

## Equities

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# Wal-Mart Stores Inc (WMT)

## 3Q11 EPS Review: Strong Topline Result; EPS Misses By \$0.01

- **Our Take** — WMT reported 3Q11 EPS from continuing operations of \$0.97 a penny below our estimate and consensus of \$0.98, vs. guidance of \$0.95 to \$1.00, and vs. \$0.89 last year. Worse-than-expected gross margin performance ((-52) bps vs. our (-21) bps estimate) was mostly offset by better-than-expected SG&A (including D&A) leverage and lower interest expense during the quarter. WMT also reported strong SSS results at Walmart U.S. and Sam's Club, as well as +20.3% total sales growth at Walmart International. We believe the strong results at Walmart U.S. demonstrate that the company's initiatives are gaining traction. We reiterate our Buy rating on WMT.
- **3Q11 Total Sales +8.2%** — Total SSS were +1.9 YOY, above our +1.1% est., and vs. (-0.7)% last year. The Walmart U.S. division reported a +1.3% SSS increase (best result in eight quarters and the first positive comp since 1Q09), vs. our +0.5% est. and above guidance of (-1) to 1%. Sam's Club posted a +5.7% increase excl. fuel, above our +4.0% est. and above of the company's +3 to 5% guidance range.
- **GM Contraction and SG&A Leverage** — GM contracted (-52) bps YOY to 24.6% of sales, worse than our estimate for (-21) bps of deterioration. WMT leveraged SG&A (incl. D&A) in 3Q11 by +40 bps to 19.9% of sales, above our estimate for +19 bps of leverage. As a result, WMT's 3Q11 operating margin contracted (-18) bps YOY to 5.4% of sales, slightly below our estimate of (-6) bps.
- **4Q11 and 2011 Guidance** — WMT guided 4Q11 SSS for Walmart U.S. to be 0 to +2% and SSS for Sam's Club to be +4 to 6%. WMT's 4Q11 EPS guidance is \$1.42 to \$1.48, which encompasses current consensus of \$1.45. WMT also narrowed its FY guidance to \$4.45 to \$4.51, vs. \$4.41 to \$4.51 previously.
- **Raising Target Price** — We are raising our target price for WMT to \$69, up from \$63 previously. We arrive at our \$69 target price by using a 14x target forward P/E multiple (vs. 13x prev.) on our 2012 EPS estimate of \$4.99 (vs. \$4.95 prev.).

- Company Update
- Target Price Change
- Estimate Change

<b>Buy</b>	<b>1</b>
Price (15 Nov 11)	US\$57.46
Target price	US\$69.00
	from US\$63.00
Expected share price return	20.1%
Expected dividend yield	2.5%
<b>Expected total return</b>	<b>22.6%</b>
Market Cap	US\$198,044M

### Price Performance (RIC: WMT.N, BB: WMT US)



EPS	Q1	Q2	Q3	Q4	FY	FC Cons
<b>2011A</b>	0.87A	0.97A	0.89A	1.34A	4.07A	4.07A
<b>2012E</b>	<b>0.97A</b>	<b>1.09A</b>	<b>0.97A</b>	<b>1.49E</b>	<b>4.51E</b>	<b>4.50E</b>
Previous	0.97A	1.09A	0.98E	1.46E	4.49E	na
<b>2013E</b>	<b>na</b>	<b>na</b>	<b>na</b>	<b>na</b>	<b>4.99E</b>	<b>4.91E</b>
Previous	na	na	na	na	4.95E	na
<b>2014E</b>	<b>na</b>	<b>na</b>	<b>na</b>	<b>na</b>	<b>5.51E</b>	<b>5.43E</b>
Previous	na	na	na	na	5.46E	na

Source: Company Reports and dataCentral, CIR. FC Cons: First Call Consensus.

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Fiscal year end 31-Jan	2010	2011	2012E	2013E	2014E
<b>Valuation Ratios</b>					
P/E adjusted (x)	15.6	14.1	12.7	11.5	10.4
EV/EBITDA adjusted (x)	7.4	7.2	7.0	6.4	5.9
P/BV (x)	3.1	3.0	2.8	2.5	2.3
Dividend yield (%)	1.9	2.1	2.5	2.9	3.4
<b>Per Share Data (US\$)</b>					
EPS adjusted	3.67	4.07	4.51	4.99	5.51
EPS reported	3.71	4.47	4.51	4.99	5.51
BVPS	18.30	19.07	20.80	23.02	25.27
DPS	1.09	1.21	1.46	1.68	1.93
<b>Profit &amp; Loss (US\$M)</b>					
Net sales	408,085	421,849	450,082	481,423	512,509
Operating expenses	-383,823	-396,307	-423,357	-452,510	-481,331
<b>EBIT</b>	<b>24,262</b>	<b>25,542</b>	<b>26,725</b>	<b>28,913</b>	<b>31,178</b>
Net interest expense	-1,884	-2,004	-2,207	-2,312	-2,336
Non-operating/exceptionals	0	0	0	0	0
<b>Pre-tax profit</b>	<b>22,378</b>	<b>23,538</b>	<b>24,518</b>	<b>26,601</b>	<b>28,842</b>
Tax	-7,626	-8,013	-8,228	-9,044	-9,806
Extraord./Min.Int./Pref.div.	-382	864	-630	-731	-818
<b>Reported net income</b>	<b>14,370</b>	<b>16,389</b>	<b>15,660</b>	<b>16,825</b>	<b>18,218</b>
Adjusted earnings	14,239	14,921	15,663	16,825	18,218
Adjusted EBITDA	31,419	33,183	34,985	37,991	41,099
<b>Growth Rates (%)</b>					
Sales	0.9	3.4	6.7	7.0	6.5
EBIT adjusted	4.6	5.3	4.6	8.2	7.8
EBITDA adjusted	5.0	5.6	5.4	8.6	8.2
EPS adjusted	7.4	10.7	10.9	10.7	10.3
<b>Cash Flow (US\$M)</b>					
<b>Operating cash flow</b>	<b>25,657</b>	<b>24,073</b>	<b>24,208</b>	<b>26,387</b>	<b>28,594</b>
Depreciation/amortization	7,157	7,641	8,260	9,078	9,921
Net working capital	4,316	-1,695	314	514	485
<b>Investing cash flow</b>	<b>-11,620</b>	<b>-12,193</b>	<b>-13,500</b>	<b>-13,500</b>	<b>-13,838</b>
Capital expenditure	-12,184	-12,699	-13,500	-13,500	-13,838
Acquisitions/disposals	0	0	0	0	0
<b>Financing cash flow</b>	<b>-14,191</b>	<b>-12,028</b>	<b>-10,429</b>	<b>-9,303</b>	<b>-10,020</b>
Borrowings	-1,520	7,819	988	1,500	1,500
Dividends paid	-4,217	-4,437	-5,168	-5,803	-6,520
<b>Change in cash</b>	<b>40</b>	<b>-82</b>	<b>278</b>	<b>3,584</b>	<b>4,737</b>
<b>Balance Sheet (US\$M)</b>					
<b>Total assets</b>	<b>170,407</b>	<b>180,663</b>	<b>188,332</b>	<b>198,566</b>	<b>209,384</b>
Cash & cash equivalent	7,907	7,395	7,673	11,257	15,994
Accounts receivable	4,144	5,089	5,430	5,808	6,183
Net fixed assets	102,307	107,878	113,118	117,540	121,457
<b>Total liabilities</b>	<b>97,452</b>	<b>109,008</b>	<b>112,449</b>	<b>116,568</b>	<b>120,596</b>
Accounts payable	30,451	33,557	34,417	35,230	35,968
Total Debt	40,797	48,833	49,752	51,160	52,568
<b>Shareholders' funds</b>	<b>72,955</b>	<b>71,655</b>	<b>75,883</b>	<b>81,998</b>	<b>88,788</b>
<b>Profitability/Solvency Ratios (%)</b>					
EBITDA margin adjusted	7.7	7.9	7.8	7.9	8.0
ROE adjusted	21.0	21.5	22.3	22.5	22.6
ROIC adjusted	15.2	15.2	15.1	15.6	16.3
Net debt to equity	45.1	57.8	55.5	48.7	41.2
Total debt to capital	35.9	40.5	39.6	38.4	37.2










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# Tidbits from WMT's 3Q11 Earnings Call

## Walmart U.S. Category Performance

Grocery, Health & Wellness, and the Hardlines categories delivered the strongest comp results in 3Q11 (up low-single digits). These three categories currently account for approximately 75% of Walmart U.S. revenues. Management noted that its focus on expanding merchandise assortment, improving in-stock levels (above 93% currently), and communicating price throughout the store and the media helped drive results during the quarter. Moderating sequential gas prices during the quarter also benefited topline trends. We provide comp details on the individual categories in the following figure.

Figure 1. Walmart U.S. Category Performance

Segment	Comp	Sequentially Change
Apparel	 (-LSD)	 +170 bps
Entertainment	 (-MSD)	 +160 bps
Grocery	 +LSD	N/A
Hardlines	 +LSD	 +300 bps
Health & Wellness	 +LSD	N/A
Home	 (-LSD)	N/A

Source: Company Reports; Citi Investment Research and Analysis

- **Apparel.** Apparel was down (-LSD), which was a +170 bps improvement from 2Q11. The category benefitted from WMT's assortment initiatives especially in its shoe department. In addition, colder than average temperatures in October drove cold weather apparel sales.
- **Entertainment.** Although comp sales in the entertainment category (which includes electronics and toys) were down (-MSD) YOY, the category improved +160 bps sequentially from 2Q11. Management noted that a strong release schedule during the quarter, drove favorable sales performance in the entertainment category. However, electronics experienced (-MSD) negative comps as the category was negatively impacted by price deflation in key electronic items.
- **Grocery.** Grocery comps were up +LSD. Walmart noted that grocery inflation was approximately +4.0% during the quarter. However, Walmart U.S. did not pass all of the inflation along to the consumer, which limited the impact.
- **Hardlines.** Comps in the hardlines category experienced a +300 bps sequential improvement from 2Q11, and moved into positive +LSD comp sales during the quarter. Heritage categories (sporting goods and stationery and crafts) were the main driver of the improvement as WMT continues to add back space and assortment in these areas.
- **Health & Wellness.** WMT experienced +LSD comps in its health and wellness business, which was driven by the strength of its prescription sales. In addition, the category's over-the-counter business benefitted from improved on-shelf availability. The company continues to benefit from the additional traffic in its pharmacies as a result of the Humana Program. Management expects to see an

increase in conversions from branded prescriptions to generics, as strong brands such as Lipitor become available in generic form.

- **Home.** The company's home category was down (-LSD). Outdoor living, including patio furniture, was the strongest performer, but economic pressure and slow housing sales continue to have a negative impact on discretionary spending.

## Health of the Consumer

- Management believes that the consumer is still struggling. In the company's monthly survey, only one in ten Walmart moms view the state of the U.S. economy as good. Walmart noted that its customers are juggling credit cards, using coupons, and skipping restaurants and vacations. In addition, Walmart's core customer is still negatively impacted by high unemployment, which is leading to declining consumer confidence.
- While gas prices remain higher YOY, which negatively impacts the number of trips customers take, prices have moderated during the quarter. Another positive in the quarter was that the paycheck cycle was less pronounced, which likely had a positive impact on spending.

## Holiday Update

- WMT is focused on winning the Holiday season this year, and plans on communicating its price message as well as its broader assortment in a number of different media outlets. The company has bought a strong share of voice nationally and is also running ads in key individual markets.
- WMT is also offering programs that will make the shopping experience easier for its customers. The company rolled out its Holiday layaway program on October 17, 2011, and is also offering its Christmas Price and Ad Match guarantees throughout the Holiday season. WMT has also rolled out a zero-percent financing offer on Walmart credit cards and is offering free shipping options to help drive additional spending both in-store and online.
- Management noted that the company's Holiday Layaway program has received a lot of positive feedback and layaway transaction volume is exceeding WMT's internal plan. The layaway program is restricted to toys, electronics, and fine jewelry and some of the top products on layaway include LeapPad learning system, Elmo Rocks, bikes, and ride-on vehicles. In electronics, top layaway products are tablets, TVs, and laptops. WMT has incorporated a service fee to reduce layaway cancellations in the fourth quarter.
- For Black Friday, WMT plans on kicking off at 10pm by offering discounts on toys, home, and apparel. The company will then begin offering electronic items at midnight. In addition, the company will have rollback prices throughout the store all day on Black Friday.

## 3Q11 Earnings Wrap-Up

**WMT reported 3Q11 EPS from continuing operations of \$0.97, a penny below our estimate and consensus of \$0.98, vs. guidance of \$0.95 to \$1.00, and vs. \$0.89 last year.** Worse-than-expected gross margin performance ((-52) bps vs. our (-21) bps estimate) was mostly offset by better-than-expected SG&A (including D&A) leverage (+40 bps vs. our estimate for +19 bps of leverage) and lower interest expense (\$535M vs. our \$604.9M estimate) during the quarter. *Income statement highlights are included below:*

Figure 2. WMT – Income Statement Highlights

	Our Estimate (3Q11E)	Actual (3Q11A)	Last Year (3Q10A)	Comments
<b>Total Same-Store Sales</b>	1.1%	1.9%	(-0.7)%	<ul style="list-style-type: none"> <li>The increase in sales was driven by Walmart U.S., Walmart International, and Sam's Club and included a currency exchange rate benefit of \$1.3 Bn.</li> </ul>
<b>Walmart U.S. SSS</b>	0.5%	1.3%	(-1.3)%	<ul style="list-style-type: none"> <li>SSS were better than WMT's (-1) to 1% guidance range. Higher average ticket, more than offset slower traffic YOY. Although traffic was lower YOY, it improved sequentially by +160 bps. While grocery inflation was approximately +4.0%, the total box only experienced +70 bps of inflation as consumers traded down to lower price point items and smaller pack sizes, and the company focused on initiatives to widen the price gap with its competition.</li> </ul>
<b>Sam's Club SSS</b>	4.0%	5.7%	2.4%	<ul style="list-style-type: none"> <li>SSS results were above guidance of +3 to 5%. Comparable ticket, exclud. fuel, increased for both Business and Advantage members in 3Q11. Comp traffic increased +2.3%, while comp ticket increased by +3.4% during the quarter. Sam's Club experienced an approximately +325 to 375 bps benefit from inflation during the quarter.</li> </ul>
<b>Gross Margin</b>	24.8%	24.6%	25.0%	<ul style="list-style-type: none"> <li>Inventories increased +7.5% vs. a total sales increase of +8.2%.</li> <li>Gross margin contracted (-52) bps YOY, worse than our (-21) bps estimate. In addition, gross margin declined in all three business segments. We believe the decline was driven by the significant price investments that WMT is making to drive traffic and price leadership in the mind of its customers.</li> </ul>
<b>SG&amp;A Ratio (Incl. D&amp;A)</b>	20.0%	19.9%	20.2%	<ul style="list-style-type: none"> <li>WMT leveraged SG&amp;A (incl. D&amp;A) by +40 bps, above our +19 bps estimate. The company was able to leverage expenses due to ongoing productivity initiatives, including associate labor management. The company's workforce management program and backroom receiving initiatives helped drive the expense leverage for the quarter.</li> </ul>
<b>EBIT Margin</b>	5.5%	5.4%	5.5%	<ul style="list-style-type: none"> <li>EBIT margin deteriorated (-18) bps YOY, slightly below our expectation for (-6) bps of contraction.</li> </ul>
<b>Net Interest Expense</b>	\$604.9 M	\$535 M	\$516 M	<ul style="list-style-type: none"> <li>Net interest expense increased +3.7% during the quarter. The lower-than-expected result was due to tax-related interest accruals.</li> </ul>
<b>Effective Tax Rate</b>	34.0%	34.5%	33.3%	
<b>Diluted Share Count</b>	3,460.8 M	3,458.0 M	3,631 M	<ul style="list-style-type: none"> <li>In 3Q11, WMT repurchased roughly 27 M shares for \$1.4 B (vs. our \$1.5 B estimate).</li> </ul>
<b>Diluted EPS From Cont. Ops.</b>	\$0.98	\$0.97	\$0.89	<ul style="list-style-type: none"> <li>Below consensus of \$0.98 and in-line with guidance of \$0.95 to \$1.00 per share.</li> </ul>

Source: Company Reports and Citi Investment Research and Analysis

## 3Q11 Segment Results

We have provided details on Wal-Mart's results by division below.

### Walmart U.S.

- **SSS:** SSS increased +1.3%, better than our +0.5% estimate, above guidance of (-1) to 1%, and vs. (-1.3)% last year. This was the best comp for Walmart U.S. in eight quarters, and the first positive SSS result since 1Q09. In 3Q11, the comp was driven by growth in average ticket as overall comp traffic was negative for the third quarter. However, traffic trends improved sequentially during 3Q11 and overall Walmart U.S. comp traffic improved +160 bps sequentially over the second quarter, with October traffic relatively flat. Although inflation was +4.0% during the quarter, the benefit was offset by consumers trading down to lower price points and smaller pack sizes, as well as Walmart's new price investments. For the total box, inflation was +70 bps.
- **Gross Margin:** In 3Q11, the gross margin rate was down (-22) bps YOY at Walmart U.S. The company noted that it began its price investments in 3Q11, which had a negative impact on gross margin. In addition, cost increases in a number of categories were not passed on to its customers.
- **SG&A:** Walmart U.S. leveraged operating expenses by approximately +70 bps during 3Q11. The company's on-going productivity initiatives continue to generate savings. In addition, WMT's workforce management programs are helping improve efficiencies in associate labor scheduling, while initiatives in backroom receiving is also helping to reduce expenses.
- **EBIT:** Walmart U.S. operating income grew faster than sales during the quarter. Operating income rose +5.1% YOY to approx. \$4.6B (vs. +2.7% sales growth).
- **Inventory:** Inventory increased +5.1% YOY, an acceleration of +30 basis points from the second quarter. Productivity gains offset inventory growth that was primarily driven by inflation, the implementation of its new layaway program, and the assortment add-back initiative. Overall, management believes that WMT's inventory is in good shape as it heads into the Holiday season.

### Sam's Club

- **Sales:** Net sales for Sam's Club, excluding fuel, grew to \$11.8 billion, an increase of +6.2% YOY. Comp club sales increased +5.7%, above our 4.0% estimate and above management's guidance of +3 to 5%. The quality of Sam's Club's sales growth was strong despite a headwind of approximately (-100) bps from tobacco sales. The segment anticipates tobacco being a headwind for the rest of the year as Sam's Club is cycling difficult compares in the tobacco category due to strong sales in this category last year from pre-buys and changes in Sam's Club's credit card rewards program. Comparable ticket, excluding fuel, increased for both Business and Advantage members in 3Q11. Comp traffic increased +2.3%, while comp ticket increased by +3.4% during the quarter. In addition, Sam's Club benefitted from inflation, which management noted was in the +325 to 375 bps range during the quarter. Despite inflation, units sold increased YOY.
- **Regions:** Sam's Club experienced strong results across all three geographic operating divisions. The West experienced the strongest sales.

- **Category Performance:** Comp increases were strong across fresh foods, grocery, pet, home, health and wellness, and apparel. Despite average selling price deflation, the consumer electronic business experienced LSD comp sales increases. However, laundry and home care comp sales were down YOY, as the categories were negatively impacted by deflation. In addition, baby care was down, due to the difficult competitive environment.
- **Membership Revenue:** Membership and other income decreased (-13) bps YOY in 3Q11. The decline in other income was due to lost rental income when Sam's Club shifted its wireless business in-house. The company is encouraged by the results and believes that the strategy will be a positive to its operating results.
- **Fuel:** Sam's Club's fuel business remained strong in 3Q11. Fuel prices were up approximately +34% YOY, and gallons sold increased +11%. In addition, the fuel business is pumping more gallons of fuel and generating more sales dollars per gallon this year vs. last year. Management believes that fuel price is an important first price impression for its members and has been a great traffic driver.
- **Gross Margin:** The gross margin rate at Sam's Club decreased (-28) bps YOY. Inflation had a negative impact on gross margin during the quarter along with the highly competitive retail environment.
- **SG&A:** Sam's Club, excluding fuel, leveraged operating expenses by +31 basis points. For the quarter, sales per labor hour increased +2.1% but units per labor hour decreased +1.5 bps.
- **EBIT:** Sam's Club's EBIT income was \$390 million, a +6.3% increase YOY.
- **Inventory:** Sam's Club inventory, including fuel, was up +1.0% YOY. Management is pleased with its inventory levels in its clubs and distribution centers.





















## International

- **Sales:** Walmart International grew third quarter net sales by +20.3% YOY. Changes in currency rates increased net sales by \$1.3B. On a constant currency basis, Walmart International net sales were up +15.3% YOY for the third quarter.
- **Strongest Countries:** All countries experienced sales increases. China, Mexico, and Argentina provided the strongest net sales growth during the quarter.
- **Gross Margin:** Gross margin declined (-57) bps YOY.
- **SG&A:** Walmart International's operating expenses grew slower than sales at +12.4% in 3Q11. Chile, Japan, and the U.K. had expense leverage during the quarter.
- **EBIT:** Walmart International EBIT margins were 4.3%, down (-23) bps YOY.
- **Inventory:** Inventory grew at +11.9%, faster than the company's target. In most cases, WMT's days payable exceeded the company's days on hand. The company's goal remains to grow inventory at or less than half the rate of sales growth.

## Segment Traffic and Ticket Results

In the following chart we summarize the traffic and ticket trends of each of WMT's reporting segments.

Figure 3. WMT 3Q11 Traffic and Ticket Trends

Segment	Traffic	Ticket
Walmart U.S.	 <b>Negative</b>	 <b>Positive</b>
Sam's Club	 <b>2.3%</b>	 <b>3.4%</b>
Walmart International (Estimate)	 <b>Negative</b>	 <b>Positive</b>
U.K	 <b>(-1.3)%</b>	 <b>2.6%</b>
Walmex	 <b>(-0.4)%</b>	 <b>3.4%</b>
Brazil	 <b>Negative</b>	 <b>(-0.8)%</b>
Canada	 <b>(-1.3)%</b>	 <b>2.2%</b>
Japan	 <b>0.4%</b>	 <b>1.5%</b>
China	 <b>(-7.1)%</b>	 <b>14.1%</b>
<b>Total Company</b>	 <b>Negative</b>	 <b>Positive</b>

Source: Company Reports; Citi Investment Research and Analysis

# Earnings Outlook

## 4Q11 Earnings Outlook

**We are raising our 4Q11 EPS estimate to \$1.49 per diluted share, up from \$1.46 previously.** Our estimate is above WMT's guidance range of \$1.42 to \$1.48, above current consensus of \$1.45, and vs. \$1.34 last year. We expect total SSS of +2.7% (vs. +1.3% previously), gross margin contraction of (-55) bps (vs. (-40) bps previously), and SG&A (incl. D&A) leverage of +54 bps (vs. +29 bps previously). Our estimate is based on the following assumptions:

Figure 4. WMT – 4Q11 EPS Outlook

	Our Estimate (4Q11E)	Last Year (4Q10A)	Management Guidance	Comments
<b>Total SSS</b>	+2.7%	(-1.1)%	—	<ul style="list-style-type: none"> <li>WMT began including Massmart in its consolidated results in 3Q11. We estimate Massmart will increase WMT International sales by \$1.9B in 4Q11.</li> </ul>
<b>Walmart U.S. SSS</b>	+2.1%	(-1.8)%	0 to 2%	<ul style="list-style-type: none"> <li>Our estimate is slightly above management's guidance range.</li> <li>We expect SSS for Walmart U.S. to be negatively impacted by the overall economic environment, especially high unemployment among its core customer.</li> <li>4Q11 SSS drivers include: 1) Grocery inflation; 2) Traction from the Humana Program (Rx sales); 3) Improvements in apparel as the company continues to focus on its more basic offering; 4) Increased marketing for the Holiday season; 5) Increased price investments; 6) Improved traffic trends as the broader assortment initiatives continue to gain traction; and 7) the Holiday layaway program.</li> </ul>
<b>Sam's Club SSS</b>	+6.0%	2.7%	+4 to 6%	<ul style="list-style-type: none"> <li>Our estimate is at the high-end of management's guidance range.</li> <li>WMT expects Sam's Club's strong sales momentum to continue across grocery, home, and apparel. In addition, we believe the company will drive growth in consumer electronics, specifically, tablet sales. We also expect Sam's Club's price investments to drive increased traffic. However, Sam's Club is cycling difficult compares in the tobacco category due to strong sales in this category LY from pre-buys and changes in Sam's Club's credit card rewards program. As such, tobacco is expected to be a headwind for the remainder of 2011.</li> </ul>
<b>Gross Margin</b>	23.9%	24.6%	—	<ul style="list-style-type: none"> <li>We forecast (-55) bps of gross margin contraction. The company's focus on widening the price gap with its competition will have a negative impact on GM. In addition, GM results will be impacted by higher inventory associated with Walmart's International business, strong gasoline sales at Sam's Club, and possibly inflation (the company noted that it is not fully passing cost increases through to the consumer).</li> </ul>
<b>SG&amp;A Ratio (Incl. D&amp;A)</b>	17.7%	18.3%	Leverage	<ul style="list-style-type: none"> <li>We forecast +54 bps of SG&amp;A leverage due to continued improvements in labor productivity, including workforce management programs.</li> </ul>
<b>EBIT Margin</b>	6.9%	6.9%	—	<ul style="list-style-type: none"> <li>We forecast EBIT margins to contract (-6) bps YOY.</li> </ul>
<b>Net Interest Expense</b>	\$575.6 M	\$532 M	—	<ul style="list-style-type: none"> <li>Reflects \$5 Bn of long-term debt issued in 1Q11.</li> </ul>
<b>Effective Tax Rate</b>	34.0%	34.0%	Low-end of 33.5 to 34.5% Guidance in 2011	<ul style="list-style-type: none"> <li>In-line with guidance.</li> </ul>
<b>Diluted Share Count</b>	3,438.2 M	3,563 M	—	<ul style="list-style-type: none"> <li>We are forecasting \$1.3 Bn in share repurchases in 4Q11. As of 3Q11-end, WMT had approx. \$12.7 Bn remaining in its \$15 Bn share repurchase authorization, which was announced on June 3, 2011.</li> </ul>
<b>Diluted EPS</b>	\$1.49	\$1.34	\$1.42 to \$1.48	<ul style="list-style-type: none"> <li>Our estimate is above consensus of \$1.45 per diluted share.</li> </ul>

Source: Company Reports and Citi Investment Research and Analysis

## 2011 Earnings Outlook

**We are raising our 2011 EPS estimate to \$4.51 per diluted share, up from \$4.49 previously.** Our estimate is above consensus of \$4.50, and vs. \$4.07 per share in 2010. Recall, WMT provided 2011 full-year EPS guidance of \$4.45 to \$4.51 when the company reported 4Q11 results. We expect SSS of +1.2% (vs. +0.6% previously), gross margin contraction of (-36) bps (vs. (-24) bps previously), and SG&A (incl. D&A) leverage of +27 bps (vs. +15 bps previously). Our estimate is based on the following assumptions:

Figure 5. WMT – 2011 EPS Outlook

	Our Estimate (2011E)	Last Year (2010A)	Management Guidance	Comments
Total SSS	+1.2%	(-1.1)%	—	
Walmart U.S. SSS	+0.4%	(-1.6)%	—	<ul style="list-style-type: none"> <li>We expect SSS for Walmart U.S. to be negatively impacted by the overall economic environment, especially high unemployment among its core customer.</li> <li>2011 SSS drivers include: 1) Grocery inflation; 2) Traction from the Humana Program (Rx sales); 3) Improvements in apparel as the company continues to focus on its more basic offering; 4) Increased marketing for the Holiday season; 5) Increased price investments; and 6) Improved traffic trends as the broader assortment initiatives continue to gain traction.</li> </ul>
Sam's Club SSS	+5.2%	+1.7%	—	<ul style="list-style-type: none"> <li>We expect Sam's Club's strong sales momentum to continue across grocery, home, and apparel. In addition, we believe the company will drive growth in consumer electronics, specifically, tablet sales. We also expect Sam's Club's price investments to drive increase traffic. However, Sam's Club is cycling difficult compares in the tobacco category due to strong sales in this category LY from pre-buys and changes in Sam's Club's credit card rewards program. As such, tobacco is expected to be a headwind for the remainder of 2011.</li> </ul>
Gross Margin	24.4%	24.8%	—	<ul style="list-style-type: none"> <li>We forecast (-36) bps of gross margin contraction. The company's focus on widening the price gap with its competition will have a negative impact on GM. In addition, GM results will be impacted by higher inventory associated with Walmart's International business, strong gasoline sales at Sam's Club, and possibly inflation (the company noted that it is not fully passing cost increases through to the consumer).</li> </ul>
SG&A Ratio (Incl. D&A)	19.1%	19.4%	—	<ul style="list-style-type: none"> <li>We forecast +27 bps of SG&amp;A leverage due to continued improvements in labor productivity, including workforce management programs.</li> </ul>
EBIT Margin	6.0%	6.1%	—	<ul style="list-style-type: none"> <li>We forecast (-12) bps of EBIT margin contraction in 2011.</li> </ul>
Net Interest Expense	\$2,206.6 M	\$2,004 M	—	<ul style="list-style-type: none"> <li>We are modeling higher interest expense YOY due to higher total debt levels, partially offset by lower average interest rates.</li> </ul>
Effective Tax Rate	33.6%	34.0%	Low-end of 33.5 to 34.5%	<ul style="list-style-type: none"> <li>In-line with guidance.</li> </ul>
Diluted Share Count	3,473.5 M	3,671 M	—	<ul style="list-style-type: none"> <li>We are forecasting approximately \$6.3Bn in share repurchases in 2011. As of 3Q11-end, WMT had approx. \$12.7 Bn remaining in its \$15 Bn share repurchase authorization, which was announced on June 3, 2011.</li> </ul>
Diluted EPS	\$4.51	\$4.07	\$4.45 to \$4.51	<ul style="list-style-type: none"> <li>Our estimate is at the high-end of WMT's guidance range and above consensus of \$4.50 per diluted share.</li> </ul>
Capital Expenditures	\$13.5 Bn	\$12.7 Bn	\$13.0 to \$14.0 Bn	

Source: Company Reports and Citi Investment Research and Analysis

## 2011-2014 EPS Outlook

We are revising our 2011-2014 EPS estimates as follows. Our assumptions for 2011-2013 are summarized in Figure 4 below.

- **2011 EPS Estimate.** We are raising our 2011 EPS estimate to \$4.51, up from \$4.49 previously. Our quarterly 2011 EPS estimates are as follows:
  - 1Q11A: \$0.97A
  - 2Q11A: \$1.09A
  - 3Q11A: \$0.97A
  - 4Q11E: \$1.49, vs. \$1.46 previously
  - 2011E: \$4.51, vs. \$4.49 previously
- **2012 EPS Estimate.** We are raising our 2012 EPS estimate to \$4.99, up from \$4.95 previously, and vs. consensus of \$4.91 per diluted share.
- **2013 EPS Estimate:** We are raising our 2013 EPS estimate to \$5.51, up from \$5.46 previously, and vs. consensus of \$5.43 per diluted share.
- **2014 EPS Estimate:** We are lowering our 2014 EPS estimate to \$6.09, down from \$6.13 previously, and vs. consensus of \$6.03 per diluted share.

Figure 6. WMT EPS Revisions (Before and After)

Wal-Mart Stores (WMT)	BEFORE			AFTER		
	2011E	2012E	2013E	2011E	2012E	2013E
<b>Sales (% Growth)</b>						
- Growth	6.9%	7.3%	6.4%	6.7%	7.0%	6.5%
- Total Comp Sales	0.6%	1.4%	1.7%	1.2%	1.6%	2.3%
- Walmart U.S. Comp Sales	-0.1%	1.0%	1.5%	0.4%	1.0%	2.0%
- Sam's Club Comp Sales	4.1%	3.0%	2.5%	5.2%	4.5%	3.5%
- Total Square Footage Growth	3.2%	3.7%	4.1%	5.5%	4.3%	4.0%
<b>Margin (bps improvement)</b>						
Gross Margin	(24)	(20)	(15)	(36)	(25)	(20)
SG&A (incl. D&A)	15	27	25	27	35	30
Operating Margin	(12)	4	8	(12)	7	8
<b>Earnings</b>						
<b>Diluted EPS</b>	<b>\$4.49</b>	<b>\$4.95</b>	<b>\$5.46</b>	<b>\$4.51</b>	<b>\$4.99</b>	<b>\$5.51</b>
- Growth	10.5%	10.2%	10.3%	10.9%	10.7%	10.3%
<b>Consensus EPS</b>						
<b>Mean</b>	<b>\$4.50</b>	<b>\$4.91</b>	<b>\$5.43</b>	<b>\$4.50</b>	<b>\$4.91</b>	<b>\$5.43</b>
High	\$4.59	\$5.26	\$6.15	\$4.59	\$5.26	\$6.15
Low	\$4.45	\$4.70	\$4.90	\$4.45	\$4.70	\$4.90
<b>Guidance</b>	\$4.41 to \$4.51	N/A	N/A	\$4.45 to \$4.51	N/A	N/A

Source: Citi Investment Research and Analysis

## Raising Our Target Price to \$69

**We are raising our target price for WMT to \$69, up from \$63 previously.** We arrive at our \$69 target price by using a 14x target forward P/E multiple (vs. 13x prev.) on our 2012 EPS estimate of \$4.99 (vs. \$4.95 prev.). Please refer to the *Valuation & Risks* section for additional details.

## Store Count

As of 3Q11-end, Wal-Mart operated 4,460 domestic stores and 5,366 international locations in 28 countries.

Figure 7. WMT - Store Count

	Beg. Store Count	Opened	Closed	Relocation/ Expansion*	End Store Count	End Sq. Ft. (MM)
Discount Stores	689	0	0	(-42)	647	68.4
Supercenters	2,939	21	0	42	3,002	548.5
Neighborhood Market	183	9	0	0	192	7.7
Supermercado	2	0	0	0	2	0.1
Marketside	4	0	(-4)	0	0	0.0
Super Ahorros*	2	0	0	0	2	0.0
Walmart Express	4	2	0	0	6	0.1
Walmart on Campus*	1	0	0	0	1	0.0
Sam's Club	609	1	0	0	610	81.4
<b>Total U.S. Stores</b>	<b>4,431</b>	<b>33</b>	<b>(-4)</b>	<b>0</b>	<b>4460</b>	<b>706.2</b>
International	5,236	132	(-2)	0	5,366	317.4

Beg. Store Count is as of 7/31/11. End Store Count and Square Footage are as of 10/31/11.

\*Super Ahorros Square footage is 29,765 and Walmart on Campus is 3,371

Source: Company Reports and Citi Investment Research and Analysis

- **3Q11 Summary.** WMT added approximately 8.7 million of new retail square footage and 159 new operating units during the quarter.

## Wal-Mart Stores Inc

### Company description

Wal-Mart Stores, Inc. (WMT), based in Bentonville, AR, opened its first discount store in 1962 and has grown to become the world's largest retailer with 2010 sales topping \$400 billion. In addition to discount stores, WMT operates Supercenters (first opened in 1988 and offer customers a combination of food and general merchandise), the membership-only warehouse club, Sam's Club (first opened in 1983), and Neighborhood Market (first opened in 1998 as a supermarket format). In May 2003, WMT sold McLane Company, a wholesale distributor of consumer packaged goods, to Berkshire Hathaway Inc. WMT's primary business is its Walmart discount stores and Supercenters, which sell merchandise in six primary categories, including 1) grocery, 2) health & wellness, 3) entertainment, electronics, and toys, 4) apparel, shoes, and jewelry, 5) home, and 6) seasonal and hardlines. In 2006, the company revolutionized the market for prescription drugs with its \$4 generic prescription drug program.

In 1992, WMT began its international operations through a JV in Mexico with Cifra S.A. de C.V. After its withdrawal from Germany and South Korea in 2006, WMT's international segment now consists of wholly-owned operations in Argentina, Brazil, Canada, Puerto Rico, and the U.K. and majority-owned subsidiaries in Chile, Costa Rica, El Salvador, Guatemala, Honduras, Japan, Mexico, and Nicaragua. WMT operates in China through a combination of JV's and minority-owned subsidiaries, and the company entered the Indian retail market in 2Q09 through a JV with Bharti.

### Investment strategy

We rate the shares of WMT Buy (1). We expect long-term same-store sales growth to be driven by WMT's strong value proposition and improved in-store execution. In addition, the company should continue to gain market share from the supermarkets in food and consumable categories, given the significant price savings offered by WMT. With lower-income consumers still under financial stress, we believe that WMT's low-price message will resonate well with these consumers. From an earnings perspective, we expect growth to be driven by market share gains and the growth of WMT's international operations, including acquisitions in new markets. Improved inventory management, a new course for WMT's merchandising organization led by Bill Simon (Walmart U.S. CEO), and increased global sourcing should also drive stronger profitability.

### Valuation

We have assigned Wal-Mart Stores a 1 (Buy) rating. We are valuing Wal-Mart using an approx. 14x target forward P/E multiple on our 2012 EPS estimate, which yields a 12-month target price of \$69.

In our P/E valuation analysis, our target multiple of approx. 14x our 2012 EPS estimate is below WMT's ten-year median of approx. 15.5x. Our target multiple reflects multiple expansion from current levels, driven by 1) market share gains in food, and 2) strong growth in WMT's International division, 3) cost savings from improved global sourcing, and 4) opportunity to improve traffic as well as sales performance in the Walmart U.S. division. However, we do not award WMT a higher multiple due to challenging sales growth currently, a more moderate recovery in consumer spending, pressures facing WMT's core lower income consumer, and strong competition in the food retail industry.

## Risks

We believe WMT faces risks based on political risks, stock liquidity, earnings stability, price volatility, and financial strength. Our risk rating also reflects industry and company specific risks.

Risks to the achievement of our target price include: 1) a retrenchment in consumer spending and retail sales; 2) WMT's size may hinder both sales and earnings growth in the future; 3) WMT's core customer is highly sensitive to macroeconomic pressures; 4) the earnings impact of foreign currency exchange rates could be greater or less than expected; and 5) the implementation of new merchandising strategies, carry execution risk.

If the impact on the company from any of these factors proves to be greater/less than we anticipate, it may prevent the stock from achieving our target price or could cause our target price to be materially outperformed.

## Appendix A-1 Analyst Certification

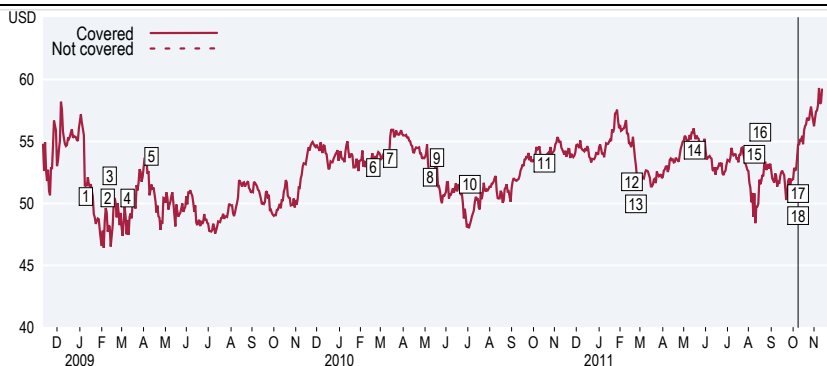
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### Wal-Mart Stores Inc (WMT)

#### Ratings and Target Price History Fundamental Research

Analyst: Deborah L Weinswig



	Date	Rating	Target Price	Closing Price
1	9-Jan-09	1L	*\$65.00	51.58
2	10-Feb-09	1L	*\$60.00	47.72
3	12-Feb-09	1L	*\$53.00	48.13
4	10-Mar-09	*2M	*\$48.00	48.67
5	13-Apr-09	2M	*\$53.00	51.53
6	18-Feb-10	2M	*\$54.00	53.47

\* Indicates change

	Date	Rating	Target Price	Closing Price
7	14-Mar-10	*1M	*\$65.00	53.90
8	9-May-10	1M	*\$63.00	52.40
9	19-May-10	1M	*\$65.00	53.04
10	5-Jul-10	1M	*\$64.00	48.00
11	17-Oct-10	1M	*\$63.00	53.35
12	17-Feb-11	1M	*\$62.00	54.75

	Date	Rating	Target Price	Closing Price
13	23-Feb-11	1M	*\$63.00	53.03
14	17-May-11	1M	*\$70.00	55.54
15	9-Aug-11	1M	*\$66.00	50.82
16	17-Aug-11	1M	*\$63.00	51.55
17	8-Oct-11	Stock rating system changed		
18	8-Oct-11	*1	63.00	53.70

Rating/target price changes above reflect Eastern Standard Time

# Wal-Mart Stores Inc (WMT)

## Ratings and Target Price History

### Best Ideas Research

### Relative Call (3 Month)

Analyst: Deborah L Weinswig



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Deborah L Weinswig; Michael S Palahicky

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