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Conference Call Transcript

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CORPORATE PARTICIPANTS

Carol Schumacher

Wal-Mart Stores, Inc. - VP IR

Lee Scott

Wal-Mart Stores, Inc. - President, CEO

Hank Mullany

Wal-Mart Stores, Inc. - SVP & President, Northeast Division

CONFERENCE CALL PARTICIPANTS

Adrienne Shapira

Goldman Sachs - Analyst

PRESENTATION

Adrienne Shapira - Goldman Sachs - Analyst

Today's retail sales. Thank you all for spending the day with us. And just to run through sales a bit, let's just walk through our Goldman Sachs Retail Composite Index to get a sense of what the month's look like. It was up 1.6%; our estimate was 0.6%. If you dig down beneath that, department stores were down 3.8%; our estimate was down 3.2%. Specialty apparel, down 3.4%; that's versus our estimate of down 3.1%. But the big upside surprise were, was found in the discount stores--up 3.4% versus our estimate of 2.0%.

A big reason for that outperformance is our lunch presenter today. What a difference a year makes at Wal-Mart, and it's clearly been reflected in the stock price. You heard us talk about our Goldie Award yesterday, and that's given to the company with the best stock performance. And Wal-Mart came in third place, up 37% year over year, from conference to conference. Had we market cap weighted that award, Wal-Mart would have won by a mile.

So let's just think about that in the context of where Wal-Mart's been over the past two years. Sure, a tougher environment stacked the deck in Wal-Mart's favor given its more defensive mix, but after two years of talking about a turnaround effort, we are clearly seeing signs in store and in their results.

And someone who can help us understand how much of it is driven by the cycle and how much of it is driven by their execution, we are thrilled to have President and CEO, Lee Scott.

Before Lee takes the podium, Carol Schumacher, VP of IR, will walk us through the good news of the day.

Carol Schumacher - Wal-Mart Stores, Inc. - VP IR

Thanks, Adrienne, and thank you all for your interest in Wal-Mart. We are clearly a global company, and the formats that you see here represent a few or a handful of the formats that we do have around the world. Back in mid-August, we announced our second quarter results, and we were pleased with the solid quarter that we had. Our net sales were \$101.6 billion. This was the second quarter that we had achieved \$100 billion in sales in a quarter, the first being the fourth quarter of last fiscal year.

I won't go through any of the numbers, but do want to point out a couple of highlights for the quarter. We did achieve free cash flow of approximately \$4.9 billion for the first half of fiscal '09, and that compared to a deficit of nearly \$800 million the previous year. Our consolidated gross margin improved by 32 basis points, and that was driven by strong performance in inventory management and merchandise flows at our Wal-Mart US operations.

But we considered one of our most significant achievements to be the fact that our ROI for the quarter was 19.3%, which was flat. And I would certainly like to refer you to our website for additional details on the quarter.

As you know, we may be making forward-looking statements here today, and you can certainly get additional information about our Company on the website.

As Adrienne referenced, with Retail Sales Day today, we did announce our results this morning before the market opened. You can see the numbers here, but overall, the total net sales increased by 8.7%. So year to date, our Company's sales are now more than \$227 billion.

From a comp perspective, the numbers speak for themselves, as Adrienne pointed out. Our total US comp was at 3.0%, and our comps were strongest in grocery and health and wellness. But we also pointed out this morning that both back-to-school and back-to-college gained a lot of momentum, especially in the back half of August. We believe this is due to Wal-Mart's very strong value proposition and our ability to deliver on our mission statement of "Save Money and Live Better."

Some specifics on that performance--denim in our Apparel division, licensed apparel items, and items that college students needed for their dorms or apartments all did well. So that also sends a message that we are pleased with our performance and the improvements we are making in Home and Apparel.

On the Sam's side, let me just remind you that our non-fuel comp excludes all fuel sales, not just the impact of inflation on fuel sales. But Sam's delivers strength in fresh food, dry grocery, and consumables. And I'd also like to point out that both traffic and tickets for Business and Advantage members helped drive our comps this past month. Fuel sales continue to remain a driver, both in sales and traffic for Sam's Club.

And I'd like to close by pointing out that our guidance for the five-week September period, which is well underway, is between 2% and 3%.

And with that, I'd like to turn the program over to the President and Chief Executive Officer of Wal-Mart Stores, Inc., Lee Scott.

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

Thank you. Thank you, Carol. Wow! An impressive room, but I can see the back table. They were concerned that they might be able to take a nap and not be seen. I can see you.

As I start this presentation, there are three things that Carol has outlined for me that are takeaways that you are supposed to understand when I finish. Rather than embed those somewhere in this discussion, let me just cover them, and then I can tell her I've done my job.

Number one is that Wal-Mart is well positioned now and for the future in meeting our mission of saving people money so they can live better.

Number two is the capital efficiency model is on track to meet reduced capital expenditure levels this year of a range between \$13 billion and \$14 billion.

And number three is a strong management team throughout Wal-Mart Stores organization is behind the solid results and laying the groundwork for a solid future.

I would add one more, Carol, and that is that from a responsibility standpoint beyond the business, we believe that we have made significant progress in the last several years and have the opportunity to continue to make progress in areas such as health care, sustainability, job opportunity for our associates, and responsible sourcing.

Let me go through just a little bit of my view of the world and the economy, recognizing I'm not an economist, and then I'll talk about each of our divisions after I talk about the Company as a whole, and then what I'd like to do is leave most of the time for questions.

One of the great things about this job is you get to see a lot of people; you get to travel, see much of the world. I've been in stores in the last several months from Russia to China to Japan, from Nashville to New Jersey, and this, yesterday, I've talked to a lot of CEOs from around the world. They all are facing the same challenges--the inflation that is embedded in energy and the impact that is having on their customers, the inflation that is embedded in food and the impact that is having on customers. It is clear that the customer is putting more of their pocketbook into energy and food than they have historically, and that has implications for all of us as we think about how we merchandise our stores, our clubs, how we run our businesses.

It is also true that what you see is that the customer is moving to values. In many cases, they don't have a choice. I have a perspective that maybe is a little different than some, and it's simply an opinion, and that is that even people who don't necessarily have to save money today want to, because they don't want to seem out of touch with what's happening in the greater part of society. They don't want to feel like they're being treated special or treating themselves in a special way when so many people are, in fact, suffering. And so we see people who are more willing to look for value than we ever have in the past.

Food inflation has risen rapidly in the first half of the year. There is some likelihood that those increases will diminish, that they don't have to be ongoing increases. On the other hand, in the area of consumables, many of those increases did not get into the price of merchandise. You saw large companies make announcements and revise earnings because they were not able to get the input increases into their wholesale prices at a fast enough level. Some of those will continue, then, to hit into the price and cost of products through the fall of this year.

The third element of increased pricing that we see as we travel around the world and talk to other people is what's happening in individual countries. Some countries have been subsidizing raw materials and energy to build the export business. Some of those countries are not harmonizing those prices, and it is likely this fall and early next spring that as those changes are made, that you would see some increase in pricing on some imported merchandise.

Overall, though, it's very interesting in that worldwide, the customer is pulling back in certain areas, but in areas where they have an interest, they are fully willing and capable to spend. So we talk about the energy costs in the US. We talk about the food costs in the US. But yet, flat screen LCD TVs are increasing in sales dramatically, and people are buying the HDMI cables at the same time they buy those televisions. People are buying video games. People are buying cell phones. People are participating in things that they are very, very interested in--things that are new, things that are exciting, things that they believe contribute to their overall quality of life.

The danger is on those things that are in the middle or those things that are on the fringe. I hope to get back to that as I talked about Wal-Mart US and some of the things that Wal-Mart is doing.

There's been discussion about Wal-Mart in this market where capital is somewhat constricted, difficult to get. Have we seen any implication to our worldwide business? The answer is no, because at a time like this with a strong balance sheet, quite honestly, it plays to our strength. And the relationships we have with our bankers have allowed us to continue to be able to do the things that we need to do.

We think it is the right time to be thoughtful about what it is you do, but on the other hand, it is not the right time to be fearful. So we are very opportunistic as we see opportunities to move into new areas. People say, "Well, does that mean just new countries?" No. Do you realize with the price of fuel going up and the price of food going up, we now are having an increased number of communities who are contacting us and asking us to build a Wal-Mart store in their town or in their state, and some of those are the very towns and states you would have read about historically who were not that enchanted with the prospect of a beautiful Wal-Mart store.

I think it turns out, through serendipity or through the pressure of our shareholders or whatever the combination might be, that our move to a capital efficiency focus this past year was absolutely the right thing to do. It has positioned us very well for this market. What we're seeing worldwide is that those stores closest to the customers seem to be doing the best. Our small store program in Central America, small store program in Argentina, the Chango Mas stores, some new small stores we're opening in India are doing very well.

We're also finding in the US, the 100,000-square-foot Super Center in the metro area is very successful. The 143,000-square-foot store, the 175,000 versus the 195,000 is doing very well.

So that decision to really look at our use of capital and to make sure that we were being prudent and thinking about our shareholders in the appropriate way has turned out to be very, very significant to us.

I want to talk a little bit about the management team at Wal-Mart. I have in the past shamelessly taken full credit for the \$4.00 generic drug program, the three-year plan. And what else, Leslie? Inventory control, "Save Money, Live Better"--I thought that up one night. But the truth is, as any of you who know me, I have no relationship with any of those other than to have been smart enough to not stand in the way of any of them.

We have a strong management team. The way we are running Wal-Mart today is that we are running it in a very much a divisionally structured manner. Mike Duke is the President of Wal-Mart International. He has the responsibility. We do ask that he tells us before he acquires people, but it is his responsibility to run that organization. It is Doug McMillan's responsibility to run the Sam's group. It is Eduardo Castro-Wright's responsibility to lead the Wal-Mart US team and get the results that we need to get for our shareholders, for our customers, and for our associates.

We also, though, have a very strong team that backs them up. We have a very strong CFO who is committed to the appropriate controls. We have a very strong general counsel, Senior General Counsel in Tom Hyde--and, by the way, having a strong General Counsel at Wal-Mart is quite important--who has done a great job for us. We have strength in Human Resources with Susan Chambers, and Systems with Rollin Ford, who came out of Logistics. And then Leslie, one of the best hires that I have ever made, who has really helped us to understand our responsibility to society and how to better tell that story, because we have a great story to tell. So we have a very strong senior team.

Let me walk briefly through the individual groups. First of all, people ask me, are we still committed to the club format? We are still committed to the club format. In this day and time, when people need value, the club format offers the greatest value that there is. It is, and I remember Sam Walton saying it one time, "It is the most efficient form of retail that exists in this world today." As you look at the releases, the one group who all three did well were in the club business--the Costco, BJ's, and Sam's Club.

It is a business that we operate in successfully. It is also a business where we have great competitors and where we must continue to get better. Doug has that fairly in his sight. We have just promoted Cindy Davis to Executive Vice President of Marketing and Membership, and we feel like that is an area where we can strengthen ourselves. She's been a new addition over the last year, has done a remarkable job. We think that we can continue to enhance the membership value of belonging to Sam's Club.

In addition to that, there's testing going on at Sam's Club--the business center in Houston, where we're going to be serving the business needs of our members. But we also have some other things that we're working on that we're not announcing at this time that I think will help to energize the club format for Wal-Mart. It is a good business, but it could be a lot better, and that is our focus.

Wal-Mart International really has a portfolio management strategy. We have now a President of Wal-Mart Asia, Vicente Trius, who is over, responsible for Japan, China, and India. We have a President of Wal-Mart, the Americas, Craig Herkert, who is responsible for everything in the Americas except for the Wal-Mart US and Sam's Club. And then we have Andy Bond, who's doing such a fine job in the UK.

Mike has diminished the role of the central headquarters. He has moved people out into those regional offices, running them closer to the place of business with more autonomy among these Regional Presidents. We think that is working very well. We are gaining significant market share in every market we are in, with the exception of Japan. And most interesting to me and probably less so to you, is today in all of the countries we are in, the President of Wal-Mart in that country is seen as promotable at least one level. That's the first time we have ever been in that position. Many of our best leadership talents today are running the individual countries that Mike is responsible for.

We are pleased, as I said, with India. We are exploring Russia and Eastern Europe. But we are committed to not lag plant. We have a strategy for the Americas. But we are not going to go to Europe, buy a chain of 40 stores in a country that has a unique language, and then try to cause that country to contribute to the value of our shareholders. There is no value in us doing that. We're going to concentrate on the majors. We're going to concentrate on India, on China, on Brazil, on Canada, on the UK--on those places that make a difference.

Mike has done a very nice job, I think, of aligning compensation with the needs of the specific country. So in the more mature countries, there's much more of a reward for the growth and return on investment. In less mature countries where what you as shareholders would want is growth, then the management team is rewarded more for growth, but an appropriate amount for return on investment. We think this is the right way to run the business.

Sourcing is another area under Mike, and it's an area that we have told our shareholders that we are working on. I believe we started telling our shareholders that in 1984. We are still working on it. It is a strength of the Company, but it is not nearly the strength that it needs to be. We have a meeting in China on October the 22nd that I think is one of the most important meetings for us that we will have this year. We're bringing together 1,000 of our suppliers in Beijing, and we're going to talk about Wal-Mart's commitment to socially responsible sourcing.

It is my belief that the person who cheats on overtime, who cheats on forced labor or the age of the labor, the person who dumps their scraps or their chemicals in the river, the person who cheats on their taxes, that there is no way that that supplier isn't ultimately going to cheat on us--either in the form of quality or somewhere down the road in their ability to perform.

We think that improving our relationship with our customers worldwide is tied hand-in-hand with improving the quality of the factories and the quality of the products that we get on direct imported merchandise. And you're going to see a real commitment from us that we lay out in this October meeting. And that commitment, it won't happen overnight, but over the next three to five years, we expect a significant change.

Somebody out in the audience may be wondering, "Well, does that mean you think you'll pay more?" No. I think by making commitments and doing business with the right people, that ultimately, when you factor in all of the business issues associated with either disciplining customers or returns or a product that gets over here and fails testing, that at the end of the day, we'll be more competitive than ever by doing it the right way.

Wal-Mart US, a subject that's of interest to everybody in this room, has improved their results dramatically. They have improved their results, I think, because first of all, they have a clarity of vision of what it is that we stand for. They created "Save Money, Live Better." And under that simple phrase, they have been able to collectively have a focus and an understanding across the organization that allows them to execute to that principle.

John Fleming has been, reformatted that into thinking about merchandising as "win, play, and show." Sometimes I get confused and say, "Win, place, and show," and John gets mad. "Win, place, and show."

"Win" are those categories that are growing and where mass has implications, positive implications. We can win in those categories--flat-screen TVs, iPods, those kinds of things. We can win in that area.

"Play" is an area where maybe mass has a role to play, or maybe it's growth. But it's not both. And we can play in those areas and do good business.

And "show" is about categories that are important, but they're flat or declining, but you must have those, and you must be competitive in those areas for your customer. Your customer expects it. It's not something that you can walk away from or turn your back on.

John has taken those three simple elements and crystallized division for his merchants in a way that I think is causing them to get aligned with the overall strategy of the Company.

In the stores, Bill Simon came up with just simply, "Clean, Fast, and Friendly." And that's what he talks about. Clean stores, fast checkout service, and friendly associates. And just by hammering on those three things and causing an understanding in the organization about those three things being the driver of what we want to do instead of the multi--in leadership, it's easy to send a new email out every week that corrects last week's problems and refocuses everybody. And in some cases over the years, we've done that. In Bill's case, he stayed on the same things every day.

And what both John and Bill have done, then, is come around and use Stephen Quinn in our marketing department, whose team came up with "Save Money, Live Better," and they are using consumer information and feedback information from our individual stores that is much more robust than we've ever had in the world, and they're using that information, then, to validate the progress against these goals.

And they're holding themselves accountable every Friday morning with green light, yellow light, and red light. "Where do we stand on the customer experience? Where do we stand on associate engagement? Where do we stand on each one of these elements, be it in merchandising or be it in operations?" And running that business that way--really, I keep using the word "clarity"--that it has given clarity to the organization.

Another thing we've done as we've run these things divisionally, we've integrated Real Estate, Logistics, and other areas for the United States within Eduardo's department. And so what you now see is, instead of a Corporate Logistics Department, you have a Logistics Department that is embedded within the Wal-Mart Stores US group and working in a much more dramatic fashion about, "What does the future look like? What do we do about labor costs in the stores? How do we make it more efficient? How do we make it more effective?" It is, in fact, I think, making a big difference.

And by the way, I must say our Distribution Center and our Logistics group have done an incredible job of managing cost during this highly energy-inflationary period of time. I believe that we've raised our fuel mileage by almost 25% in our fleet since this started. It's a huge savings that is never seen as a savings because it's really just a reduction in cost increase. But our truck drivers and our Wal-Mart leadership in Logistics have done a wonderful job.

It's an interesting time in the Wal-Mart US. Who would have ever thought we would be celebrating 3% comps? And yet we are and feel like that we are on the right track. My belief is if you look at the team, if you look at the people who are running Food with Jack Sinclair and Pam Kohn and Dede Priest; if you look at the people who are running General Merchandise with Gary Severson in Electronics and Andy and the other teams that we have; and Scott McCall, we have a very solid US Merchandising team that believes that they can perpetuate the type of business that we have seen in the past.

You know, these are challenging times. Customers are constrained financially. There's an uncertain economy. There's pressure on trade. There's increasing discussion of economic nationalism that is out there. There's an election that creates uncertainty. But if you get to all of that, the truth is at the end of the day, we are well positioned to serve our customers across the world. The customer across the world is facing very much the same issues that the customer in the US is facing. We have the management team, I think we have the focus--but most of all, what we have is something that Sam Walton left us, and that is a philosophy that if you sell great merchandise for less money than anybody else, you're going to do a lot of business.

And we're going to stay true to that. We're going to make sure it's contemporary and meaningful for today's customer. But there isn't anything about what I see today, or what I see for next year, or the year after next, that tells me that people are going to want to pay more for less.

So with that, I think let's open it up for questions.

QUESTION AND ANSWER

Adrianne Shapira - Goldman Sachs - Analyst

Great. Thank you, Lee. Lee, we've asked all of our participants the first three questions, and then we'll open the floor up for your questions.

The first question on macro. How are you thinking about the macro backdrop over the next six to 12 months--better, worse, or the same?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

You know, it wasn't long ago people were saying that the second half of this year they thought we would see improvement. Interestingly enough, almost nobody is saying that in the first half of next year we will see improvement.

I did see something on CNBC--which must be true--that the housing market they now expect to turn in the fall of 2009. I think our view is, and our plans are built around the fact that this next year will look very much like this year did--that you will have to fight for your customers, you'll have to be the champion for them, and you have to drive value. So for the most part, I think we see next year as a challenging year but one in which we can do well.

Adrianne Shapira - Goldman Sachs - Analyst

The second question relates to margins. Over the next 12 months, do you expect margins to rise, fall, stay the same? Anything about near-term pressures, long-term opportunities?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

Well, I don't see any reason why they would fall. I think we would see margins staying in line where they are. Trying to be very careful as we have price increases and trying to see where we can push back and not have to pass all of that increase on if we can create additional gross profit dollars by taking a lower increase at the store or the club level. But if we have an increase in margin, I would hope it's because our inventory management program causes us to continue to make progress in markdowns and continues to allow us to make progress in strength, and additionally, that we continue to catch hold in areas like Home and Apparel and we get an advantage from mix.

Adrianne Shapira - Goldman Sachs - Analyst

Great. And then lastly, as it relates to capital allocation, we've heard last year, obviously, you reined in square footage. How do you think about it? Are you more guarded or less guarded as it relates to capital allocation across leverage, buyback and real estate?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

I think we try to always be thoughtful about capital allocation. In our case, we know how many stores we're going to build for the next five years. We know about where those stores are. We know what we want to do internationally with new stores. Probably the only thing that's out there that you would say we would be opportunistic, and that is, "Is there an acquisition in a country that is meaningful for us that might come up?" And in those cases, on our five-year plan, we don't plug acquisitions in. So I think you'll see us continue to just be thoughtful about what we're doing.

The one thing we are going to do, though, as we've seen the results from the refurbishments of the stores, similar to what we were in yesterday in New Jersey, you will see us spend capital in the next year against store remodels. As that Merchandising Operations team in the US has finalized on what the looks are, what the sense is they want to do in the Home pad, the Electronics pad, the Apparel pad, I think they have a little more enthusiasm and a little more courage about going ahead and getting the remodels done. Held off a little bit in the last two years as we more tried to define, "What does that future look like?"

Adrienne Shapira - Goldman Sachs - Analyst

Great. There's a mic out in the audience, so if there are any questions, as the mic is making its way, let me just continue to lead with some questions. A few years ago, Eduardo was here talking about the three-year plan for the US. His timing was right; things are falling into place. Give us a sense of where do you think we are in that three-year turnaround?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

Well, I think as far as the three-year plan, we're in the last six months, so I asked him the other day, "Where's the next one?" And the Company intends to be around a long time. He said, "Don't worry. I've got a good one."

I think, if I was here last year--Eduardo's, he and I have a great relationship--and it's funny, because Eduardo says if he had done anything differently, he would have moved faster. I'm going to tell you, this time last year, I wasn't sure either one of us was still going to be with Wal-Mart. So moving faster at that time really wasn't an option.

But it turned out the plan is right. And it's not only the plan is right, the execution of the plan has really been exceptional.

There are very many interesting things that Wal-Mart US is testing today and working on today. Because of the size and scope, they can do things in 20 stores, 200 stores, 50 stores. They can really push the bubble. And so as we get the results of some of those tests back and understand where we want to go, where do we want to push the accelerator down, then I think those will be integrated into the next three-year plan.

I think an awful lot of it is going to revolve around customer experience--an awful lot of the next three-year plan. And we have a world of opportunity there. And a world of opportunity to better define assortments for our customers and offer them a wider range, whereas today in many cases we have lots of items within a certain price range. And I think you'll see John Fleming make real progress on getting brands in that really do provide a meaningful assortment.

Hank Mullany - Wal-Mart Stores, Inc. - SVP & President, Northeast Division

I'm Hank Mullany, Senior Vice President and President of the Northeast Division for Wal-Mart. Lee, you mentioned you had a chance to visit a couple of stores in the Northeast yesterday. You want to share some observations or key learnings? Or things that I should focus on?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

Yes. Hank is a reflection of how we're really running the Company, because Eduardo has taken and placed Bill Simon as Divisional Presidents out in the field. And Hank is responsible for this area. This area is leading our profit growth this year. And I'm sure that's why Hank was brave enough to ask a question.

And the stores yesterday, if I went back, it had been two years since I'd been in either store. The stores yesterday looked substantially better than they would have two years ago. Clearly, the Union, New Jersey, store was outstanding. The associates wanted to all say hello, they wanted to tell their story, great stories about associate opportunity and job opportunity and where they've gone and the leadership of Wade, the store manager.

The other store wasn't good, and I was disappointed. It wasn't nearly like the stores were when they were so bad at the year end, people who owned our shares would call me and say, "I was in your store." But I want us to be past that. This is a Company whose time has come to surge again, and we can't surge in nine out of ten stores, or 99 out of 100. We've got to surge in 100 out of 100. And while there are reasons for what I saw to exist, we have to get past that, and we have to be consistent. And if that customer drives in there, they've got to know that store is going to be in stock on brooms and mops. And so I was disappointed, and my disappointment is driven by a higher standard.

A year and a half ago, if I'd have gone in that store and it looked like that, it would have been so much better than the prior year, I might have been happy. But our Operations Team is on a roll, and we've got to get every store, every store manager and every associate, engaged in that. But I appreciate the sales and the earnings, Hank, and the opportunity to do your midyear eval in front of 900 people. Another question?

Unidentified Audience Member

Yes. Are you still itching to get your hands on a bank, and do you think the credit crisis has perhaps improved the political climate for you to do that?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

I think the current financial difficulties reflect a good reason why Wal-Mart should be allowed to be in banking. I have very little confidence that we will be allowed to be in banking. I think our people, through Financial Services, through Jane Thompson's leadership, have done a remarkable job, and I think as shareholders, people will be very pleased with the ongoing success of that organization. And we will find other things we can do to serve our customers' financial needs. But I think getting a bank charter is just going to be extraordinarily difficult.

Unidentified Audience Member

Good afternoon. Two questions for you. One, you had begun talking about price increases and had noted that not all of those had gone through. In working with your supplier partners, is that because not all of those increases were justified or that the pace of them would be too much of a shock to your customers, and so they're more on a delayed path? And what's happened with their brand versus your own private label brands within the stores? And then the second question I had--.

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

Can we do one at a time?

Unidentified Audience Member

Sure.

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

I've reached the age where I just can't. As the champion of the customer, your initial reaction to every price increase, justified or not, that comes through is to say no. That's just the first response. Then, when people come back, it is to try to understand what--let's just take this item. If this item is \$1.00, and they come back and they say, "Because of the price of oil increase, we have to raise this item to \$1.10," our people then will ask them for the breakdown of the costs associated with this. "How much oil is in this?"

And what you many times find out is that they need a cost increase, but the cost increase needs to be 2%, not 10%. And they're looking, sometimes suppliers are looking at an inflationary period of time to build in more penny profit for themselves. So we are very rigorous about pushing back, delaying when we take them. I know other retailers say that they're going to be the last man standing in taking price increases. Many of us are that way. And you just have to fight for them.

And then in other cases, you'll go ahead and take the price increase, but maybe while your competitors are moving up on that price, maybe you'll do a rollback. So where they were right on top of you, maybe you can do a rollback. They take the price increase, and all of a sudden you've got a

spread and you can try to create more gross profit dollars through that. But you have to understand somewhat the price-demand elasticity of the item and whether or not selling it for less creates more gross profit dollars.

John Westling has just done a fabulous job--because that's complex--of helping to set up a pricing group to better understand where do you just pass it on and where do you take more dramatic action. And that's been very helpful.

We are having a significant increase in the sale of private label merchandise. We're not doing anything different. We actually have hired a young woman to head that area, Andrea Thomas, who is doing a fantastic job. And it will be rolling out--her work and her team's work will be rolling out this fall. But we are having a significantly greater increase in private label than we are in non-private label.

Unidentified Audience Member

And then the second question I had for you. You've obviously had a couple big wins for the Wal-Mart brand in generics and in your environmental efforts. It sounds like that perhaps your sourcing meeting in a month or so might be another big win. Or is there something else that you have on the dock for the second half of this year to surprise folks?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

I wish there was a surprise we were holding back. But I will tell you, in this environment, if we get a good idea, we try to get it in this afternoon. I think the sustainability movement at Wal-Mart has shocked me, it has been so overwhelmingly embraced by our associates and by many people outside of Wal-Mart who have historically not been friends of ours. It is the elimination of waste, it is running a better business, it is coming back to the very core beliefs we have. And at the same time, in executing to those beliefs, allowing people to embrace us who would not have. It also is causing young people who work for us to be more energized about the Company. It's created a level of excitement.

I think the sourcing meeting in China will be just as big, if not bigger, than what we're doing in sustainability. I think it's all part and parcel. I think it will make a huge difference for us. As this world becomes increasingly concerned about global trade, and being the world's largest retailer, we have got to be on the forefront of ensuring that global trade is done in a fair and wholesome manner and a manner which our customers would be proud of how we as a Company are conducting ourselves. And I think China in October is going to give us the opportunity to start that journey.

We've been on it incrementally, but we need to take a stand, just like we did on sustainability. We want you to not only be able to be proud of what our comps are and what our earnings are and what our share price is, but we want you as a shareholder to be able to be proud of what this Company stands for and the difference that it makes on the "Live Better" side of the equation.

Unidentified Audience Member

Mr. Scott, could you please give us some guidance or some color on the progress that Wal-Mart has made in terms of the expansion to Russia? What sort of opportunities do you see there, and what are the main pros and cons in the face of this potential expansion and any challenges you see?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

Long term, Russia has natural resources and a fairly low population density, so the likelihood of Russia being economically successful for a long period of time in this world is probably substantial. We would like to be in Russia. We would like to be there in a way that has appropriately evaluated the risk and the rewards. How much money do our shareholders want us to risk at a time like this if we were to do an acquisition? Or how much money would our shareholders like us to not risk?

On the other hand, 20 years from now, do our associates want--do our shareholders want to sit in a meeting like this, and Wal-Mart has done nothing in Russia, and Russia has evolved and is one of the best retailing environments in the world? We think we have an obligation to our shareholders to be there, but we think we have an obligation to be extraordinarily prudent about it. I would like to be in Russia sooner than later, but we are going to do it at the appropriate time.

You know, it took us a long time in Brazil. We got a lot of criticism. But you know what? We built a base, we created a management team, and we have now great success in Brazil. And that, to me, is the same opportunity that we have in Russia. I don't have a sense in retailing that you have to be the first one there to win. If that is true, Wal-Mart wouldn't exist as a company.

Adrianne Shapira - Goldman Sachs - Analyst

Lee, if I could follow up on that. Over time, how do you see the, or the long-run distribution of sales and EBIT contribution across the US, International, and Sam's?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

We see there is pressure on International to raise their return on investment as markets mature. But at the same time, in those individual markets, then, to take some of those dollars and invest in the markets where we believe there is long-term growth. So part of our program has always been to continue to improve every day. So there's always pressure on Mike or Eduardo or Doug to do that.

I see the balance. I mean, if you see anything, you'd like to see the ROI within the International group continue to go up as we have more markets that mature and we start for our shareholders being able to harvest the investments that have been made historically. I don't see a big change other than the ongoing change through sales per labor hour, efficiency of stores, size of stores, and those things that we're continuing to make improvements in the Wal-Mart US side.

And then in Sam's, hopefully being able to take the dollars that we have and reinvest in price and reinvest in membership services that allow us to be particularly special within the wholesale side of the business.

Unidentified Audience Member

One of the major markets in the world is Japan, and you have a major position in the country and a pretty big foothold, yet it doesn't seem to be getting the traction that some other places have.

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

Well, we don't sell for less. I mean, we have a model, except for the Superama in Mexico. We have a model that where we sell for less, we do the business. In Japan today, what we're doing is we are rolling out Everyday Low Price, and we're rolling it out by individual departments and we're rolling it out geographically. And we have a very disciplined program to do that.

And what we're doing in Japan is we are rolling out Everyday Low Price before we are rolling out Everyday Low Cost, and we are forcing the costs down. So if I was over there a few weeks ago, we have taken 230 basis points out of cost in the stores. We've taken 25% of the home office expense out. We are forcing the issue.

And what we're doing, though, is trying to continue to make sure that we're cash flow positive in Japan, as we have been. But there's no reason to spend our time trying to figure out how to make \$100 million in Japan in the current circumstances. The real issue in Japan is how do we get Everyday Low Price so we can win? And that is where the whole focus is.

I was very encouraged at the stores. I think you would be encouraged with the way the stores look today versus two years ago, encouraged with the management team, and I am encouraged with the reaction of the customer to EDLP across consumables, across pets, across any number of categories where we're doing it. It is just a process that we are going through.

And so my--what Mike told me when I went over there, he said, "I think when you return, you will be encouraged but not satisfied." And that is exactly how I felt. I am encouraged about the direction but not satisfied with the speed. But also not deeply worried about whether or not we're going to get there.

Adrianne Shapira - Goldman Sachs - Analyst

Go ahead.

Unidentified Audience Member

You mentioned that smaller stores where you're closer to the customer have performed the best. Given the success of the proliferation of formats in Latin America, for example, what does that say about the opportunity for new formats here in the US? And related to that, can you comment on the Tesco initiatives and how that's impacting Wal-Mart?

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

It's very difficult to analyze what the Tesco format has done to individual stores. You know, if a Target store opens down the street or a Costco opens down the street, it's pretty easy to measure exactly what's happened. The size of those stores when they come in, and we have a \$130 million to \$140 million Super Center sitting right down the road, it's really difficult to understand what impact that they have. Our assumption is anybody who does any retail business impacts us, so that first of all, we believe--and we're paranoid--we believe they take some of our business.

I think that everybody here knows that there's been reports that they're not satisfied and other reports that they are satisfied. The thing that bothers me is Tesco is a very good retailer. And whether they're satisfied today or not, you know that they are going to continue to tinker with that until they figure out how to make it work.

So I have a lot of faith that they will find their direction, and it is something that we need to pay attention to. In fact, I just talked to Bill Simon about them yesterday, and Eduardo. So we're paying a lot of attention to them.

I think there's lots of opportunity for formats, I think, in the US. I think you'll see Eduardo continue, he and his team--Santiago Roces runs that area--you'll see new formats come out there. I think, with Mike and the team working worldwide on formats, you'll see an expansion of the formats that are working in Mexico, working in Brazil. And I think you'll see those rolling out in China and other places. I think you will see that that's part of being a global company. We'll accelerate over the next few years, and they're not all going to--you know, we're not going to put a bodega store necessarily in the US, but store in the US that might remind you of a bodega store, I think, is clearly possible.

Adrianne Shapira - Goldman Sachs - Analyst

Maybe I'll just ask the last question. You've talked about the benefits of embracing the capital efficiency model. We've seen the changes in the compensation structure of the senior management, and we've seen the results this past quarter upon ROI. Talk about what you've changed from top to bottom to get people more focused on embracing that returns focus.

Lee Scott - Wal-Mart Stores, Inc. - President, CEO

We actually have a very good Comp Committee at Wal-Mart. And it is chaired by Linda Wolf, who came out of the advertising industry. Doug Daft from Coca-Cola is there, and Allen Questrom is on that committee. Am I forgetting anyone? Because I don't want to overlook anyone on the Comp Committee, Leslie.

Anyway, and one of the things they've really helped us do is to make sure that we have alignment between compensation and the goals of the shareholders. And it has worked out really well as we this year used comp store sales as a focus in the US, whereas in some of the other international countries we're using total sales, because we're trying to drive total sales and we're not as worried about cannibalization. They have a real focus on return on investment, which has been one of the things that the analysts have really pressed us on.

So there's complete alignment with the strategy that we rolled out to our Board in 2006 on how we were going to run the Company, what we thought needed to be done, and then how you reward the management team for the accomplishments of those goals. And all of those things are aligned. And I think that has helped.

And I think the other thing is, is that the management team is on the same page. It is a group of people that in kindergarten learned to share their toys and to play well with each other. And I think that has made a difference in that Mike Duke and Eduardo, or Eduardo and Doug McMillan--two weeks ago Friday, Doug McMillan and Eduardo and I went out and just went to Joplin, Missouri, and just walked clubs and stores and

competitors and just talked about what's going on, and what would Eduardo do if he was in Sam's, and what would Doug do if he was in Wal-Mart, and, "What are you thinking about?"

And it is that alignment we have--all the way down through--and you just cannot understate the importance of Fleming and Simon and Quinn and Priest and Cohen and this team and the alignment that goes all the way through the organization, from Rob Walton, the Chairman, through the Board all the way down, and then everything supporting it. It is that that has done it. And they have done, I think, a remarkable job in an extraordinarily difficult time. And I have a great deal of pride in the team. And my only regret is that I can't stand up and just simply take credit for it. Because if I could, I would.

So anyway, thank you all for being here.

Adrianne Shapira - Goldman Sachs - Analyst

Thank you.

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