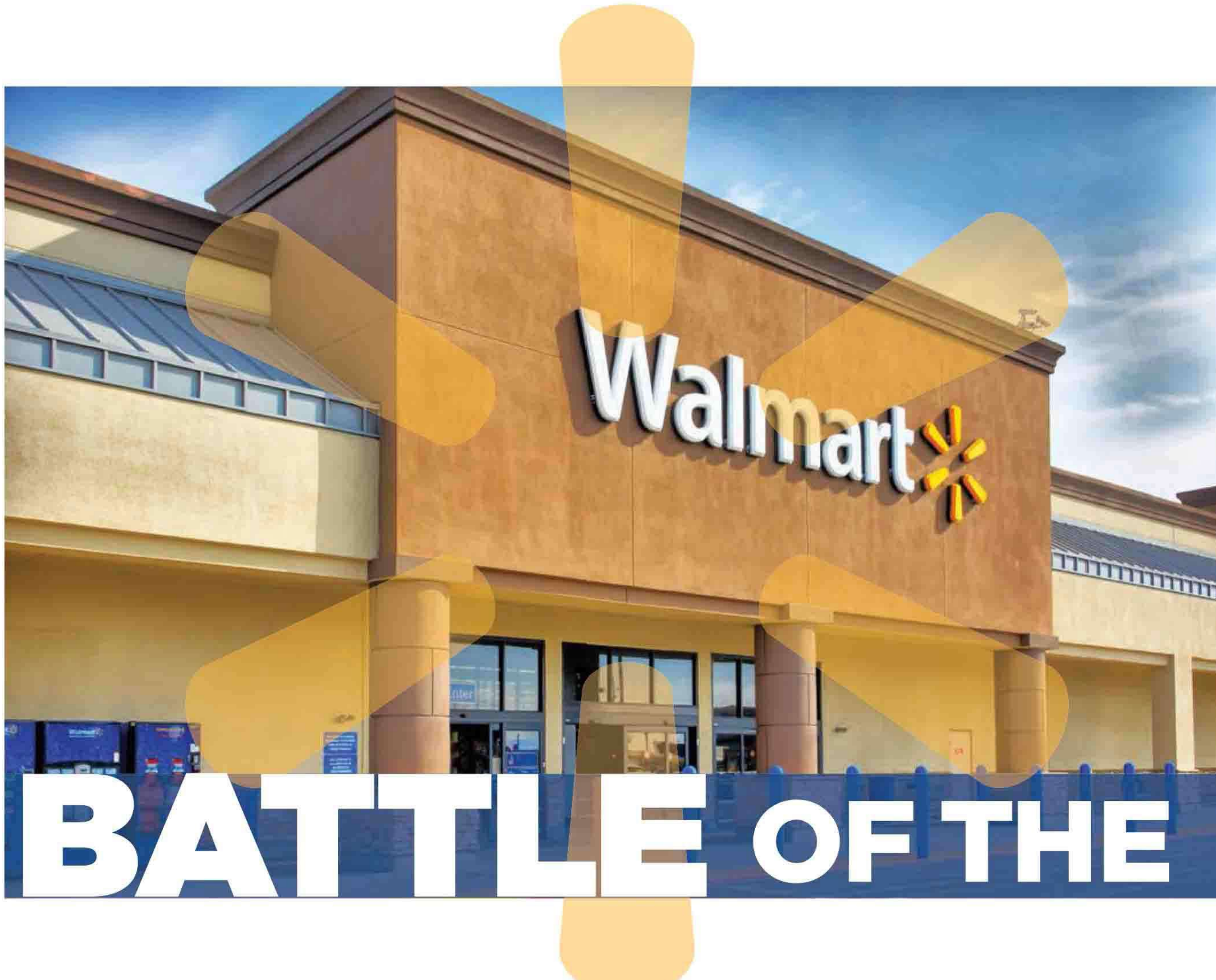


BATTLE OF THE

Retail giants Walmart and Target try to survive as consumers flock to a whole new way of shopping for mass merchandise.

WALMART EXTERIOR: KEN WOLTER / SHUTTERSTOCK.COM;

By Steve Kaufman, Contributing Writer

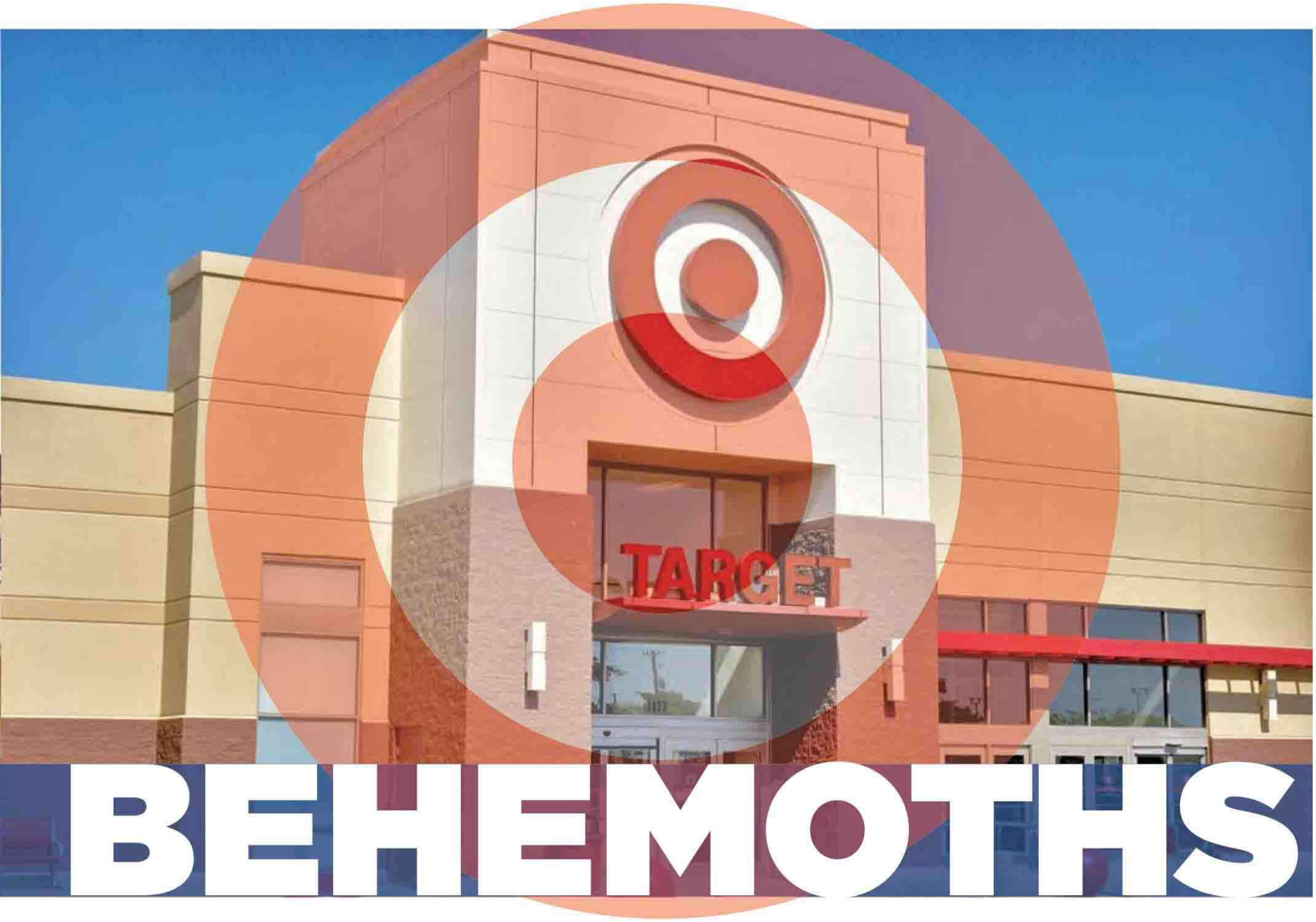
IN AUGUST 2016, THE RETAIL AND INVESTMENT worlds paused for the second-quarter financial reports from the country's two largest mass merchandisers.

On consecutive summer days, Walmart Stores (Bentonville, Ark.) exceeded Wall Street expectations, and the day prior, Target Corp. (Minneapolis) reinforced analysts' fears that it's still struggling.

Target reported a same-store sales drop of 1.1 percent and a total sales decline of 7 percent, and lowered its projections for the year. The following day, Walmart reported a same-store sales gain of 1.6 percent and a revenue gain of 0.5 percent.

In terms of online sales, both continue to lag far behind Amazon (Seattle). eMarketer, a market research company that tracks digital commerce, reported that Walmart recorded $12.5 billion in online sales in the past year in the U.S., and Target earned roughly $650 million, while Amazon pulled in a whopping $82.8 billion by comparison.

Walmart said it plans to spend $900 million on its e-commerce operations this year and $1.1 billion next year, and just spent $3.3 billion to acquire Jet.com, a Hoboken, N.J.-based online sales fulfillment company. Target said it's currently investing $1.3 billion to ramp up its IT infrastructure and distri-



BEHEMOTHS

TARGET EXTERIOR JONATHAN WEISS / SHUTTERSTOCK.COM

bution to support its omnichannel model, the largest part of its $1.8 billion capital expenditure budget.

Both Walmart and Target still have a huge investment in physical retail space. Walmart has more than 4600 stores in the U.S., and Target has nearly 1800. So how can they keep brick-and-mortar space relevant in the mass market?

One thing brick-and-mortar retailers know, says Kraig Kessel, co-founder of the San Francisco consulting firm Kraido, is that "they can't rely on 'build it, stock it, and they will come' anymore. Consumers expect an experience now."

Though Walmart shuttered its 102 small-format Walmart Express stores earlier this year, both retailers have insisted they're actively involved in strategies that rely on in-store growth, not on store closings.

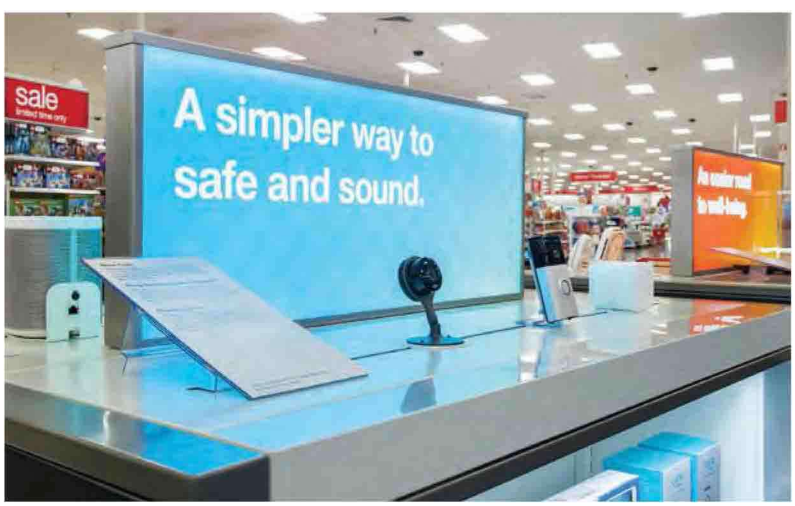
Walmart, for example, has spent $2.7 billion in the past two years to improve its stores, upgrade its in-store staff and keep shelves replenished, a problem that had reportedly cost it billions in sales over the years.

Target also remains invested in its stores. "Looking ahead, we remain focused on our enterprise priorities, as we continue to see the benefits of investing in signature categories, store experience, new flex-format stores and digital capabilities," said

Target CEO Brian Cornell on the company's second quarter earnings call in August.

Both retailers are reportedly looking at expanding their health and wellness offerings, including mini-clinics, remodeled pharmacies and enlarged vision departments. Other initiatives include coffee shops, playgrounds and/or experiential centers for kids, in addition to high-tech dressing rooms.

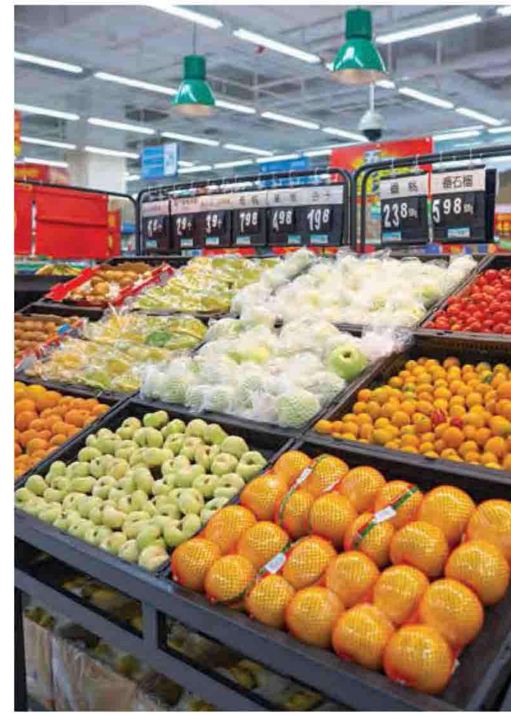
Ken Nisch, chairman of JGA Inc. (Southfield, Mich.), says big-box stores could be secondary tenants for service retailers – food and select vertical, fashion and lifestyle retailers – left homeless by the closing



COURTESY OF TARGET, MINNEAPOLIS

of shopping malls around the country. "The big-box operators could be the portals for those displaced brands," he says, "partnering with the online marketing, logistics and fulfillment, but also sampling or inventorying the brands in their stores as they look for enhanced productivity."

Also consider fresh food and groceries. Walmart has overhauled its grocery section to better compete with higher-priced – and higher-quality – players such as supermarket giant The Kroger Co. (Cincinnati). Grocery now generates more than half of Walmart's $482 billion annual revenue. It's also one product category that, because of its complex supply chain and the demand for fresh foods, Amazon hasn't entirely



SORBIS / SHUTTERSTOCK.COM

mastered despite its AmazonFresh delivery service.

The fresh grocery initiative, started by Walmart about 20 years ago, has been credited for extending its competitive margin over Target, which had closed the gap with spiffier stores and trendier merchandise in the 1990s. Target announced this spring it would re-focus on grocery with an emphasis on organic products and fresh food, which has proven tricky for the retailer in the past.

"[Target] thought it would be a way to optimize shopping baskets and build traffic," says Lee Peterson, executive vp, brand, strategy and design, for WD Partners (Dublin, Ohio). "They didn't take into account the cost of operating a perishables business." Target reportedly has double the normal distress rate of the supermarket industry.

"Walmart, early on, saw milk as a way to get people into the store," Peterson says, "and now more than half of its business is grocery. Target lagged. It continued to emphasize apparel and home. During the recession, people stopped buying apparel, but they never stopped buying groceries."

In fact, the world and the consumer never stop changing. Walmart and Target were the two most successful retailers of the last 20 years. But the next 20 years are looking considerably different. Will they be up to the challenge?