Walmart’s Stock’s Selloff Hinges on Perceived Economic Gloom

Within minutes of Walmart’s announcement on Wednesday that the world’s largest retailer would see its profits drop between six and 12 percent next year, the company’s stock started a decline that only ended after it had lost 10 percent of its value, its worst single-day performance in 37 years.

Despite a previous warning from Walmart in August that its quarterly profits, year-over-year, would likely fall by 15 percent, and despite the company’s stock continuing its decline from $90 a share in January to $67 before the announcement, investors were caught off guard. Now trading below $60 a share, investors have seen the value of their Walmart holdings drop by a third since the first of the year.

The selloff coincided with a report from the Federal Reserve that factory output was sluggish, thanks in part to the relatively strong dollar making American products more expensive overseas. Another report showed that consumer spending was essentially flat, except for new car sales. And a third report, the Empire State Index, showed that in the New York region, business activity declined for the third straight month, coming in substantially below forecasts. A close look revealed that the decline in new orders and shipments is accelerating.

Adding to concerns about the U.S. economy was the poor jobs report earlier in the month, and the continuing decline in commodity prices worldwide, reflecting a nascent global slowdown.

Investors were therefore trying to connect the dots: Walmart shares are off because the U.S. and world economies are slowing. As a result other retailers suffered losses on Wall Street following Walmart’s announcement, and both the Dow and the S&P 500 Index ended the day with losses.

A closer look at Walmart’s announcement, however, shows the giant retailer adjusting to changing market conditions, not necessarily shrinking. First, in order to draw to itself new workers in an increasingly competitive marketplace, the company announced in April that it would raise starting wages to $9 an hour, and to $10 an hour starting next year. That cost the company $1.2 billion this year, and will cost it another $1.5 billion next year.

Second, many of its 4,600 stores are getting long in the tooth, and the shoppers' "experience" has declined as a result. The company's internal "red" light or "green" light rating on customer service, cleanliness, and efficiency had put a majority of those stores on "red" alert. The company is committing $1.5 billion in new training programs for the new people it is hiring to turn that around. It's already seeing some positive results: Two-thirds of the company's stores are now in the "green."

Even that isn't satisfactory, said Greg Foran, Walmart's head of its U.S. business: "That is really only getting us to at best, mediocrity. So that bar is now being moved up so that a whole bunch of stores that were "green" are now going to find themselves "red" — but they've been told that."

And then there's Amazon, which has continued to eat away at Walmart's brick and mortar business with competitive prices, free shipping, and shopping at home convenience. As a result Walmart is making massive investments in its own e-commerce operations, expecting that its huge network of distribution centers will allow it to compete with Amazon with speedier deliveries. As Walmart CEO Doug McMillon asked, rhetorically:

> Here is a key question: will it be easier for an e-commerce company [i.e., Amazon] to build out a massive store network and create a customer-service culture at scale, or are we better able to offer digital and supply-chain capabilities and leverage our existing stores?

One thing that Amazon isn't yet able to do is deliver groceries. Walmart has slowed its growth in new Supercenter stores and is concentrating more and more on expanding its Neighborhood Markets, along with curbside and delivery services.

But even there Walmart has found competition it didn't expect: local grocers who often have fresher and broader selections of fruits and vegetables. As Walmart's Moran said: "To be completely candid, when we are up against someone who is really good at supermarkets, frankly, our fresh offering has not been on a par with what it takes to win in those environments."

Finally, Walmart has learned that squeezing its suppliers is a strategy — called supply chain management — that isn't likely to work as well in the future. Besides, many of its competitors have also learned that strategy, so Walmart must look elsewhere to continue to grow.

Interestingly, it is looking at upscale shoppers to give the company a boost. Part of the huge capital spending program announced on Wednesday is going to be invested in sprucing up existing stores in an attempt to attract a customer with more discretionary income. As McMillon expressed it: "You clean up your house before you invite people over." Globally, he added: "We know [our] growth will disproportionally come from middle- and upper-income households in the years ahead."

Those trying to connect the dots between Walmart's announcement and the trio of economic reports showing a slowing national and global economic outlook are reaching too far. Walmart is just doing what it does best: finding ways to serve its customers that are better and more satisfying than its competitors. For years that has meant low price. And it has been enormously successful. The *Washington Post* reported a decade ago that "Walmart's discounting on food alone boosts the welfare of American shoppers by at least $50 billion per year [equivalent to $60 billion in current dollars], while MIT measured Walmart's impact on consumer finances and learned that the poorest segment of the population has benefited the most from discounters like Walmart."

While Walmart's dependence upon that segment isn't likely to change very much, in the next few years a new Walmart is emerging, giving McMillon and his company the temerity to forecast that the behemoth company's profits will grow between five and 10 percent annually after the changeover is completed. Instead of reacting to what some perceive to be a slowing economy, Walmart is doing its best to keep the economy humming by keeping its existing customers happy and finding new ones to serve.

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