

Frontline

## Is Wal-Mart Good for America?

### One, Two, Three, Four ... We Don't Want Your Superstore

Across the country communities weigh the costs and benefits of opening their doors to the nation's largest discount retailer.

Wal-Mart has made billions selling toaster ovens and polo shirts for pennies less than its competitors; after all, the company motto is "Always low prices." And who wouldn't want cheaper goods? Yet some communities are fighting to keep the retail giant out of their neighborhoods, claiming that Wal-Mart's low prices could damage their quality of life. In Vermont, Wal-Mart's opponents argue that the state's economy and culture would be damaged by the retailer's presence. In California, opponents say the company has cost taxpayers millions by shortchanging its employees on healthcare. Here is a roundup of some instances of community backlash against Wal-Mart and the company's response.

#### **Superstore vs. small business**

Activists regularly argue that competition from Wal-Mart destroys small businesses, particularly the "mom and pop" stores that they say make their communities unique. This criticism has become even more vocal since Wal-Mart began moving into additional retail areas, such as groceries, opticals and flowers. In [an article](#) in the *Los Angeles Times*, one small businesswoman, Bonnie Neisius, owner of a UPS franchise in Las Vegas, Nev., described how she has watched surrounding businesses close and her own business decline since Wal-Mart moved in down the road. "I'm probably down 45 percent," Neisius said. "I just don't get the foot traffic anymore."

More recently, the retailer has come under attack in Vermont, where preservationists say the character, culture and economy of the entire state is under threat from an influx of superstores, particularly Wal-Mart. In May 2004, the National Trust for Historic Preservation put Vermont on its "endangered" list amid fears that Wal-Mart was planning a big expansion in the state. Wal-Mart already has four stores in Vermont; three of them are moderate-sized buildings -- 75,000 to 80,000 square-feet -- that have been designed with the input of the community and are situated in the heart of downtown areas. The fourth, built in the town of Williston in January 1997, was the first large, 150,000 square-foot Wal-Mart store in Vermont. Not long after, Williston saw other "big-box" stores -- Home Depot, Toys "R" Us and Bed Bath and Beyond -- move in next door.

Richard Moe, president of the trust, told the *New York Times*, "We know the effects that these superstores have. They tend to suck the economic and social life out of these downtowns, many of which wither and die as a result. I think it will drastically affect the character of Vermont, which I think is quite unique."

Mia Masten, a spokeswoman for Wal-Mart, told the *Times* that Wal-Mart often tries to work with communities and is not "just coming in and bulldozing our way in." "We've also heard from a lot of Vermonters who want a Wal-Mart closer to their communities," Ms. Masten said, "And

customers have told us they like a larger store. It enhances their shopping experience that there's a wider selection and the aisles are larger."

In St. Albans, Vt., where Wal-Mart has announced plans to build in 2005, some local residents are excited. "I thought it was wonderful news," David Giroux, a lifelong resident, told *The Burlington Free Press*. "You can't buy a set of sheets in this town. We've needed this for a while now."

### **Wal-Mart and the "health" of communities**

Another charge that local communities have made against Wal-Mart is that the company provides inadequate benefits and that local taxpayers are forced to pick up the burden. Critics say Wal-Mart's healthcare benefits are often so poor and the coverage is so expensive that many employees chose to go without it and instead get their coverage through state programs like Medicaid and or hospital charity.

A November 2004 *New York Times* article cites a study in Georgia that found 10,000 children of Wal-Mart employees were in the state's healthcare program at a cost to taxpayers of \$10 million a year. The same article describes a hospital in North Carolina that found that 31 percent of its 1,900 patients were Wal-Mart employees on Medicaid, and an additional 16 percent were Wal-Mart employees with no insurance at all. And in California, a study released in August 2004 by researchers at the University of California at Berkeley determined that the healthcare expenses of uninsured Wal-Mart employees were costing the already economically-strapped state \$32 million a year in taxpayer funds. Wal-Mart has disputed findings that the company encourages its employees to apply for public assistance and called the California study "biased," noting that the researchers at Berkeley did not contact the company for facts and statistics.

Wal-Mart officials claim that 90 percent of its employees are insured either through the company's policies or elsewhere. Wal-Mart spokeswoman Sarah Clark told FRONTLINE that over 500,000 of the company's 1.2 million U.S. employees are insured by Wal-Mart and that the company insures a total of 900,000 employees and their dependents. According to Clark, 29 percent of Wal-Mart associates are ineligible for coverage. Stringent eligibility requirements and the employee turnover rate may account for that 29 percent: Full-time employees must work for six months before they can be covered, and part-time employees must work for at least two years. Wal-Mart's labor turnover rate is 44 percent per year -- close to the retail industry average.

Wal-Mart's healthcare premiums are also high for the average associate's salary. Currently, Wal-Mart's employees must pay 33 percent of their healthcare costs: \$30.50 a month for an individual or between \$132.50 and \$230.50 a month for families. Wal-Mart argues that its associates are a different demographic base than most companies' employees. "One of the most significant facts is that about two-thirds of Wal-Mart associates are senior citizens, college students or second income providers, which also means that many of our associates receive their healthcare coverage from a parent, spouse or even Medicare," Wal-Mart spokeswoman Clark wrote in an e-mail to FRONTLINE. But Wal-Mart spokesperson Mona Williams admitted to the *Los Angeles Times* that Wal-Mart might not be the right job for a family breadwinner: "Wal-Mart is a great

match for a lot of people," she said. "But if you are the sole provider for your family and do not have the time or the skills to move up the ladder, then maybe it's not the right place for you."

Another argument from Wal-Mart's critics is that the company encourages its employees to apply for public assistance programs. [Jon Lehman](#), a former Wal-Mart manager now working to unionize Wal-Mart stores, tells FRONTLINE that he actively encouraged and assisted his staff with applying for public assistance. "I thought I was doing a good thing at the time, he said. "Now, when I look back, I think, 'Wow, that's incredibly poor that the company doesn't care enough about its workers to pay them a living wage and to help them with their medical costs, to pay their medical expenses and things like that'."

Wal-Mart's McAdam told FRONTLINE, "The accusation that we somehow direct our people to public assistance is just not true." "... When we have people in need, we're going to reach out to them and try to help them," he said. "... But we are not trying to offload our burden on somebody else." McAdam argued that Wal-Mart's benefits for its employees is similar to the industry standard: "I don't accept the premise that we are different from any other business in how we offer and provide health care coverage for the people that work for us," McAdam said. "We do offer a substantial and comprehensive benefits package to both full and part-time people with a reasonable waiting period for those who are in transition into our company." He reiterated that 90 percent of Wal-Mart's employees are covered "under one healthcare coverage or another," and concluded, "...Is there someone in our work force that's taking public assistance? Probably. But I don't think that's any different than any other business."

In November 2004, activists in California went to the ballot with Proposition 72, a statewide initiative that would require big employers, such as Wal-Mart, to offer adequate, affordable healthcare coverage to all of their employees or else pay into a state insurance fund. Wal-Mart campaigned strongly against Proposition 72 and stated, "Wal-Mart believes companies should have the opportunity to provide benefit choices that both they and their employees can afford." On Nov. 2, 2004, California voters rejected the proposed initiative 50.9 percent to 49.1 percent.

### **The communities decide**

In 2002, Wal-Mart unveiled plans to introduce 40 new Wal-Mart Supercenters in California. It also announced it was planning a combination Supercenter and Sam's Club to be located in the Los Angeles suburb of Inglewood, a middle-income, predominantly black community. "We looked at Inglewood ... there were not a lot of discount retail options," Wal-Mart Vice President Bob McAdam told FRONTLINE. "... We thought it would be a great location for a store that would serve people close to home." Wal-Mart argued the project would bring 1,000 jobs to an area that had been economically depressed in recent years, but local groups vigorously lobbied the city council to stop the project, claiming that it would be a net-loss for the community.

Citing independent studies by the Orange County Business Council and the San Diego Taxpayers Association, Inglewood activists argued that if Wal-Mart entered its community, good-paying union jobs would be replaced by low-wage, low-benefit Wal-Mart jobs. McAdam strongly disagrees with these claims. "I can look where we actually have caused jobs to be created in addition to the ones we bring," he argued, citing a location in Panorama City, Calif.,

that has been revitalized since Wal-Mart moved in. "When we came into that location, the mall that we're associated with there was basically boarded up and closed," McAdams said. "Every storefront is full today with little business that are adjacent to the Wal-Mart store."

But the Los Angeles City Council refused to consider Wal-Mart's proposal, and instead, adopted an emergency ordinance specifically designed to keep out large retailers. The ordinance requires that before a large-scale building project can be approved, planners would have to examine how the proposed superstore would affect the community. Undeterred, Wal-Mart garnered 9,250 signatures to take its proposal directly to Inglewood's voters in a referendum. McAdam explained Wal-Mart's decision to FRONTLINE: "It's really important to remember that the council specifically said they wouldn't consider [the project].... Our belief was that [an initiative] was the only way the voters were going to have their say."

Elsewhere in California, a dozen other communities like Oakland and Contra Costa County have passed zoning laws to keep out retailers like Wal-Mart. In Bakersfield, homeowners and union workers successfully fought Wal-Mart's building plans by arguing that the superstore would destroy local business. But in other urban areas, Wal-Mart has been allowed in -- even invited. In May 2004, after intense lobbying by both supporters and opponents of the superstore, Chicago's city council voted to allow Wal-Mart to build one of its discount stores on the West Side. And in Derby, Vt., 1,500 citizens have signed a letter to CEO Lee Scott asking the retailer to open a store in their community.

When Inglewood voters went to the polls in April 2004, they voted to oppose Wal-Mart's initiative by an overwhelming margin of 60.6 percent to 39.3 percent. Though that decision may keep Wal-Mart out of Inglewood, it will not stop the company's growth elsewhere, McAdam says: "The results were certainly not what we had hoped for, but we don't view Inglewood as some major setback. ... Just while everybody was talking about Inglewood, a number of other Wal-Mart Supercenter projects were being approved elsewhere in the state."

## The Economist Special Report

# Wal-Mart - How big can it grow?

**The world's biggest retailer is defying its critics by continuing to grow vigorously**

Apr 15th 2004 | FRANKFURT, LONDON AND VALLEY OF THE SUN, ARIZONA [[From the print edition](#)]

AT A recent retail-industry convention, Wal-Mart's boss, Lee Scott, was asked whether his firm was trying to take over the world. "I don't think so," Mr Scott replied with a smile on his face. "All we want to do is grow."

How big can Wal-Mart grow? With \$256 billion in sales in the year to January 31st, the firm is already the world's biggest company by that measure. Its nearest retailing rival, a French supermarket chain called Carrefour, is less than half Wal-Mart's size. In America, Wal-Mart manages nearly 3,000 giant discount stores and hypermarket "supercentres". Abroad, it has ventured into Mexico, Britain, Japan, Canada, Germany and China, as well as making smaller investments elsewhere. Eight out of ten American households shop at Wal-Mart at least once a year. Worldwide, more than 100m customers visit Wal-Mart stores every week. Photographs circulated over the internet and purporting to come from the *Exploration Rover* show NASA's recent discovery of a Wal-Mart on Mars.

The mathematics of big numbers suggests that Wal-Mart's growth must slow. Amazingly, the opposite appears to be happening. In America this year, Wal-Mart intends to open some 50 new discount stores and more than 220 new supercentres, some of which will be existing stores moving to new locations. Overseas, it plans another 140 or so new stores, including relocations. This adds up to some 50m square feet of new space—even more than many of its rivals operate in total.

As Mr Scott likes to point out, Wal-Mart still represents "only" 8% of total retail sales in America. It is not unusual for dominant firms in mature industries to command market shares of 30% or more. So, in theory at least, Wal-Mart could still get an awfully lot bigger.

Although the firm possesses undeniable momentum at the moment, its sustained smooth expansion is by no means inevitable. Wal-Mart's success is sharpening the acts of other retailers, some of whom are learning how to compete more effectively against the "Beast of Bentonville" (Wal-Mart's headquarters are in Bentonville, Arkansas). Legal and labour problems threaten the firm's decentralised, entrepreneurial culture—a culture which, until now, Wal-Mart has zealously protected against creeping corporate bureaucracy. Abroad, the firm's success remains in doubt, as does its ability to make money out of new retail formats at home. Most important of all is the likely future growth of its core domestic discount-store business, which makes up 65% of the firm's sales and 87% of its profits. When will that begin to slow?

One of the guiding principles of Sam Walton, the company's late founder, is to pass on savings won from suppliers to consumers, which encourages more of them to shop at the company's

stores and to buy more things. Wal-Mart then profits from higher sales, instead of simply putting the savings directly into its coffers. The company is skilled at obtaining products cheaply, and the emergence of China as a centre of low-cost production is playing to its strengths. Wal-Mart already buys \$7.5 billion-worth of goods directly from China each year and another \$7.5 billion via its suppliers, with scope for more in future. Shoppers make such big savings that economists credit Wal-Mart with driving down America's inflation rate.

This strategy of “Always Low Prices. Always” continues to surprise even Wal-Mart with its success. When Tom Schoewe joined the firm as its chief financial officer four years ago, Wal-Mart thought that its core discount-store business was about to slow, he says. The company began looking for other sources of growth by investing more heavily in different formats: smaller groceries, called neighbourhood markets, that were meant to fill in the spaces between the larger discount stores and supercentres, and a warehouse-style format, which Wal-Mart calls Sam's Club. But, says Mr Schoewe, Wal-Mart then changed tack. It began to realise that America's suburbs can absorb many more supercentres than the company had previously supposed.

## Glorious suburbia

If that seems fanciful, then spend the 45 minutes it takes to drive across Arizona's Valley of the Sun from Scottsdale, a well-heeled suburb of Phoenix, to the city of Surprise to the west. Between the strip malls, low-rise apartments and Whataburger franchises that dot the route, Wal-Mart's name pops up again and again. On a single 20-mile stretch of road sit six giant Wal-Marts, all of them doing a reasonable business on a recent rainy weekday. Shoppers have 14 more Wal-Marts to pick from a few miles further south and east. The area, says Mr Schoewe, with obvious pride, “shows you what can happen.”

The valley's sprawl—the Phoenix area has annexed 400 square miles of desert in the past 50 years—suits Wal-Mart perfectly. In other bits of America, the firm is finding growth more difficult. Some communities (notably in California and the north-east) oppose yet more supermarkets and edge-of-town hypermarkets. There are plenty of Americans who accuse the so-called “big-box” retailers of driving local firms out of business. In prickly California, Wal-Mart has tried to bypass planning committees by appealing directly to voters, so far without success. On April 6th, 60% of voters in a local referendum in Inglewood, a suburb of Los Angeles, turned down a proposal for a giant new Wal-Mart.

Some of Wal-Mart's new supercentres, which can range up to 220,000 square feet in size, are now being designed to be just a fraction smaller than the 100,000 square-



foot limits on retail units that have been imposed in some parts of America. For instance, Wal-Mart recently opened a 99,000 square-foot outlet in Florida.

In states with strong trade unions, such as New Jersey, Illinois and California, Wal-Mart has faced what has been called an “invisible picket line”: obstruction and boycotts, sometimes only on an individual basis, by people who object to its strong anti-union stance. Naturally, Wal-Mart has grown fastest where it has been easiest to build its big boxes. Per head of population, there are between five and ten times as many stores in Arkansas, Oklahoma, Mississippi and Missouri as there are in New Jersey, California and New York.

Wal-Mart is buying up land at an astonishing rate. The monthly real-estate meeting in Bentonville approves more than \$1 billion-worth of land purchases every time it gathers, says Mr Schoewe. Yet as Wal-Mart makes more of those purchases in the less-served, but more difficult states, growth will inevitably slow. It can take the company two or even three times as long to open an outlet in California than in Arizona, for instance. All the same, Michael Silverstein of the Boston Consulting Group (BCG), thinks Wal-Mart's core business has three years of decent growth left in it. Darrell Rigby of Bain, another consultancy, thinks there is “plenty of room at least through 2010.”

That growth alone would result in a firm with annual sales of somewhere between \$350 billion and \$450 billion. On top of this, investors must weigh the likely success of Wal-Mart's expansion overseas where, in the longer term, the firm will have to find the bulk of its growth. Traditionally, retailers are not very good at going abroad. Wal-Mart is no exception. It has done well in America's border countries. It has been successful in Canada, for instance, and in Mexico, where Wal-Mart is the biggest private employer.

But in Germany, Wal-Mart ended up with egg on its face. Even Mr Scott has admitted that the company's arrival was “somewhat embarrassing”, although the situation is improving. Wal-Mart entered Germany, the third-biggest retail market after America and Japan, in 1997-98 by buying two local retail chains, Wertkauf and Interspar, for \$1.6 billion. Whereas Wertkauf was well-known and profitable, Interspar was weak and operated mostly run-down stores. Wal-Mart has lost money in Germany ever since. Problems have included price controls, which prevent below-cost selling, rigid labour laws and tough zoning regulations, which make it extremely difficult to build big stores.

Wal-Mart also faced well-established rivals in Germany, like Metro, and hard discounters such as Aldi and Lidl, already comfortable with razor-thin profit margins. Many retailers in Germany are owned by wealthy families whose business priorities are not always the maximisation of shareholder value.

But there was more to it than that. Wal-Mart's entry was “nothing short of a fiasco”, according to the authors of a study at the University of Bremen. At first, Wal-Mart's expatriate managers suffered from a massive clash of cultures, which was not helped by their refusal to learn to speak German. The company has come to be seen as an unattractive one to work for, adds the study. In part this is because of relatively low pay and an ultra-frugal policy on managers' business expenses.

This contrasts with Wal-Mart's much smoother expansion into Britain, where it bought Asda for \$10.7 billion in 1999. Asda already had a strong business competing on price, and it has since overtaken struggling J. Sainsbury to become the second-biggest supermarket chain after Tesco. But that may say more about Sainsbury's difficulties in overcoming its problems than Asda's successes. Unlike Tesco, under its boss Sir Terry Leahy, Sainsbury was slow in responding to Wal-Mart's expected arrival in the British market. In particular, it was late in expanding into non-food goods, the source of much of Tesco's growth. Tesco, which now has half its retail space overseas, also competes with Wal-Mart in other countries.

## A force for good?

In the popular imagination, Wal-Mart ruthlessly exterminates the competition, especially local mom-and-pop retailers. Yet as Bain's Mr Rigby argues, Wal-Mart is more than just a destructive force. "Wal-Mart is good for retailing in the same way that any good predator is good for an ecology," says Mr Rigby. "Life works through struggle, and many retailers are better today because of Wal-Mart."

A number of retailers in America have gone up against Wal-Mart and survived—even thrived. They have deliberately avoided trying to do the same thing as Wal-Mart. Hence Target, based in Minneapolis, competes as a sort of "upmarket" Wal-Mart with low prices, but a more edited selection of goods. It also employs its own designers to create exclusive ranges. Costco, based in Issaquah, Washington state, operates a chain of membership discount-warehouses, which rival Wal-Mart's Sam's Club chain. Costco carries international brands and is particularly noted for its wines and surprises: it recently had \$52,000 diamond rings for sale. Costco also has a reputation for paying its staff well above the average union rates.

Then there is HEB, a 100-year-old retailer operating supermarkets in Texas and Mexico. It looked to be doomed when Wal-Mart rode into town. But it was re-invigorated into an award-winning grocer that impresses many in the industry. "They looked to where they had an advantage," says Mr Rigby. "They are, like Wal-Mart, an everyday low-price grocer. But you don't have to match prices on everything." One of HEB's features is a concept called "Central Market" which provides a wide variety of fresh and prepared foods within its stores, including on-site chefs who show how to prepare the evening meal.

All three of these retailers offer something similar: low prices, with something extra on top, be it a nicer shopping experience or luxury goods. Conceivably, this might hint at a more threatening market change: that shoppers might begin to tire of the attractions of rock-bottom prices alone. BCG's Mr Silverstein has written a book\* describing how American shoppers are becoming increasingly sophisticated in the way they discriminate between "trading up" to those goods they think of as luxury items, and "trading down" to the rest. "Costco does trading up and trading down under one roof," says Mr Silverstein. "Wal-Mart just does trading down. At some point, that will have played out."

Alternatively, the everyday-low-price pull may lessen as prices stop falling so quickly. Mr Schoewe says that, because Wal-Mart has already gained most of the advantages of importing goods from China, deflation in the Wal-Mart economy should slow down in coming years. He



maintains that this will be a source of future financial growth for the company. But perhaps slowing deflation will work in the opposite direction, as consumers no longer stampede with such relish through Wal-Mart's stores in search of the DVD player that has dropped from \$49 to \$28.

Perhaps Wal-Mart might even begin to suffer upward pressure on prices as it struggles to hold down costs. A.T. Kearney, a consultancy, recently examined the perception that Wal-Mart uses its huge size to clobber its suppliers into providing lower prices, but concluded that this is "not a significant source of cost advantage". Indeed, in many cases manufacturers actually make more money selling through Wal-Mart than through other retailers. Wal-Mart is not easy to work for, but some suppliers say the experience has made them leaner and fitter. One of the latest companies to conclude that it would be better off supplying Wal-Mart is Levi Strauss. It has been struggling to boost sales through traditional department stores, but has now produced a range of jeans, called Levi Strauss Signature, for sale through Wal-Mart and other discount stores. Some are selling in Arizona for \$9 a pair. So far, the decision seems to be paying off. This week Levi reported a better-than-expected 9.7% increase in first-quarter sales.

According to A.T. Kearney, Wal-Mart's three-biggest sources of cost advantage are low corporate overheads, the efficiencies of its supply-chain and, above all, its low labour costs. A newly hired "associate", as Wal-Mart calls its employees, could earn as little as \$8 an hour, some 20-30% less than unionised workers at rival supermarkets. Union members might also have benefits, such as health-care insurance.

There are several reasons to suppose that this labour-cost advantage might begin to erode. One is falling costs elsewhere as Wal-Mart squeezes its competition. In February, for instance, unionised grocery-store workers in southern California agreed to wage and benefit reductions following a five-month-long strike. This strike began after local supermarkets proposed to cut wages and benefits in preparation for Wal-Mart's entry into the market.

A second reason might be slowing staff turnover at Wal-Mart itself, as the firm struggles to renew its 1.4m-strong workforce. In recent years, staff turnover at Wal-Mart has fallen from over 60% to 44%, close to industry averages. Yet even with a turnover rate of 44%, the firm has to hire an astonishing 600,000 people every year simply to stay at its current size. As the company grows and employs yet more people, that task will become even more difficult, suggesting that Wal-Mart will want to push turnover lower still. That might put pressure on costs, as workers gain tenure, pay rises and better benefits.

Another force working to slow Wal-Mart down is the company's mounting legal and labour-compliance problems. At any moment, Wal-Mart faces about 8,000 lawsuits. The vast majority of these are personal-injury claims from employees. More material, given the sheer numbers of people that Wal-Mart employs, are employee suits seeking class-action status. Among other suits, Wal-Mart's most recent annual report lists 33 putative class-action suits alleging violations of the Fair Labour Standards Act, including forcing employees to work "off the clock" and failing to provide work breaks; eight further putative suits alleging that the firm failed to pay overtime; and a suit that could prove costly alleging discrimination against its female employees. The potential size of this class alone is 1.5m plaintiffs.

## **Cleaning up its act**

An investigation is also continuing into allegations over whether Wal-Mart knew that a subcontractor was using illegal workers. Last year, federal agents raided a number of stores and took documents from the company's headquarters. Wal-Mart has denied doing anything wrong.

In response to a comment by Mr Scott that “my mornings start with reading sales, followed by a visit from our general counsel,” Forrester, a research company, predicted that “Wal-Mart will spend more legal energy than other retailers as it battles a barrage of lawsuits and struggles to not get distracted by any more legal issues in 2004.” The company is recruiting more legal help: in January, it hired Tom Gean, a former United States attorney, to work with its “operation compliance groups”, which have been set up to assist store managers keep within laws and regulations.

That points to a broader worry for the company: that its cherished entrepreneurial culture might become choked by expanding human-resources, public relations and legal departments. Wal-Mart has fought hard to preserve its entrepreneurial culture, which pushes responsibility out to the company's powerful store managers and endeavours to check central, bureaucratic growth. But being big makes companies a magnet for social issues. And freedom among the firm's store managers to set policies which they think will make their outlets as profitable as possible also provides room for abuse.

With so many eyes watching it, Wal-Mart may have decided that it has to sacrifice a bit of its entrepreneurialism to reduce its legal risks. It recently set up a “reputation taskforce”, introduced new personnel procedures, hired extra lobbyists in Washington, DC, created an “office of diversity”, and launched new public-relations and advertising initiatives, dubbed “good jobs” and “good works”, featuring lots of beaming associates. These are not the actions of a company intending to get smaller. Wal-Mart, already huge, is preparing to get a whole lot bigger.