge of becoming Canada's largest retailer of any sort. As indicated in Exhibit 3, the company today has 144 Wal-Mart stores in Canada, 347 in Mexico, and nine in Puerto Rico. Note that Wal-Mart also operated 61 Supercenters and 40 SAM'S Clubs outside the United States as fiscal 1998 ended. The world's largest Wal-Mart is in Mexico City.

Wal-Mart considers its Hong Kong stores as training centers for the company's expansion into China. Wal-Mart Chair Rob Walton, Sam's oldest son, is leading the company's efforts to open stores in China.

Wal-Mart recently announced plans to purchase a majority interest in Cifra SA, its joint venture partner in Mexico. This move marks Wal-Mart's first direct investment in any of its foreign partners and reflects the chain's increasing efforts to expand its international business.

With more than 50,000 associates and over 300 locations outside the United States, Wal-Mart already is serving some 5 million customers every week.

According to Bob L. Martin, president of the International Division, "We are a global brand name. To customers everywhere it means low cost, best value, greatest selection of quality merchandise, and the highest standards of customer service. But the fact

that International has grown to \$5 billion in sales in less than five years gives us an idea of how great the potential is."

Community involvement, responding to local needs, merchandise preferences, and buying locally are all hallmarks of the international Wal-Marts, just as they are in the United States.

### Distribution Centers

Wal-Mart has 30 distribution centers nationwide, including six centers in Arkansas; four in Texas; and two each in California, Indiana, Pennsylvania, and South Carolina. Wal-Mart's distribution operations are highly automated. A typical Wal-Mart Discount Store has more than 70,000 standard items in stock. Supercenters carry more than 20,000 additional grocery items, a lot of them perishable, so they have to be ordered frequently. Associates use hand-held computers, linked by a radio-frequency network to in-store terminals, to scan items electronically and check on their availability in other area stores. To place orders, each store wires merchandise requests to the warehouses, which in turn either ship immediately or reorder. Wal-Mart computers are linked directly with over 200 vendors, so deliveries are faster. Wal-Mart has one of the world's largest private satellite communication systems to control distribution. Wal-Mart has installed point-of-sale bar-code scanning in all of its stores.

Wal-Mart owns a fleet of truck-tractors that can deliver goods to any store in 38 to 48 hours from the time the order is placed. After trucks drop off merchandise, they frequently pick up merchandise from manufacturers on the way back to the distribution center. This back-haul rate averages over 60 percent and is yet another way Wal-Mart cuts costs.

With an annual technology and communication budget of \$500 million and an information systems staff of 1,200, Wal-Mart leads the industry in information technology. This means Wal-Mart is dedicated to providing its associates with the technological tools to work smarter every day. "With this technology, we're getting better, quicker, and more accurate information to manage and control every aspect of our business," said Randy Mott, senior vice-president and chief information officer.

## OPERATIONS

Wal-Mart's expense structure, measured as a percentage of sales, continues to be among the lowest in the industry. Although Walton watched expenses, he rewarded sales managers handsomely. Sales figures are available to every employee at Wal-Mart. Monthly figures for each department are ranked and made available throughout the organization. Employees who do better than average get rewarded with raises, bonuses, and a pat on the back. Poor performers only rarely are fired, although demotions are possible.

All employees (called "associates") have a stake in the financial performance of the company. Store managers earn as much as \$100,000 to \$150,000 per year. Even part-time clerks qualify for profit-sharing and stock-purchase plans. Millionaires among Wal-Mart's middle managers are not uncommon. Executives frequently solicit ideas for improving the organization from employees and often put them into use.

With Wal-Mart stock selling at 20 to 30 times earnings—an almost incredible price—Sam Walton presided over a sizable fortune before his death. Wal-Mart stock is still 39 percent held by the Walton family. Family holdings are worth nearly \$8 billion.

Continuing a Walton tradition, Wal-Mart invites over 100 analysts and institutional investors to the fieldhouse at the University of Arkansas for its annual meeting in mid-June. During the day-and-a-half session, investors can meet top executives as well as Wal-Mart district managers, buyers, and 200,000 hourly salespeople. Investors see a give-and-take meeting between buyers and district managers.

### **Employee Benefits**

Wal-Mart management takes pride in the ongoing development of its people. Training is seen as critical to outstanding performance, and new programs are implemented often in all areas of the company. The combination of grass-roots meetings, the open-door policy, videos, printed material, classroom and home study, year-end management meetings, and on-the-job training has enabled employees to prepare themselves for advancement and added responsibilities.

Wal-Mart managers stay current with new developments and needed changes. Executives spend one week per year in hourly jobs in various stores. Sam Walton himself once traveled at least 3 days per week, visiting competitors' stores, and attending the opening of new stores (leading the Wal-Mart cheer, "Give me a W, give me a A . . .").

Wal-Mart encourages employee stock purchases; about 8 percent of Wal-Mart stock is owned by employees. Under the Stock Purchase Plan, stock may be bought by two different methods. First, an amount is deducted from each employee's check with a maximum of \$62.50 per check. An additional 15 percent of the amount deducted is contributed by Wal-Mart (up to \$1,800 of annual stock purchases). Second, a lump-sum purchase is allowed in April up to \$1,500, with an additional 15 percent added by the company. Wal-Mart also offers an associate stock-ownership plan, and approximately 4,000 management associates have stock options.

Wal-Mart has a corporate profit-sharing plan. The purposes of the profit-sharing plan are to furnish an incentive for increased efficiency, to provide progressive recognition of service, and to encourage careers with the company for Wal-Mart associates. This is a trustee-administered plan, which means the company's contributions are made only out of net profits and are held by a trustee. The company from time to time contributes 10 percent of net profits to the trust.

Company contributions can be withdrawn only on termination. If employment with the company is terminated because of retirement, death, or permanent disability, the company contribution is fully vested (meaning the entire amount is nonforfeitable). If termination of employment occurs for any other reason, the amount that is nonforfeitable depends on the number of years of service with the company. After completion of the third year of service with the company, 20 percent of each participant's account is nonforfeitable for each subsequent year of service. After seven years of service, a participant's account is 100 percent vested.

### **Predatory Pricing**

Three independent pharmacies in Conway, Arkansas, filed a suit claiming Wal-Mart deliberately was pricing products below cost to kill competition. Wal-Mart argued that it priced products below cost not to harm competitors but to meet or beat rivals' prices. Chancery Court Judge David L. Reynolds on October 11, 1996, found Wal-Mart guilty of predatory pricing and ordered the company to pay the pharmacies \$286,407 in damages. The judge also forbade Wal-Mart from selling products below cost in Conway in

the future. Competitors who had been stung by Wal-Mart's pricing policies watched the case closely.

The ruling in Arkansas marked the first time Wal-Mart failed to settle a predatory pricing case out of court. If upheld, the decision could prompt similar lawsuits elsewhere.

Wal-Mart intends to appeal the ruling to the Arkansas Supreme Court. "Wal-Mart is extremely disappointed," said Robert K. Rhoads, the retailer's attorney. "If this decision is allowed to stand, the result will be higher prices—not just for Wal-Mart customers but customers of every retail store, large and small, in Arkansas."

### Diversity Among Employees

Sam Walton was admittedly old-fashioned in many respects. Wal-Mart store policies reflect many of his values. For example, store policies forbid employees from dating other employees without prior approval of the executive committee. Also, women in management positions are rare. Annual manager meetings include sessions for wives to speak out on the problems of living with a Wal-Mart manager. No women are in the ranks of Wal-Mart's top management. Walton also resisted placing women on the board of directors. Only 12 women have made it to the ranks of buyers (they are 12 percent of all buyers). Wal-Mart is an EEOC/AA employer but has managed to get away with apparently discriminatory policies.

Wal-Mart has instituted several initiatives to increase the recruitment and promotion of women and minorities including:

- a mentoring program encompassing more than 750 women and minority managers,
- a women's leadership group, in partnership with Herman Miller and ServiceMaster, to develop opportunities for high-potential female managers, and
- store internships during the summer for college students between their junior and senior years, with 70 percent being women or minorities.

### Philanthropy

Education is a primary beneficiary of Wal-Mart charitable giving. Examples include:

- Each store awards a \$1,000 college scholarship to a qualifying high school senior. More than \$11 million in scholarships have been awarded since the program's inception.
- A major commitment to the United Negro College Fund. In 1997, Wal-Mart pledged \$1 million to UNCF over a four-year period.
- Sponsorship of the Competitive Edge Scholarship Fund. In 1993, Wal-Mart teamed up with participating vendor-partners to start the fund, which makes four-year scholarships—each worth \$20,000—available to students pursuing technology-related college degrees.
- Since 1993, Wal-Mart and SAM'S Clubs associates have raised more than \$52 million in support of local United Way agencies.
- Wal-Mart Stores, Inc., is the number-one sponsor for the Children's Miracle Network Telethon. Associates from all U.S. divisions of the company helped raise more than \$71 million for CMN since 1988. In calendar year 1996,

Wal-Mart donated \$14.3 million, or 10 percent of the \$143 million raised in the entire CMN campaign.

- In 1994, the 7,784 local charitable projects selected by associates received \$6,572,531 of matching grant funds from the Wal-Mart Foundation.

### Marketing

The discount retailing business is seasonal to a certain extent. Generally, the highest volume of sales and net income occurs in the fourth fiscal quarter and the lowest volume occurs during the first fiscal quarter. Wal-Mart draws customers into the store by radio and television advertising, monthly circulars, and weekly newspaper ads. Television advertising is used to convey an image of everyday low prices and quality merchandise. Radio is used to a lesser degree to promote specific products that usually are in high demand. Newspaper and monthly circulars are major contributors to the program, emphasizing deeply discounted items, and are effective at luring customers into the store.

Efforts also are made to discount corporate overhead. Visitors often mistake corporate headquarters for a warehouse because of its limited decorating and "show." Wal-Mart executives share hotel rooms when traveling to reduce expenses. The company avoids spending money on consultants and marketing experts. Instead, decisions are made based on intuitive judgments of managers and employees and on the assessment of strategies of other retail chains.

Wal-Mart censors some products. The company has banned recordings and removed magazines based on lyrics and graphics, and has stopped marketing teen rock magazines. Wal-Mart advertises a "Buy American" policy in an effort to keep production at home. Consequently, Wal-Mart buyers constantly are seeking vendors in grass-roots America. In Tulsa, Zebco responded to Wal-Mart's challenge by bucking the trend toward overseas fishing tackle manufacturing. Zebco created more than 200 U.S. jobs to assemble rods and manufacture bait and cast reels. The company's bait and cast reels are the first to be manufactured in the United States in 30 years.

### Innovations

Wal-Mart's Innovation Network (WIN) is one of two related services that provide entrepreneurs with a point of entry into Wal-Mart's mammoth distribution system. "The key to our approach is our use of consistent standards and open criteria," explains Gerald Udell, a professor at Southwest Missouri State University and the executive director of its Center for Business and Economic Development. Udell conceived, designed, and now administers the two Wal-Mart entrepreneurial support efforts, WIN and the Support American Made program. These programs already have helped over 3,000 inventors and entrepreneurs by evaluating products and prototypes for possible distribution by the chain.

For a \$175 fee, entrepreneurs can submit their products and detailed company information to a team of analysts. Within two months, applicants receive a detailed evaluation of their company and products. These programs are aimed at explaining reasons that Wal-Mart does business with some and not with others. Instead of giving a simple no, they explain how to get a yes.

In conjunction with Chase Manhattan Bank, Wal-Mart introduced its Wal-Mart MasterCard. There is no annual fee and a low 14.48 percent APR fixed rate for purchases. On transferred balances, the APR rate is 9.9 percent.

## COMPETITORS

Kmart is the second-largest U.S. retailer. However, compared to Wal-Mart, the scope of Kmart's problem becomes evident. Even though each company operates roughly the same number of stores, Wal-Mart's sales are roughly three times Kmart's sales of almost \$34.4 billion. Wal-Mart's discount stores are larger than Kmart's and produce sales of about \$300 per square foot, or twice the amount of Kmart's.

Should Wal-Mart, the price leader in discounting, choose to sacrifice \$0.10 to \$0.15 of its earnings per share, it virtually could ensure that Kmart would not operate above the break-even point.

Kmart is in a capital-intensive battle with Wal-Mart, whose annual capital expenditures are nearly four times that of Kmart's. Kmart's capital resources for this battle are limited, and if its earnings fail to improve, it cannot stay in this capital-intensive race for long. When Kmart cut its dividend rate in half, management took a step in the right direction to conserving its financial resources. The new CEO's recommendation regarding the dividend payout will be a litmus test of the urgency with which management intends to apply the company's assets toward turning around the Kmart discount stores.

Supercenters are revolutionizing the discount store battlefield, just as tanks redefined trench warfare. Wal-Mart started 1995 with 68 Supercenters, but by 2000, it will operate 800 to 900, and each will shatter the profit potential of at least one older Kmart discount store. This is the dusk of the discount-store era, and improvements in the merchandising and systems of Kmart's discount stores might do little to forestall their decline.

Kmart has slowed its rollout of its Super Kmart Centers to allow more time to develop the staff and skills needed for these stores to achieve an adequate return. By the time the rollout reaccelerates, Wal-Mart probably will be operating 500 Supercenters, and retailing will have changed greatly.

On a positive note, Kmart's board has been strengthened by new appointments and is steering the company; new management provides a fresh perspective for the company; new strategies are being implemented; same-store sales are strong; expenses are being reduced; and earnings should rise in 1998. Kmart's earnings rose dramatically to \$249 million in 1997.

J.C. Penny and Sears responded to the reality of retail competition several years ago by offering consumers better values than before. They have succeeded in lifting their sales, in both dollars and units. Kmart planned to take market share from them, but was blocked. As this escape route from direct competition with Wal-Mart closes, Kmart must protect itself and fight an uneven battle with Wal-Mart and with another strong firm, Target. Dayton Hudson added 60 new Target stores in 1997 alone for a total of 796 stores.

## FUTURE STRATEGIES

What strategies would you recommend to CEO David Glass? How aggressively should Wal-Mart expand internationally, and where? Should Wal-Mart get a foothold in Europe before competitors seize the initiative? Should Wal-Mart expand further in

Mexico, the United States, or Canada? Should Wal-Mart make further acquisitions such as their Woolco acquisition in Canada? Is Wal-Mart's rate of growth of Supercenters too fast? What can Wal-Mart do to improve its SAM's Clubs operations?

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