Read the case study “Wal-Mart Goes South” below and respond to the following questions:

1. **How much of Wal-Mart’s success is due to NAFTA, and how much is due to Wal-Mart’s inherent competitive strategy?**
2. **How has the implementation of NAFTA affected Wal-Mart’s success in Mexico?**
3. **Faced with going out of business, what steps did Comerci take to remain competitive? What other steps do you think Comerci should take to secure its future and further compete with Wal-Mart’s operations in Mexico?**

APA format is required for text citations and references. You are expected to support your answer with:

(1) the textbook “International business environments and operations (twelfth edition), Daniels, J. D., Radebaugh, L. H., & Sullivan, D. P. (2009). New Jersey, NJ: Pearson Education, Inc.”, and

(2) news articles, internet articles, and academic source.

**WAL-MART GOES SOUTH**

Comercial Mexicana S.A. (Comerci), one of Mexico’s largest retail chains, is faced with a serious dilemma. Since Wal-Mart’s aggressive entry into the Mexican retail market, Comerci has found it increasingly difficult to remain competitive. Wal-Mart’s strong operating presence and low prices since NAFTA’s lifting of tariffs have put pressure on Comerci, and now management must determine if Comerci’s recent participation with the purchasing consortium Sinergia will be sufficient to compete against Wal-Mart.

What’s caused this intense competitive pressure on Comerci, and what is likely to be its future? Mexico’s retail sector has benefited greatly from the increasing trade liberation the government has been pushing. After decades of protectionism, Mexico joined GATT in 1986 to help open its economy to new markets. In 1990, with Mexico’s economy’s on the upswing and additional free trade negotiations with Canada and the United States taking place, the founder of Wal-Mart, Sam Walton, met with the president of Cifra, Mexico’s leading retail store. Their meeting resulted in a 50/50 joint venture in the opening of Mexico’s first Sam’s Club, a subsidiary of Wal-Mart, in 1991 in Mexico City.

It only took a couple of months after the opening to prove the store’s success---it was breaking all the U.S. records for Sam’s Club. The joint venture evolved to incorporate all new stores, and by 1997, Wal-Mart purchased enough shares to have a controlling interest in Cifra. In 2000, it changed the name to Wal-Mart de Mexico, S.A. de C.V., and the ticker symbol to WALMEX.

Prior to 1990, Wal-Mart had never made moves to enter Mexico or any country other than the United States. Once Wal-Mart started growing in Mexico, management created the Wal-Mart International Division in 1993. The company has expanded internationally to 14 countries through new-stores construction and acquisitions. It now operates in Argentina, Brazil, Canada, China, Costa Rica, El Salvador, Guatemala, Honduras, Japan, Mexico, Nicaragua, Puerto Rico, and the United Kingdom. Wal-Mart serves 49 million customers weekly through its international operations.

With growth stalling in the United States, Wal-Mart is looking to international expansion for growth. It currently has over 2,700 retail units worldwide and employs 500,000 people. In December 2005 alone, it acquired 545 new stores and increased its personnel by 50,000 in Japan and South America. In fiscal year 2007, the international division increased sales over the previous year by 30.2 percent---to $77.1 billion---and operating profit increased 21.5 percent---to $4.2 billion. The division accounts for approximately 22 percent of sales and 37.5 percent of profits.

Some forecasters believe Wal-Mart’s growth outside of the United States will grow by an average of 26 percent for the foreseeable future and estimate that its holdings could double by the end of the decade. These predictions hold with the company’s recent acquisitions of local retailers in both Brazil and China that have dramatically increased its market presence in the two countries.

Nevertheless, Wal-Mart’s success internationally has varied by country. It has struggled to match consumer preferences and work successfully with suppliers in Japan, encountered trouble in the United Kingdom, and failed to turn profits in Germany and South Korea, forcing it to withdraw completely from both markets. However, it has flourished in Canada and, most notably, in Mexico. Wal-Mart’s operations in Canada began in 1994 with the acquisition of 122 Woolco stores. It now has more than 277 stores, 6 Sam’s Clubs, and 7 Supercenters and enjoys strong partnerships with Canadian suppliers. In Mexico, Wal-Mart operates 912 units, including Sam’s Clubs, Bodegas (discount stores), Wal-Mart Supercenters, Superamas (grocery stores), Suburbias (apparel stores), and VIPS restaurants, and it has become the largest retailer in the country.

Given its hit-and-miss success rate on the international scene, it is natural to wonder how much of Wal-Mart’s triumph in Canada and Mexico has stemmed from its internal processes, international strategies, and geographic proximity and how much can be attributed to the close economic ties shared by the three countries through NAFTA.

**Wal-Mart’s Competitive Advantage**

Much of Wal-Mart’s international success comes from the tested practices on which the U.S. division bases its success. Wal-Mart is known for the slogan “Every Day Low Prices.” It has expanded that internally to “Every Day Low Costs” to inspire employees to spend company money wisely and work hard to lower costs. Because of its sheer size and volume of purchases, Wal-Mart can negotiate with suppliers to drop prices to agreeable levels.

It also works closely with suppliers on inventory levels using an advanced information system that informs suppliers when purchases have been made and when Wal-Mart will be ordering more merchandise. Suppliers can then plan production runs more accurately, thus reducing production costs, which are passed on to Wal-Mart and eventually to the consumer.

Wal-Mart also has a unique distribution system that reduces expenses. It builds super warehouses known as Distribution Centers (DCs) in central locations that receive the majority of merchandise sold in Wal-Mart stores. It sorts and moves the merchandise via a complex system of bar codes and its inventory information system then transports it to the various stores, using its company-owned fleet or a partner. The central distribution center helps Wal-Mart negotiate lower prices with its suppliers because of the large purchasing volumes.

These strategies have resulted in great success for Wal-Mart. In 2001, it passed GE and ExxonMobil to become the largest company in the world, with sales of $344.9 billion. It has the largest private-sector workforce, with 1.9 million people in 6,995 facilities throughout the world. And it even uses the second most powerful computer in the world---behind the Pentagon’s---to run its logistics.

**Wal-Mart in Mexico**

Despite its current success in the region, Wal-Mart encountered some difficulties with its opening in Mexico prior to the passage of NAFTA. One of the biggest challenges it faced was import charges on many of the goods sold in its stores, thus preventing Wal-Mart from being able to offer its “Every Day Low Prices.”

Unsure of local demand, Wal-Mart stocked its shelves with things like ice skates, fishing tackle, and riding lawnmowers---all unpopular items in Mexico. Rather than informing headquarters that they wouldn’t need those items, local managers heavily discounted the items, only to have the automatic inventory system reorder the products when the first batch sold. Wal-Mart also encountered logistics problems due to poor roads and the scarcity of delivery trucks. Yet another problem was the culture clashes between the Arkansas executives and the local Mexican managers.

Some of these problems were solved by trial and error, but the emergence of NAFTA in 1994 helped solve most of the problems. Among other things, NAFTA reduced tariffs on American goods sold to Mexico from 10 percent to 3 percent. Prior to NAFTA, Wal-Mart was not much of a threat to companies like Comerci, Gigante, and Soriana, Mexico’s top retailers. But once the agreement was signed, the barriers fell and Wal-Mart was on a level playing field with its competitors---all it needed to become number one.

NAFTA encouraged Mexico to improve its transportation infrastructure, thus helping to solve Wal-Mart’s logistical problems. The signing of NAFTA also opened the gates wider to foreign investment in Mexico. Wal-Mart was paying huge import fees on goods shipped to Mexico from areas like Europe and Asia. Foreign companies knew that if they built manufacturing plants in Mexico, they could keep costs low with Mexican labor but ship to NAFTA’s free trade zone---Mexico, the United States, or Canada.

As companies began to build manufacturing plants in Mexico, Wal-Mart could buy these products without paying the high import tariffs. An example of this tactic is Sony’s flat-screen television line, Wega. Sam’s Clubs in Mexico imported Wega TVs from Japan with a 23 percent import tariff plus huge shipping costs, resulting in a $1,600 retail price at Sam’s Club. In 1999, Sony built a manufacturing plant in Mexico, thus allowing Sam’s Club to purchase the Wegas without import tariffs; this tactic also yields much lower shipping fees. Sam’s Clubs passed on the savings to customers---with a retail price of only $600.

The benefits of NAFTA, such a lower tariffs and improved infrastructure, helped not only Wal-Mart but also its competitors, like Comerci. But Wal-Mart used the advantages of NAFTA better than anyone else. Rather than pocketing the differences the lower tariffs made, Wal-Mart reduced its prices. In 1999, it closed one of its Supercenters for a day to discount up to 6,000 items by 14 percent.

Comerci and others have combated Wal-Mart’s tactics by lowering their own prices, but on many items, they can’t get the price as low. Wal-Mart’s negotiating power with its suppliers is large enough that it can get the better deal. Also, most of Mexico’s retailers priced goods differently. They were used to putting certain items on sale or at deep discount, a strategy known as “high and low,” rather than lowering all prices. They have been trying to adjust their pricing structure to match Wal-Mart’s, but they are still frustrated with the continued cost cutting of Wal-Mart. Competitors and certain suppliers are so angry that they have gone to Mexico’s Federal Competition Commission (known in Mexico as CoFeCo) with complaints of unfair pricing practices.

**Formation of Sinergia**

Unable to compete with Wal-Mart under the new conditions, Comerci has been faced with extinction. Wal-Mart is the largest retailer in Mexico and owns about 55 percent of the market share in Mexico’s supermarket sector, with $15.4 billion in sales and $585 million in profit in the country during 2005. In 2007 alone, Wal-Mart added 120 new stores in Mexico. In contrast, Comerci realized only $3.6 billion in sales and $167.5 million in net profit and has seen its market share drop to 15 percent.

Fear over the giant retailer’s predominance and over its unexplained withdrawal from the Mexican National Association of Department Stores (ANTAD) in 2004 prompted Comerci to band with two other struggling homegrown supermarket chains, Soriana and Gigante, to form a purchasing consortium that would allow them to negotiate better bulk prices from suppliers.

The collaboration, known as Sinergia, was initially rejected by CoFeCo and met resistance from the Consumer Product Council of Mexico, a 46-member organization representing major consumer goods companies, which feared that Sinergia would use its purchasing power to force unreasonably low prices on suppliers. However, after its second presentation to CoFeCo, the consortium was at last approved, provided that it issue regular reports to CoFeCo outlining the nature of its purchasing agreements and that it sign confidentiality agreements with the participating chains to prevent price-fixing and monopolistic behavior. As a representative body with no assets, Sinergia’s purchases are currently limited to only local suppliers, and its future is still uncertain.

Should Sinergia fail to improve the situation, Comerci could still look for possible foreign buyers, like France’s Carrefour, or it could duplicate the efforts of its Sinergia partner Soriana, which is attempting, with some notable success, to differentiate itself from Wal-Mart by offering products and a store atmosphere that appeal more to Mexicans’ middle-class aspirations.

The government may give Comerci a break if it rules against Wal-Mart’s aggressive pricing, but as one analyst put it, “We do not believe the CFC will end up penalizing Wal-Mart for exercising its purchasing power in an attempt to get the best deals available in the marketplace, which is the goal of every retailer in the world, especially when [these savings] are ultimately passed on to consumers.” One thing is certain, however---Comerci cannot afford to sit still.