

Walmart Business Model Study

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Abstract---This report explores the features and the role of business model of Walmart in creating and capturing value. A successful business model always links to its strategy, internal and external environment, technologies, management and value chain. The first part of this report introduces Walmart's mission, strategy and its history. The second part analyses Walmart's business model using Nine Building Blocks. The third part critically discusses the validity of the Walmart's business model. According to the analysis of the business model, the fourth and fifth parts address the low cost strategy and how Walmart innovates the business model to achieve its mission. This report concludes that the Walmart's business model is a successful one, but also needs to continuously innovate and develop the research on limitations.

1. Introduction

"Saving people money so they can have a better life" Walmart's mission on which its business model is based on. The current President and Chief Executive officer of Walmart; Michael Duke stated that the company is well positioned in today's difficult economy and tomorrow's changing world (WM Annual Report, 2008). With \$405 billion in revenues net sale (WMAR, 2010), Walmart is said to be World largest retailer in the world and the largest employer in the US (Basker, 2007). 2 million associates in more than 8,400 stores around the world Walmart's serve more than 200 million customers and members each week. Walmart has grown in the US market because it connects itself symbolically to the dominant ideologies of American life. As a matter of approach, Walmart chains are assumed to focus on sales and margins in the short run. Indeed its Everyday Low Pricing format has catapulted it into the leading grocery chain in the U.S and International that was very successful (Jones, 2004).

1.2. History

Walmart is an American public corporation that runs a chain of large discount department stores and warehouse stores that operates in various formats around the world. It was found in 1962 by Sam Walton Headquartered in Bentonville, Arkansas. From the beginning Sam Walton's guiding philosophy for his stores was to offer consumers a wide selection of goods at a discounted price. The strategy of the company was locating stores in small towns where residents had few options for retail shopping. Walmart's success in

small towns led to criticism that the stores took business away from small, hometown merchants (Magretta, 2002).

When Walton died in 1992, the adjustment to a post-Sam environment proved difficult. Even though Walmart executives had emphasized for years that their company depended on a set of principles and habits more than it did on any one person, Walton's death wound up marking a fateful shift in how the company was perceived. Between 1997 and 2001, the company's stock value increased by over 500 percent, rising by 70 percent in 1997 alone. This undoubtedly helped to mollify employees who'd been unhappy with the slump earlier in the decade. (Frank, 2006)

1.2 Walmart today

Today, with \$288 billion in annual revenues (more than Switzerland's GDP) and over \$10 billion in profits, Walmart is the world's largest corporation, according to 2005 Fortune 500 list. It operates over 5,000 stores worldwide and employs over 1.6 million people" (Frank, 2006)

Walmart USA alone has more than 4,300 stores employing more than 1.4 million associates including Walmart Discount Stores, Walmart Supercenters, Walmart Neighborhood Markets and Market side. In 2004 Walmart handled 8.8% of U.S retail sales and the number has since been increased. Meanwhile Walmart International is consist of more than 4,000 stores and 800,000 employees in 14 different countries (Basker, 2007)

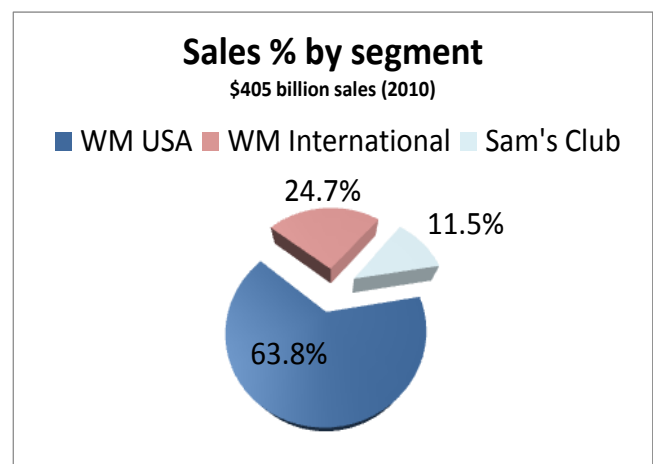


Figure 1. Net sales in 2010 were a record \$405 billion. (Walmart Annual Report, 2010)

2. Walmart's Business Model

"A business model describes the rationale of how an organization delivers, captures and creates value"(Osterwalder & Pigneur, 2010:3). Although Johnson *et al.*(2008) considers only four key elements of the business model, the analysis of Walmart's Business Model will follow Osterwalder and Pigneur's (2010) Nine Building Blocks.

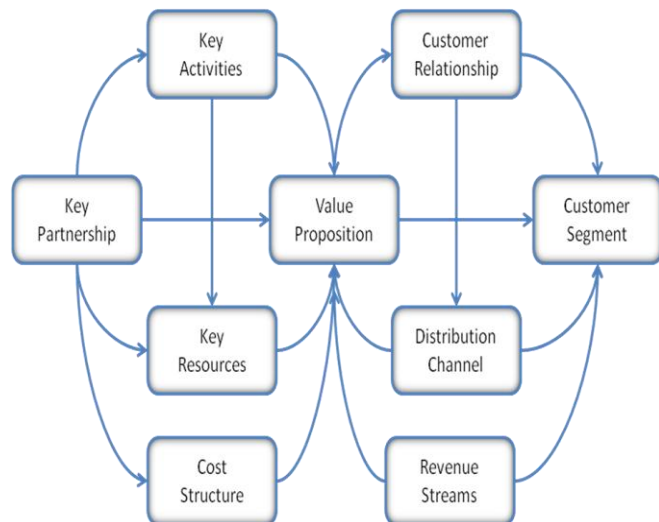


Figure 2: Osterwalder's 9 point decomposition of a Business Model (Chesbrough, 2010)

Value proposition

Walmart's value proposition is based on offering Everyday Low Price (EDLP). This is the core of Walmart's Business Model, and the rest of the key features of Walmart's Business Model are aligned to keep the everyday low price.

This proposition implies that the customers do not need to wait for sales to have the best deal possible (Manning *et al.*, 1998). Besides, not only the sells convenience is associated by providing the wide range of products and services to choose from, but also with one-stop is possible to make all the shopping needed, from groceries to pharmacy (Basker, 2007). Walmart' customers save time and money.

Distribution channel

To deliver its value proposition Walmart communicates with and reaches its customer segments with its distribution channels which are owned and direct, and brings higher margin. Walmart also is corresponding with its customers mainly through mass media and other ways which have a low cost, such as internet.

Customer relationships & Customer segment

Walmart establishes a customer relationship is based on self-service and automated and towards co-creation of some products once it is possible. Walmart tends to reach to the mass market toward mass customisation. Walmart's customers can be divided into three groups: "brand aspirations", people with low incomes who are obsessed with brand; "price-sensitive effluents" wealthier shoppers who love deals; and finally "value-price shoppers" who like low prices and cannot afford much more (Barbaro, 2007).

Key activities

The key activities which are needed to run Walmart's business model are:

- Purchasing goods
- Their delivery
- Total cost control

Other activities would be to create products that will cover needs of a specific customer segment and to control the brand, which has been developing lately.

Walmart's technological edge is in its inventory control, logistics, and distribution (Basker, 2007). The ability to move products place to place quickly and efficiently keeps the costs down as well as the time system in combination with logistics force permits Walmart to have accurate time information of the products in the stores shelves that allows restocking automatically (Tierney, 2004). In addition the logistics involves the suppliers and workforce of 85000 employees, 147 far reaching distribution centers, transportation offices, more than 100.000 tractors and trailers and 8.000 drivers (Walmart logistics facts sheet).

Key resources

The key resources of Walmart classified in 3 categories. First, the physical resources which are owned by it like stores and logistics. Second its human resources, experienced managers and stores managers, and finally the company culture. Walmart culture is based on restless effort at constant self-improvement, discipline and loyalty (Fishman, 2006).

Key partnership

Key partnership is a strong buyer-supplier relationship in which suppliers were considered as close partners of Walmart. They also are part of the value chain of each other and it provides suppliers the chance of accessing to a large market. However it made suppliers, who wish to take advantages of its broad market, to keep their prices and costs low and therefore, suppliers give the control of their own business and negotiation advantage to Walmart (Parnell and Lester, 2008). Walmart also creates economies of scale that optimizes its cost structure.

Revenue stream

Walmart Revenue Streams that generated from its customer segments are basically come from retail sale, such as music downloading with fixed menu pricing. Walmart also drive revenue from selling its own brand, produces by others to cover a segment not cover by other suppliers. Moreover, it takes advantage of selling goods before paying to its suppliers.

Cost structure

The Cost structure is cost-driven model since it is focused on minimizing costs wherever it is possible and it is characterized by economies of scale. The expansion of Walmart allowed it to benefit from economies of scale and reducing its cost besides its technology let it to grow and caused to lower its costs; hence, economies of scale at both the chain levels and stores strengthen Walmart's advantage, rather than being its root cause (Basker, 2007). Walmart's financial discipline is well known as well as their tendency to pass operating costs to suppliers.

3. Validity of Walmart's Business Model

Walmart's wholesaler Business Model is based on cost leadership business strategy (Johnson, Scholes, and Whittington, 2010). Using Chesbrough's business model framework classification (Chesbrough, 2007), Walmart's Business Model is an adapt platform. The company is committed to experimentation, and its key suppliers have become business partners, sharing the technical and business risks, integrated into the planning processes of the company. This type of business model is a valid one, very profitable. Walmart's Business Model is a role model (Baden – Fuller and Morgan, 2010) a model to be copied but on the other hand, is hard to imitate since it has constantly adjusted and improved their processes over time.

Although its size and economies of scale is a competitive advantage, there is a downturn on the way it does business. Consumers have expressed concerns about the so called "Walmart effect", the high cost of low prices (Fisherman, 2006; Basker, 2007).

Firstly, Walmart eliminates local competition creating a monopoly effect. There is a lot of discussion on the press and academics (Basker (2007) comply the main discussion) about Walmart's effects on the communities where stores are settled. Normally, the effects can be summarized in reduction of local competitors, which implies reduction of local jobs. Walmart job creation is not always sufficient to cover the jobs lost (Basker, 2007; Fisherman, 2006).

In relation with its suppliers, it comes to a point that no more efficiency can be done. Eventually, the only way to reduce costs is to manufacture products outside the USA, to countries with lower labour costs and with fewer regulations, specially labour and environmental, which means Walmart's suppliers can be less social responsible than Walmart. Walmart's responsibility in the globalization and the US's flatness economy is perceived by the consumers (Fisherman, 2006, Basker, 2007). These have been current concerns for Walmart while developing its CSR strategy during the last five years.

On the other hand, Walmart's cost control means that nothing can be expended on other services that adds value to the customer experience. While Tesco centers itself in improving the customer experience (The secret of Tesco's expansion success), Walmart almost only does in improving effectiveness.

Walmart has identified correctly the customers segment to which deliver its value proposition. However, this is not appropriate in every market. And Walmart can only approach the segment that it is already serving. Walmart has been so successful in offering itself as a discount retailer that nobody expects premium products – if there are, the suppliers branding suffers (Fisherman, 2006). Also, other competitors are taking advantage on the inability to adapt to different segments (Fisherman, 2006)

Another negative aspect of Walmart cost control is the relationship with its employees, associates. Cost control with

the core value around which Walmart has been built, hard work, implies that associates and even managers work too many hours, applying sometimes illegal practices (e. g. closing the associates inside the stores, women discrimination etc.) (Fisherman, 2006). Walmart's is against unions, since union workers' salary are higher than non-union employees.

4. The future of Walmart's Business Model

4.1 The main fine tuned objectives: Customer focus

Walmart's success is based on its business model which focused on satisfying its customer needs with low price products. However, due to the environmental changes and some factors of the business model that can be easily imitated by its competitors, Walmart has to continuously modify its competitive strategy and to develop its business model to maintain its competitive advantage in the global market. David Glass, Director and former CEO of Walmart Stores, Inc., said, *"We have made it to where we are today by appreciating and satisfying our customers and associates, they are the people who make the difference. Walmart focuses not only on its customers' needs, but also encourages participatory involvement of its employees. Furthermore, its information technology strategy involves a sophisticated data managing"* (John, F. Kennedy, 2005). Randy Mott, former Senior Vice President and Chief Information Officer explained, *"Our investment in data mining is part of Walmart's drive to deliver what its customers want: the right item, at the right store, at the right time and at the right price."* (John, F. Kennedy, 2005)

In order to achieve the objectives of satisfying customers, enhancing shareholder value and creating the profits, Walmart has three important priorities: growth, leverage and returns.

Walmart is continuing to grow around the world through a number of opportunities from opening new stores, entering in new markets, making acquisitions, integrate online channels, and develop new, innovative formats to provide customers to experience the Walmart brands.

Based on the three important priorities, Walmart keeps on improving the supply chain predictability and visibility to affect greatly the amount of inventory safety stock that a retailer must maintain in its network. Walmart not only focuses on the tactical efforts to lower costs and improve gross margin, but has looked into the impact of reducing inventory and storage or handling costs associated with excess safety stock. Currently Walmart maintains just under less 40 days of inventory on hand throughout its massive network (Kinshuk Jerath 2008). With one day reduction in inventory, Walmart can create approximately \$1.7 billion of additional cash flow from operations, which is a mean of low cost, and achieve generate profitable revenue (Kinshuk Jerath 2008).

4.2 Walmart's strategy and its business model innovations

This section provides some ideas for how to innovate Walmart business model further.

Low cost strategy

The core strategy of Walmart is "Everyday Low Prices" as its slogan states, in which the undercutting of prices is the basic principle of Walmart's business, which means low price products for customers. In order to achieve the strategy, innovation in Walmart can generate an assessment of its current business model and find an appropriate way to develop or change (Drucker, 1994).

Information technology innovation

Walmart utilizes information and communications technology in order to aid in the decision-making process and advanced the effectiveness on the response to consumers, as well as through the information technology to control the process of logistic (Chesbrough, 2003). Technology innovation of Walmart's business model involves process and service technology innovation, both of which can reduce the operation cost and time. Also the price of products can be reduced through the process of delivery and storage using new technology. And customer service within new technology will add more value in the same price and create a positive image for customers.

In order to keep track of its logistics Walmart tries more and more to rely on so-called radio frequency identification (RFID) technology (Wailgum, 2008). This technology uses a system to communicate through electromagnetic waves in order to exchange data between a terminal and the electronic tag which is attached to the delivery box. The purpose of this is their identification and tracking. Some of these tags can be recognized from a few metres away others from even greater distances.

Human resource management innovation

Based on new ideas of relationship of its employees within the organization, Walmart develops its human resources policy to adapt the changing environment. All of the employees of Walmart from top manager down to the clerks are called "associates", in which everyone receives a great autonomy and continuously keep communicating according to their performance within the company and about the operations of the stores (Demense, R. & Gardner, N. 2002). This relationship and Walmart's efficient incentives provide a strong safeguard for achieving its strategy. The recruitment of people with the proper skills, competence and working experience can influence the morale of all employees.

The problem with motivation as well as the remuneration of Walmart associates has been given a lot of coverage in the news in recent years. These articles complain about low wages and sparse benefits for the ordinary workers (Luce, 2005). Therefore, financial incentives and other forms of motivations must be constantly evaluated and adapted to ensure the satisfaction of the associates.

Organization and management styles

The management of Walmart has been based upon the values and principles of the founder. The managers always keep in touch with their customers as well as the operations on the retail stores, which leads to an effective communication between each store and the company's headquarters (Sims,

2002). Walmart puts a lot of effort on the innovation and development of its organization and management.

Suppliers relationship development

In order to achieve the objective of low price, Walmart used to adopt the centralization purchase, in which all the transactions took place at the headquarters of Walmart. Furthermore, Walmart also refused to negotiate with manufacturers from the year 1992 and only allowed them to supply no more than 2.5% to avoid the dependence on a manufacture (Raflamme, 2009). However, in order to compete in the global market, Walmart also needs to establish closer cooperative transactions with its local suppliers, which aligns with the needs of its consumers and lowers the inventory cost. Moreover, since 2008 Walmart (and its subsidiary Sam's Club) also requires its suppliers to attach RFID technology to their deliveries. Otherwise these suppliers can face tough fines of up to 2-3 US\$ per delivery (Wailgum, 2008).

Distribution and storage

The cost of distribution and storage is a big part of the product's selling price. Thus, Walmart handles 80% of the purchases that are directly shipped in the warehouse in order to reduce the cost of logistics. However Walmart is still continuously upgrading and innovating its process and system of distribution where the products that arrive via the inbound trucks are loaded and unloaded on outbound trucks without sitting first in the inventory of the warehouse.

Social responsibility and sustainability

Dealing with the imitation of low cost business model by competitors in the context of a global market, Walmart needs the innovation of technology, organizational management, relationship with suppliers and distribution services. Furthermore, Walmart's objective to establish itself as a key player in the society must incorporate cost innovation capabilities and social responsibility into their future business model which looks promising as indicating ways to sustainability (Zott & Amit 2007).

During the last years Walmart has therefore tried to rebrand itself as a pioneer in environmental sustainability. By 2011 they want to reduce the phosphates in detergents by 70 percent and the amount of packaging material by 5 percent until 2013. They have classified their involvement into five categories: sustainability, feedback to communities, care for the children, support for education, and disaster relief. For the last 13 years these employees have spent more than 180,000 in "voluntary" work for "public interests" in their communities (Walmart Social Responsibility Report, 2010).

5. Conclusions

Walmart's core competitive advantage is that delivers the lowest possible price and its business strategy is aligned with this advantage, based on cost leadership (Johnson, Scholes, and Whittington, 2010). Its wholesaler Business Models supports this strategy, all elements focused on using the least

amount possible of resources, always looking into how to improve performance and effectiveness.

As has been exposed previously, Walmart Business Model is an example followed by its competitors. Taking into account its financial results, Walmart's Business Model is a very successful one. However, Walmart effects are not always positive.

On the other hand, Walmart success is based on applying this business model to every activity that undertakes. And experience has proven that this is not always the best approach, for example, when it comes to compete in different markets, such as Germany.

The sustainability of Walmart's Business Model will depend on its ability to adapt within the changing environment, continuously satisfying customers' needs and capturing the biggest value. While doing so Walmart will have to revise its activities and match them with the image of a social corporate responsible business that is developing.

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