

Strategy Adjustment of Walmart China

LIU Yanrong^{[a],*}

^[a]School of Applied English, Dalian University of Foreign Languages, Dalian, China.

*Corresponding author.

Received 20 September 2013; accepted 2 December 2013

Abstract

With its “Everyday Low Price” strategy (EDLP), Walmart Inc established itself as the global leader in retailing. Again by adopting low price strategy, Walmart expanded its business into international market. However, 16 years after Walmart entered Chinese market, its low price strategy has not achieved its effect and its profit does not match the number of outlets it operates. Therefore, Walmart has to make adjustment to its EDLP strategy in order to survive in this complex and competitive retailing environment of China. This paper intends to illustrate the causes for Walmart’s strategy adjustment and accordingly propose some tactics.

Key words: Walmart China; EDLP; Strategy adjustment

LIU Yanrong (2013). Strategy Adjustment of Walmart China. *Management Science and Engineering*, 7(4), 88-93. Available from: URL: <http://www.cscanada.net/index.php/mse/article/view/j.mse.1913035X20130704.Z012> DOI: <http://dx.doi.org/10.3968/j.mse.1913035X20130704.Z012>

INTRODUCTION

As the largest global retailer, Walmart has 10,130 stores around the world, serving 200 million customers and its associates. Walmart employs 22 million staffs, making itself the biggest private employer on the earth. Due to its powerful influence, Walmart has become a popular research subject in the academic field. It was in 1996 that Walmart decided to move into China’s retailing market. This signalled that the largest global

retailer would do business in the world’s most populous country. In the same way, Walmart aroused the academic interest in Walmart on the part of both Chinese scholars and American scholars. Although Walmart carried out localization strategy in the countries where it operates its business, it is EDLP strategy that Walmart adopts to expand into international market. EDLP is Walmart’s operation philosophy. However, 16 years after Walmart entered China, Walmart’s EDLP strategy is challenged with the complexity and fierce competition of China’s retailing market. In this case, Walmart has to make appropriate adjustment to its strategy.

1. CURRENT SITUATION OF CHINA’S RETAILING MARKET

1.1 Intense Competition and Low Market Concentration Rate

Since 1999, China has maintained an annual economic growth rate of 8% (except for 2012). With the improvement of its people’s living standard, China has a potential consumer market. According to statistics, in 2011 the annual sales of China’s social retail goods reached CNY13000 per capita and for the first time China overtook U.S. in this respect. Besides this, retail sales in China double every five years. As a result of this, every international powerful retailer plans to tap China’s vast retail market. Among those retailers, Walmart, Tesco and Carrefour are the big players, and Japanese and Korean retailers follow on their heels. By contrast, Retailers from Taiwan and Hong Kong become the most successful ones. Over the past years, by learning advanced experience and retailing mode from their foreign counterparts, Chinese retailers have become their strong competitors. And owing to the low entry barrier, Chinese retailers have formed their scale of economy. All these lead to fierce competition at China’s retail market.

Market concentration rate is the measurement index of market structure. It measures the number of firms and the difference of their scale. It is a very important quantified indicator of market power. Market concentration rate is the basic and the most important factor in determining market structure. And it reflects competitiveness of the market and market share firms take up. China's retail market is vast but scattered. No retailer can snatch a huge market share, becoming a leader. According to Kantar World panel (see the table

below), as far as the major retailers in China's market are concerned, in terms of their market share, up to the 3rd quarter of 2012, the five biggest retailers of mainland China occupied only 15% while Walmart, Tesco and Carrefour took up 13.8%. By contrast, in Hong Kong the major retailers accounted for 76% of market share. And even in Southeast Asian countries the percentage ranged from 25 to 33.3. Therefore, although China provides a vast retailing market, it's hard and difficult for any retailers to manage and expand smoothly.

Table 1
The Market Share of Big Retailers (Based on Sales Volume) in China

	Till 9/9/2011 52 weeks roll-on	Till 7/9/2012 52 weeks roll-on	2011 3d quarter	2012 3
RTmart+ Groupe Auchan	8.1	7.9	8.0	7.9
RTmart	6.3	6.3	6.3	6.3
Groupe Auchan	1.8	1.7	1.7	1.6
Walmart China	7.7	7.3	7.8	7.0
Walmart	5.3	6.4	5.3	6.3
Trustmart	2.3	0.8	2.4	0.6
Vanguard Group	6.8	6.8	7.0	6.8
Carrefour	4.9	4.7	4.8	4.8
Bailian Group	4.4	4.0	4.3	4.0
Zhongbai	2.0	2.2	1.8	2.1
Tesco	2.1	2.1	2.0	2.0
Wumart Group	1.9	1.8	2.0	1.8
Wumart	1.1	1.2	1.1	1.3
Merrymart	0.8	0.6	0.8	0.6
Yonghui Supermarket	1.2	1.7	1.2	2.0
Lotte	1.7	1.3	1.7	1.3

Note: Kantar World Panel China Consumer Index

1.2 Scale of Economy Hard to Realize and Homogeneous Operating Mode

Economy of scales refers to the increase in the profits arising from the increase in the size of an operating unit. As retailing industry is characterised by "large sales volume but with low profit margin", retailers have to rely on economy of scales to survive and develop. This is essential to the success of big retailers because retailers can manage their own supply chains once the operation reaches a certain scale. However, the wage and benefits of Chinese workers rising at an annual rate of 15% and 20%, coupled with the skyrocketing price of real estate in recent decade put a squeeze on the profit of retailers and affect the openings of new stores. Besides, Chinese governments at different levels no longer give preferential treatment to foreign retailers. The preferential policies such as low rent, priority for store sites and tax reduction have been cancelled one by one, leading to the rise in the cost of opening stores. In 2012, the number of stores the world's

biggest three retailers, Walmart, Carrefour and Tesco declined by 27% on average.

China's retailing industry has entered the stage of multi-retail formats and rapid regional development. Moreover, chain stores gain the recognition of Chinese customers and have become the shopping destinations. Despite this, both home retailers and foreign retailers make a profit from charging entrance fees and money back offers based on sales rather than operate business on their own. They handle no more than 15% of the deals at the stores. This practice makes retailers reliant on fees and charges for revenue, thus pushing up the price of merchandise. Furthermore, the chain stores delay payment, reducing rotation rate of goods. As retailers adopt the same promotion tools such as discount, coupons & discount, gift certificates, mystery rewards, timed sales, sales promotion, money back on membership card and membership discount, the operation mode is homogeneous.

1.3 Logistics Impeding the Development of Retailing Industry

The function of logistics is to smooth the links in the flow of resources between the point of origin and the point of consumption by managing the transportation, inventory, packaging and distribution of goods, to reduce logistics costs and shorten the dealing time between suppliers and customers. Therefore, logistics, as the third source of revenue, play an important role in improving competitiveness of retailers. However, the network of roads in China is still underdeveloped. According to statistics released by transportation departments in China, in recent decade, the mileage of China's roads and highways has been extended from 1,760,000 km to 4,100,000 km, of which the mileage of highway increased from 25,000 km to 84,000 km, ranking No 2 in the world. Even if highway network is expanding at a fast pace in China, by 2035 China can reach a mileage of 89,000km¹, the same mileage that the U.S. attained in the early 1950. What's more, in China 95% of highway, 61% of the first-grade roads and 42% of the second-grade roads² are toll roads with the support of government policy. This means that a toll is charged for the use of highways in China, which increases the cost of commodity circulation.

Also, due to the restraint of conventional administration system, conditions for developing soft power of logistics industry are inadequate. Logistics market is segmented as a result of barriers such as administration departments, areas and industries. And the market is highly monopolised. So logistics management and uneven distribution of resources prevent the productivity of logistics industry and result in a higher transportation cost. Transportation cost of goods in China is four times as high as that in western countries and logistics accounts for 30% of total cost of goods. All the costs combined constitute a much higher price of goods.

1.4 Low and Uneven Consumption Level and Divergent Consumption Habits

Although China has experienced a rapid economic growth over the past two decades and consumption level has been improved a lot, overall the Chinese consumption level remains low. In 2012, private consumption in China took up only 35.7% of GDP while in the U.S. it accounted for 70%. And according to the report by the Chinese Household Finance Survey Center of Chengdu's Southwestern University of Finance and Economics, the Gini coefficient was 0.61 for 2010³, far greater than the averaged 0.44 coefficient of all countries monitored by the World Bank. This indicated a large income gap

between rich and poor, which is sure to result in an uneven consumption level in China. Based on *2010 China Statistics Annals*, regional annual income ranks as follows: the east averaged CNY 26406.04, the inner land averaged CNY 18323.16, the west averaged CNY 18159.40 and the northeast averaged CNY 18301.31. In terms of political influence and economic power, China just has 5 tier 1 cities, 22 tier 2 cities, and the rest is tier 3 or 4 cities.

Additionally, China has a vast area, the fourth largest country by land mass in the world. But there is a divergence in physical conditions. As China's market economy is not developed, its economy is highly fragmented, with local provinces and municipalities working as independent economic units. They form their own separate markets and there is no free flow of commodities and goods across the regions and the country as a whole. Therefore, consumer goods take on a regional flavour and help develop different consumer habits and consumer behaviour. The well-known eight regional cuisines are a good case in point.

2. PRESENT SITUATION OF WALMART'S BUSINESS OPERATION IN CHINA

Since it opened its first supercenter and the first Sam's club store in Shenzhen, Walmart started to expand its business into China. With its powerful brand name and strong financial support, Walmart opened its stores at an alarming speed. Yet, succumbed to China's adverse and volatile retailing environment, Walmart's EDLP failed to achieve the results it expected in terms of the operational scale and its brand effect.

2.1 Low Business Performance & Ineffective Scale Economies

Walmart has opened 390 outlets in more than 150 cities in China. Yet, this figure cannot be compared with that of 4500 in its home country. Despite dozens of store openings every year, its share of China's supermarket sales has slipped to about 5.5 per cent, according to estimates by the China Market Research Group. Apparently, China has become one of the most difficult markets to manage in the world. Retailing gross profit tends to decline and the increasing rate of sales income is far lower than the increasing rate of sales revenue.

Low sales revenue is attributed to the core competitive edge Walmart failed to realize in China. EDLP strategy Walmart has been implementing at international market cannot be fully employed in China, because Chinese markets are rife with cheap products and open-air markets nearby communities and business centers provide customers with various and low-priced offerings. Additionally, Walmart's efficient logistics system cannot be automatized in support of its EDLP strategy. So Walmart is unable to utilize its advantage of powerful supply chains and its core competitive edge is not applicable to China's retailing market.

¹ Walmart. <http://www.baikewiki.com/wiki/%E6%B2%83%E5%B0%94%E7%8E%9B> (in Chinese)

² ifeng finance 2012-10-01 06:59:03 (in Chinese). http://gongyi.ifeng.com/gundong/detail_2012_09/30/18020818_0.shtml

³ China's Gini Index at 0.61, University Report Says. <http://english.caixin.com/2012-12-10/100470648.html>

2.2 Indistinctive Business Formats

Walmart operates 4 formats in China: Walmart supercenter, Sam's club, Neighborhood Market and Discount Compact Hypermarket (DCH). Except for 2 neighbourhood markets located in Shenzhen, the other 3 business formats are no different from one another in terms of operation mode and variety of goods or products.

According to Walmart's design, Walmart Supercenter is the main format of Walmart China, which provides one-stop shopping experience and a great variety of low-priced products for customers. Sam's Club is a membership store which combines a warehouse and a store together. With thousands of high quality, brand name products from home and abroad, Sam's Club succeeds in saving time and energy for members. Members of Sam's Club can shop in a comfortable environment and enjoy hospitable service of Sam's Club. Neighborhood Markets provides convenient shopping experience for customers living in a large and prosperous community. And DCH format bases in born cities and tier 2 or 3 cities. The business area of DCH is 3000 to 5000 square meters. DCH is more flexible and more welcomed by community, and provides a more convenient shopping experience for low income families.

However, in reality, Walmart supercenters and Sam's club provide homogeneous goods and products, both offering brand name products from home and abroad. The only difference is that Sam's club offers a greater variety of foreign brands than its supercenter markets and they have their own brand name products. At the same time, Walmart supercenters and DCH differ only in operating space and there is little difference in terms of the variety and price.

2.3 Unclear Management Style

As the above-mentioned, since 1996 when Walmart opened its first supercenter and Sam's club in China, so far Walmart has opened more than 390 outlets in more than 150 cities, creating under 100,000 jobs. Despite of this, with its rapid expansion, there are loopholes with Walmart's management system. Walmart has been involved in notorious scandals such as financial scandals, quality scandals and business fraudulence. For example, within 5 years up to September of 2011, Walmart has been sanctioned 20 times due to violation of laws⁴. The worst scandal was the discovery in October of 2011 that ordinary pork was being sold as more expensive organic pork. That led to the arrests of two store managers in Chongqing and the overhaul of Walmart's China management team. Over the last two years, Walmart was embroiled in the scandals of fake brand name clothing, cakes made from expired eggs. All these scandals tarnished Walmart's reputation as a big retailer in China⁵.

⁴ Walmart involved in more scandals & punished 20 times within 5years for violations (in Chinese). <http://news.qq.com/a/20110921/000066.htm>

⁵ Walmart embroiled in egg scandal, Guangzhou senior management

Localization is the strategy international retailers usually adopt. Of course, localization is quite necessary for international retailers to win competition at international markets. Nevertheless, localization strategy puts international retailers at an awkward situation: standardized operation through up-down management or flexible operation through down-up management. When it started its operation in China, Walmart borrowed its American authoritarian management style. With the complexity of retailing environment and unbalanced development of markets in China, this management style delays decision-making, making operation inefficient and losing business opportunities. Although Walmart's headquarter delegated its decision-making to China's stores in 2007, allowing them to choose suppliers and price the products, scandals due to mismanagement rendered the change of management style uncertain.

2.4 Belittled Brand Image and Lacking of Corporate Culture

China's economy has developed for decades and consumer market has been booming. However, regulatory rules and related laws have not been updated, which has led to rampant market malpractices. The main source of retailer's profits doesn't come from the difference between wholesale price and retail price, but from channels fees charged by retailers. All the fees such as entry fees of new products, advertising charges, rewards on sales, promotion fees, display fees and information fees take up half of total revenues as gross profits do. In face of lax legal environment and below business ethics, Walmart forsook the principles upheld in developed business society for the sake of survival and better development. Consequently, Walmart has been embroiled in business scandals such as financial scandal and business frauds. This exerted an adverse impact on Walmart's brand image as the world largest retailer, affecting its brand loyalty and customer retention. After all, China used to be in planned economy and customers trusted the big state-owned enterprises. Thus, Chinese consumers favour brand-name firms like Walmart.

While it adopted EDLP strategy in China, Walmart exported a unique corporate culture and management ideology to its Chinese stores. Walmart's Arkansas headquarters promote a corporate culture as follows: respect for the individual, service to the customer and strive for excellence. At Walmart, staffs are called "associates" rather than "employees". Walmart encourages its employees to participate in store management and shares profits with its staffs by offering them stock options, which highly motivated its staffs. This corporate culture helps Walmart foster a good image as an enterprise and improve its brand effect and brand assets. When it first opened its stores in China, Walmart inherited this

rushed to rescue (in Chinese). <http://315ah.ccn.com.cn/a/news/sjbg/2013/0514/16765.html>

corporate culture. Its associates spiritual outlook and greeting with a smile impressed Chinese customers, providing a total new shopping experience for them, which they could not experience in a Chinese store. Yet, as time goes on, this corporate culture vanished in its management. Employees seldom wear a smile though they greet customers. They never welcome customers with warmth and hospitality. They are seldom seen to help each other and treat each other nicely. And cashier line becomes longer and slower. As the author observes in her hometown, a tier 2 city, Walmart employees have been witnessed to argue or quarrel with customers and even engage in body fights sometimes. Apparently, there is a lack of a corporate culture in the management of its Chinese stores.

3. STRATEGY ADJUSTMENT OF WALMART CHINA

Global economy has been in recession for five years owing to 2008 financial crisis taking place on Wall Street. There is no sign of the world economy stabilizing and recovering. Although retailers sell daily necessities, customers are becoming sensible and sensitive to product price and retail service. With China's complex retail market and unregulated operation environment, along with the competitive local retailers, Walmart has to adjust its EDLP strategy if it wants to develop in a sustainable way and become a leader at China's retail market.

3.1 Retuning Strategic Positioning and Underlining the Differentiation of Business Formats

Not only Chinese retail markets are rife with cheap products, but also problems arise such as fakes, price gouging, adulterated foods due to unregulated market. China has a trading-up retail market where new rich and middle class are not interested in low priced goods and insensitive to price. Instead, those people value the quality of goods and shopping environment. Thus, Walmart's EDLP strategy is no longer applicable to China's changing market situation. It needs to adjust its strategy in order to develop in a sustainable way in China. In fact, Walmart's adjustment of strategy should be based upon its online slogan "save money, live better" with an emphasis on the latter part "live better". Taking advantage of its brand power, Walmart should cultivate a consumer concept of being healthy, safe, environmentally-friendly and green.

Naturally, saving money for customers can help with the improvement on their life quality. However, product quality is the basis and the first guarantee of a quality life. So it stands to reason that the adjustment of strategy should focus on the complementary of its business formats, with supercentres and Sam's club targeting at tier 1 & 2 cities and DCH & neighbourhood markets at tier 3 & 4 cities and those area beyond the reach of supercentres and Sam's club.

3.2 Inheriting Corporate Culture Heritage and Creating Corporate Synergy

At its initial stage of development, Walmart concentrated on fast openings of stores, no heed given to improving management level and corporate culture training of staff. Admittedly, corporate culture is the spiritual bolster of the survival and development of an enterprise. It helps to improve the brand image and enhance brand effects of an enterprise. Due to persistent high staff turnover, which stood at 31% in China in 2012⁶, the highest across the industries, it becomes essential for Walmart to retain an efficient, stable and dedicated team of employees.

Walmart has rich culture heritage in staff management. For example, "open door" management philosophy encourages associates to raise questions and concerns in an open atmosphere. This reflects an free and open communication channel, which helps foster employees' loyalty to a firm. Walmart is ready to take social responsibility, making donations to charitable projects. In my opinion, if Walmart is concerned about its employees' benefits and raise their wage level, even a bit higher than industry average, this is sure to motivate them, willing to become an associate at Walmart.

3.3 Focusing on Market Research and Study Consumer Behaviour

With unbalanced economy and different markets in China, there exists a big divergence in consumer preference and buying patterns. Meanwhile rents and labour costs are rising rapidly, pressing retailers to make more profits by increasing sales. Therefore, by focusing on market research Walmart should improve its sensitivity to market opportunities and conduct planned analysis of competition. It also should analyze sales volume, market share, range of products, product pricing, goods display, promotion activities and recommendation on store location, and follow up sales performance. Walmart also needs to study Chinese consumers' buying habits and needs, better shopping environment and provide better shopping experience.

China is a gourmet nation and Chinese people love cuisine culture. There is a greater variety of goods in China but there is no free flow of those goods due to separate markets. Walmart should utilize its supply chain management skill to disseminate product information and facilitate flow of goods. By introducing recipe of local foods, Walmart can serve as a gourmet disseminator to attract more customers.

3.4 Strengthening Relationship Marketing With Government and Suppliers

Scandals such as Sudan 1 dyes used in food additives and melamine found in infant formula milk powder exposed

⁶ 90% staff turnover on the retail frontline (in Chinese). http://tech.ifeng.com/it/detail_2012_11/15/19179245_0.shtml

the loopholes in China's quality control system and raised consumers' awareness of safe foods and products. They turned to prefer brand-name products and chose to shop at brand-name stores. Moreover, public concern over environmental degradation caused by rapid economic growth urged Chinese government to cooperate with big retailers, stemming scandals related to food safety. With its rich retailing experience, strong adaptability to markets and intimate knowledge of products, Walmart should cooperate with government in culturing retail market and direct the retail industry in a healthy way. In fact, Walmart has made efforts in this respect. For instance, Walmart has started to increase the quantity and variety of green and organic food in its stores. In 2012, Walmart worked with the industry and commerce bureaus in some parts of China to sponsor a series of food safety initiatives, and provided training for close to 10,000 suppliers and customers. This received good feedbacks and caused social effects.

Although Walmart has 20,000 suppliers in China, Walmart and suppliers are not on the same footing. Walmart usually puts its suppliers at disadvantage with its buying power and tough negotiation. Walmart requires each supplier to guarantee the quality of goods at a lowest possible price. At meantime, each supplier has to keep pace with Walmart in information transmission by adopting new technology. All this deterred many suppliers. As the changing retail environment caused the change in the circulation of goods. The channels set up by manufacturers and e-commerce reduced the circulation of goods at physical stores. So Walmart has to strengthen its relationship with suppliers, defining the relationship as partnership. This supply chain partnership can motivate the suppliers and improve their logistic efficiency, reaching a win-win situation.

3.5 Extending Operation Mode and Invest in E-Commerce

Tablet PCs and smart-phones propelled the further development of e-commerce. Research group Verdict predicts that in 2013 the British online sales will occupy one-eighth of total sales while consultancy firm Bain & Company estimates that American on-line sales will account for 12% of the total by 2015. In 2010, China had e-commerce worth \$ 80 billion and by 2015 e-commerce is estimated to be worth \$300 billion. And in China those born in 80s and 90s constitute the majority of consumers. Their buying patterns are different from traditional consumers. They prefer to shop on-line by reading reviews on social media and comparing prices and "showrooming".

In 2012, Walmart acquired a 51% stake in Yihaodian, a Chinese e-commerce retailer. Yihaodian manages a

wide range of 180,000 merchandizes, including foods, consumer electronics and clothing. The acquisition shows Walmart's determination to explore new business formats. By utilize its supply chain system and store locations, Walmart can combine online and off-line businesses to provide two different shopping patterns and two kinds of shopping experiences.

CONCLUSION

Sam Walton, the founder of Walmart said, "The secret of successful retailing is to give your customers what they want. And really, if you think about it from your point of view as a customer, you want everything: a wide assortment of good-quality merchandise; the lowest possible prices; guaranteed satisfaction with what you buy; friendly, knowledgeable service; convenient hours; free parking; a pleasant shopping experience." His remarks epitomize the essence of retail business. As long as Walmart sticks to its business philosophy, makes strategy adjustment in accordance with the changing retail situation and work on the details of management and operation mode, Walmart will gain leadership in retail market and develop itself in a sustainable way.

REFERENCES

- Chan, A. (Ed.). (2011). Walmart in China. ILR Press.
- Ding, T., & Yang, Y. M. (2010). Walmart's expansion in Chinese market: Mode, process and strategy change. *Chinese Retail Research*, 6, 51-64. (In Chinese).
- Gao, R. A. (2012). The counter measures of China's logistics industry. *The Economist*, 4, 267-268. (In Chinese).
- He, C. Y. (2012). The problems and countermeasures of chain operation of China retail industry. *Logistics Engineering and Management*, 4, 47-48. (In Chinese).
- Jin, N. W., & Sun, Z. (2013, April 12). The future development of foreign retailers. *Financial Times*, (04), 12. (In Chinese). Retrieved from <http://www.ftchinese.com/story/001049895>
- Schell, O. (2011). *How Walmart is changing China*. *Atlantic Magazine*, 12. Retrieved from <http://www.theatlantic.com/...walmart-is-changing-china/308709/>
- Walton, S. *An introduction to Walmart.com*. Retrieved from <http://www.walmart.com/cp/An-Introduction-to-Walmart.com/542413>
- Wang, Q. L. (2009). Walmart's strategy positioning and the enlightenment of its localization in China. *Price and Market*, 8, 37-41. (In Chinese).
- Zhao, B. B. (2012). The study on logistics development of China's retail industry. *Modern Economic Information*, 19, 193-194. (In Chinese).