UNPACKING THE WAL-MART DEBATE
A DISCUSSION OF THE INTERNATIONAL TRADE PROCESS, ISSUES AND IMPLICATIONS OF WAL-MART’S ENTRY INTO SOUTH AFRICA

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Abstract
This paper attempts to discuss the management, marketing, strategies and other variables in terms of Wal–Marts entry into South Africa. It therefore discusses the international trade processes, a host of competing issues and the implications for the company, as a business entity in a democratic South Africa, post 1994. In this regard the paper attempts to establish a momentum for business management and the application of business principles, in order to consolidate Wal–Marts entry into a developing economy in Africa.

Key Words: Debate, International Trade, Implications, Entry, Dilemma, Protectionism, Markets, Economies

Introduction
Despite a plethora of objections, the South African Competition Tribunal (CT) found that it could not prevent American retailing behemoth, Wal-Mart, from acquiring a 51 per cent stake in Massmart SA. The controversial acquisition, which was initially approved by the Competition Commission (CC), has generated considerable debate around the consequences of the retailing giant’s entry. This assignment will discuss, inter-alia, the international trade process as well as the issues and implications of Wal-Mart’s entry into SA.
Firstly, in order to understand the South African Governments dilemma between opening its doors to free trade and protectionism, one needs to consider the long-lasting effects of the Apartheid regime on economic development. In 1962, the General Assembly of the United Nations voted for extensive economic sanctions to be imposed on South Africa – a scheme that condemned the Apartheid regime. In 1994, when the African National Congress (ANC) assumed state power, they inherited a superfluity of challenges associated with a poorly performing economy (Trewhela, 2010). Consequently, SA now faces R1.5 trillion infrastructure backlog (Reuters, 2011b). Given that infrastructure is a key component of economic growth and that local investment has not been able to reduce the deficit, Africa’s largest economy is forced to open its doors to Multi- National Corporations (MNCs) and Foreign Direct Investments (FDI).
Although the notion of foreign firms investing copiously in developing nations may seem appealing, Rossouw (2010) warns that the sheer size and clout of some MNCs pose a risk to those countries that welcome them. Wal-Mart is more than a MNC. The company operates internationally under 55 different names and has more than 8500 stores. The revenue that it generated last year ($405 billion) is enough to qualify it as the 23rd largest economy in the world - dwarfing SA (Sehgal, 2011). These statistics highlight the fact that Wal-Mart is indeed a powerful company that possesses significant economic and political clout.

The International Trade Process

Globalisation has offered Multinational Corporations (MNCs), like Wal-Mart, enormous opportunities in spreading their operations and activities to the far corners of the world. Kim (2006) contends that companies expand their activities across borders for many reasons. Amongst these, access to larger markets, economies of scale and cheaper resources are the most popular reasons for expansion. In Wal-Mart’s case, the company’s survival was directly linked to its growth, and the international arena provided an ideal platform for sustainable growth. Wal-Mart could not afford to confine its operations to a country that accounts for only 4 per cent of the world’s population - the USA. As a result, the company began globalizing in 1991, and has since aggressively pursued a globalisation strategy (Govindarajan and Gupta, 2002).

Although free trade agreements and advances in technology and transportation have made it easier for firms to conduct business across borders, Pearce and Robinson (2011) are of the opinion that there are numerous complexities associated with the international trade process. The authors note that rigorous assessment, both internal and external, are conducted before a company enters or expands into the international arena. Careful examination regarding the status of intended host nations - especially in terms of economic progress, industrial facilities and technological capabilities - are conducted. More importantly, a thorough understanding of political risk is a key element in the decision to do business in a foreign country. In addition to these assessments, Wal-Mart would have also examined the relative “openness” of South Africa to international trade. Being signatory to the Southern African Development Community (SADC), as well as the recently formed BRICS\(^1\) community, has signaled that SA is relatively open to trade. Consequently, Wal-Mart settled on SA as its first host country on the African continent.

Once a firm decides to extend its activities across geographic borders, it must determine the most effective and efficient mode of entry. Shetty (2010) avers that organizational structures may assist or impede organisations efforts to expand globally. The author also notes that an organization’s structure plays a key role in determining the most suited mode of entry. As such, Wal-Mart’s transnational structure - which combines key aspects of functional, product and geographic structures-, affords the company the opportunity to utilize a variety of entry modes and ownership structures (Luthans and Doh, 2009). According to Luthans and Doh (2009:282), the most common strategies include:

- Importing and Exporting;
- Licensing Agreements;
- Wholly-owned Subsidiaries;
- Mergers and Acquisitions;
- Alliances and Joint Ventures; and
- Franchising

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\(^1\) Brazil, Russia, India, China and South Africa
Wal-Mart’s entry into South Africa was through the process of Acquisition - offering to buy 51% of South African retailer Massmart Holdings Inc. for $2.5 billion (Bernhardt, 2011). The crucial question, then, is why did Wal-Mart choose to use the “acquisition” strategy and not any of the other modes of entry, especially, given that this strategy bears higher risks and requires more resources and commitment of finances? The section to follow, therefore, will critically analyse Wal-Mart’s choice of strategy for entry into South Africa. However, a defining issue needs to be emphasised before any further analysis is undertaken. Wal-Mart’s entry into South Africa will give it a critical foothold to expand in Africa and allow the American giant retailer an opportunity to beat European multinational rivals Carrefour, Tesco and Metro into the potentially lucrative sub-Saharan market. It would seem that South Africa is increasingly becoming the gateway for doing business on the African continent (Enslin-Payne, 2011).

Why did Wal-Mart not choose the Import/Export Strategy?
While this mode of entry would have required a minimum investment for Wal-Mart as an entry strategy into South Africa, the disadvantages outweigh this advantage (Luthans and Doh, 2009). Trade barriers and tariffs would have added to the cost of operation. Besides, transport costs would have also weighed heavily against the viability of their operation in South Africa. In addition, Wal-Mart would not have been able to leverage its brand reputation if it simply imported goods (especially those that are common to other retailers) into South Africa. Overall, though, Wal-Mart would have been viewed as an outsider and would have lacked access to critical local information.

Why did Wal-Mart not choose Licensing as a Strategy?
While this mode of entry would have minimised the costs of Wal-Mart’s entry into South Africa, it would lack control of its assets (Luthans and Doh, 2009). The licensee could become a competitor and there would be knowledge spill-over. Moreover, the license period could be limited and potential for sales would be low in South Africa.

Why did Wal-Mart not choose Wholly-owned Subsidiary Strategy?
Ideally Wal-Mart would have wanted to use this strategy as a point of entry into South Africa because of total control and the belief that their managerial efficiency will be better with outside partners. In addition their profits would be higher and there would be clearer lines of communication and shared visions (Bernhardt, 2011). Moreover, there would not be such strong objection to their entry, since the threat of retail concentration would have been low. However, the high set-up costs especially in terms of developing distribution channels and a customer base, as well as the strong Labour Unions in South Africa prevented Wal-Mart from using this strategy (Craven, 2011).

Why did Wal-Mart not choose the Alliances and Joint Venture Strategy?
Wal-Mart did not use this strategy as a point of entry into South Africa because it is difficult to manage and would have led to dilution of control. Besides, this strategy has a greater risk than that of importing/exporting and licensing. There would also be a risk of Wal-Mart’s partner becoming a competitor (Pearce and Robinson, 2011).
Why did Wal-Mart not choose the Franchising Strategy?
Given that Wal-Mart is a well-established retail hyper store in the USA and not a service provider like McDonalds, and the fact that it did not have a brand foothold, it could not use the franchise strategy to enter South Africa.

Why did Wal-Mart use the Acquisition Strategy to enter South Africa?
Firstly, it is important to note that that Wal-Mart has had its fair share of misfortune in competing in other parts of the world. It has used various strategies of entry in different parts of the world, for example, in Germany and Korea it used the acquisition mode of entry and failed. In South America it used the Joint Venture strategy and has succeeded, to a certain degree. In the first example it failed because it did not understand the culture of local firms and misread the political power of the labour unions. It succeeded in the case of South America, primarily because it teamed up with local firms, who fully understood the nuances of the culture of business in their home country (Govindarajan and Gupta, 2002, Angotti et al., 2010).

Wal-Mart will be entering South Africa through the Acquisition strategy, primarily, because it did not want to set up a Greenfields operation. The tactic of only acquiring only a 51% share in Massmart, has afforded Wal-Mart the opportunity to assume control, whilst avoiding even stronger opposition\(^2\) from trade unions and the SA Government. Wal-Mart realised that Massmart had made significant headway in its reach into Africa and in the process had built up the necessary economic and political infrastructure (Bleby, 2011, Moorad, 2011). Furthermore, in understanding that there was a political and cultural mismatch in dealing with labour and clientele in foreign countries, Wal-Mart decided to retain all the senior management of Massmart, and in this way it would it would retain the “intellectual property” that was necessary to deal with the indigenous cultural and political problems that face many MNCs in foreign countries. In essence, Wal-Mart wishes to gain a foothold in Africa through the bridgehead of South Africa. Wal-Mart acknowledges the potential of the emerging market in Africa with all its problems and challenges and is prepared to incur initial losses for long-term gains- a cautious but prudent approach and strategy (Jacobs, 2011).

Generally, MNCs are regarded as outsiders in their host countries. Moreover, by retaining Massmart’s earlier obligation to Black Economic Empowerment in South Africa, Wal-Mart, through the acquisition process, could be viewed as an insider.
In this way, Wal-Mart would be able to apply a greater knowledge of the local market conditions, minimise knowledge spill-over, better apply specialised skills and reduce the risks of setting up business in South Africa (Pearce and Robinson, 2011).

The Issues and Implications of Wal-Mart’s Entry into South Africa
Despite the numerous objections raised by trade unionists, politicians and ministers, the Competition Tribunal found Wal-Mart’s acquisition of Massmart, would not break SA’s completion laws\(^3\). In addition, it was found that if the CT refused entry to Wal-Mart, the SA Government would have breached the 1994 General Agreement on Trade (GAT) in Services, which it currently signatory to (Enslin-Payne, 2011, Mitchell, 2011, Stolley, 2011).
These objections, however, were never unjustified. Wal-Mart’s international reputation is not one of an ethically and socially responsible MNC. The wrong-doings of Wal-Mart in other countries have grown to include, inter-alia; (1) poor working conditions and remuneration for

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\(^2\) Considering that Wal-Mart repatriates its earnings, south Africa would stand to lose more if Wal-Mart acquired 100% of Massmart

\(^3\) SA completion laws mandate that any merger/acquisition must be evaluated from both an economic and “social impact” perspective
employees, (2) predatory pricing\textsuperscript{4}, (3) racism, (4) labour union opposition, (5) destroying local suppliers, and (6) various other anticompetitive strategies (Sehgal, 2011). As such the potential issues and implication of Wal-Mart’s entry are discussed below (Bernhardt, 2011).

**Foreign Direct Investment**

Infrastructure is critical to South Africa’s long-term goals, especially in terms of the New Growth Path\textsuperscript{5}. Although the SA Government is planning to outlay R809 billion over the next 3 years to tackle its infrastructure backlog, many analysts believe that this amount is still not enough to address the country’s issues of unemployment and jobless growth (Harris, 2011, OECD, 2008). Consequently, FDI offerings from Wal-Mart and other MNCs may prove to be a viable option to sustain the country’s growth targets. As Wal-Mart expands their operations, it is more than likely that they will add to the country’s infrastructure, as they have done in the United States of America (USA) (Sehgal, 2011).

**Local suppliers and procurement**

One of the key issues raised at the CT, was the impact that Wal-Mart will have on Massmart’s procurement patterns. It was argued that some of Wal-Mart’s competitive advantage accrued from sourcing goods cheaply in one country and then efficiently distributing them throughout its global operations. As a result, local suppliers would be snubbed in favor of cheaper suppliers from other countries. However, an analysis of Massmart’s procurement patterns- prior to the acquisition- reveals that the company itself, either imported a substantial amount, or were contracted to local suppliers who themselves, imported a substantial amount. For example, in 2010, Massmart directly imported R1.4 billion (10\%) of all the goods that it sold. Therefore, it becomes evident that, contrary to the objections, SA producers are already exposed to a considerable amount of international competition (Ridyard et al., 2011).

Despite there being a threat to local procurement, Wal-Mart’s entry may also have a positive effect on local suppliers. The company’s internationally revered supply chain and logistics may present local suppliers with an opportunity to enter foreign markets. For example, SA wine is well appreciated in many other parts of the world. In this regard, local wine suppliers may find that Wal-Mart could indeed decide to stock SA wine in their foreign stores. In addition, Wal-Mart’s local suppliers may find that they are able to achieve economies of scale, especially as the company expands and demands larger quantities. Furthermore, Wal-Mart has planned to drastically increase in-store product offerings and coverage. This may provide additional opportunities for local suppliers - that were previously not on Massmart’s procurement database - to meet this demand (Reuters, 2011c, Ridyard et al., 2011).

Although evidence from Wal-Mart’s operations in Chile, as well as its proposed ‘supplier development fund’ in SA seems to indicate that the company is in fact committed to local suppliers, Minister of Economic Development, Ebrahim Patel, believes that this will not be enough to save local suppliers (Craven, 2011).

**Domestic competition**

The impact of the recession on the retailing industry has made it difficult to judge the initial impact that Wal-Mart has had on local competition. For example it is hard to gauge whether the recent retrenchment of 3000 Pick ’n Pay employees was due to an overall decrease in consumption expenditure, or whether Pick ‘n Pay has already conceded market share to Wal-Mart (Chilwane, 2011).

\textsuperscript{4} A pricing strategy that intentionally sells a product at a low cost in order to drive competitors out of the market

\textsuperscript{5} South Africa’s long term macroeconomic strategy
The threat of retail market concentration as a result of the acquisition, is relatively low, considering the fact that Massmart currently dominates only 17.5 per cent of the retail industry in SA (Shoprite holds 12%, whilst Pick n Pay has 11%). (Riday et al., 2011)

However, the impact that Wal-Mart will have on Small, Medium and Micro Enterprises (SMMEs), is still unpredictable. The expansion of Wal-Mart stores into areas traditionally served by SMMEs may prove to be an opportunity for small firms to showcase their flexibility in responding to market trends. For example, SMMEs in South Africa have been recognized for their ability to survive the threat of organized retailers, by focusing their efforts on niche markets (Herrington et al., 2010). On the other hand, it could be the case that Wal-Mart’s sheer size, could prove to be an extremely efficient barrier to entry for new firms attempting to enter the local market.

Ultimately, the CT found that it could not refuse Wal-Mart’s entry into the country, on the grounds of economic efficiency. If it had done so, it would be a move against the very conduct which, in all other situations, it seeks to encourage (Reuters, 2011a).

**Consumer welfare**

It is undisputed, even by those that have objected to Wal-Mart’s entry, that competition in any industry benefits consumers. Aggressive competition forces firm that are competing in the retail industry to either lower their prices or raise the quality of goods being sold. The only beneficiaries in this regard, are consumers. What is more is that Wal-Mart is planning to expand their food product offerings, especially to low-income consumers (Bernhardt, 2011).

**Local employment, labour laws, labour relations and labour unions**

Wal-Mart has become notorious for its anti-union conduct, poor labour relations and low pay, in almost every country that it operates. Even in its home country, Wal-Mart pays some of it employees a wage that is below the poverty line (Greenhouse, 2005). (Jacobs, 2011) believes that Wal-Mart’s well-documented history of violation relating to labor and employment laws as well as the numerous sexual and racial discrimination laws suites levied against it, should have been reason enough for the CT to impose conditions on the company’s acquisition of Massmart. Angotti et al. (2010) found that ; (1) Wal-Mart store openings kill 3 local jobs for every 2 they create, in every country they enter, (2) Wal-Mart’s entry into a country reduces overall retail activity as well as employment opportunities and (3) Sales of Wal-Mart’s competitors decline-on average- 10- 40 % within the first year. If Wal-Mart continues with this pattern in South Africa, it could have serious consequences on the already impaired labour market.

In this regard, the objections raised by the South African Commercial, Catering and Allied Workers Union (Saccawu) and the Congress of South African Trade Unions (Cosatu) are justified, especially considering that a 1 per cent shift of purchases from local to foreign suppliers will result in roughly 4000 local jobs being lost. In addition, it is argued that even if the acquisition results in new job creation, Wal-Mart’s low employee remuneration strategies will not aid economic development (Reuters, 2011c, Reuters, 2011a)

**South Africa’s imports**

In 2010, Wal-Mart’s (USA) imports from China, accounted for approximately 10 per cent of USA’s trade deficit with China (Sehgal, 2011). The point has been made that when Wal-Mart sources cheaper good from abroad, it will be difficult for local suppliers and retail store to compete with them.

As a result, the only way local suppliers and retailing store can compete with Wal-Mart, is to source cheaper goods from abroad as well. This vicious cycle of importing large quantities, will
have serious consequences in terms of the macro economy, especially considering SA has posted its largest trade deficit (R3.9billion) in 6 months (Cohen, 2011)

**Waterbed effects**

‘Waterbed effects’ refer to a situation whereby a powerful company, such as Wal-Mart, is able to exercise buyer power over an industry supplier to the extent that the supplier is forced to increase his selling price when supplying to Wal-Mart’s competitors (UK CC, 2006). Consequently, Wal-Mart’s competitors (e.g. Pink-n-Pay) may be forced into increasing their selling prices. As a result, both Wal-Mart’s competitors and their customers may suffer.

**Tax payments and Repatriation of profits**

It is undeniable that Wal-Mart is always trying to improve its profit margins. High profits translate into higher tax payments to the SA Government. It is also possible that an expansion in the product offerings at Wal-Mart stores may indeed stimulate higher consumer expenditure, which, once again, adds to the value of tax payments that Wal-Mart will make to the South African government. In this regard, the acquisition will indirectly benefit society since the Government will collect more tax from Wal-Mart, than it did from Massmart. Although corporate tax payments are relatively well governed by the South African Revenue Services (SARS), it is rather worrying for the South African government that Wal-Mart is well known for its tax avoidance schemes (Wal-Mart Watch, 2007).

It is also acknowledged that, despite the initial investment of $2.4 billion, Wal-Mart is not expected to reinvest much of its earnings in SA. As it has done in many other countries, Wal-Mart will repatriate substantial amounts of its earning in SA, back to the USA.

**Food Security**

Wal-Mart’s strategy to increase its food product offerings, could pose a threat to domestic food security if these products are imported. The introduction of low cost food products may prove to be popular amongst consumers, especially considering the recent food price hikes. It is almost certain that the only way Wal-Mart will be able to execute this strategy, is to source cheaper foods from abroad. This in turn, may force local farmers and producers to shut down. Consequently, food in South Africa may be at the mercy of international fluctuations and varying exchange rates (Angotti et al., 2010, Ridyard et al., 2011).

**10 Dominance model**

Steiner and Steiner (2009: 26) note that the respective roles of business, government and society are equally considered in a truly democratic country. However, when corruption is highly prevalent in a country, there is an increased risk of powerful companies, such as Wal-Mart, persuading the government to overlook certain unlawful actions. Consequently, it seems as though Wal-Mart’s entry may further add to the possibility of a “Dominance Model” prevailing in SA, whereby; “corporations and a powerful elite control a system that enriches a few at the expense of many”. Such a system is undemocratic.

**Conclusion**

When McDonald’s entered SA in 1995, many critics believed that in the long-run, such a company would have adverse effects on both local fast food outlets, as well as consumers. This however, was not the case. As such, it is extremely difficult to predict how even an internationally successful company will perform in SA.

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6 American Fast Food Chain
There are advantages and disadvantages in Wal-Mart’s entry into South Africa. As much as Ebrahim Patel\(^7\), Rob Davies\(^8\), Tina Joemat-Peterson\(^9\) and the labour unions object to, and fight for ‘conditions’ to be imposed on Wal-Mart’s entry into South Africa, the country’s macro free-market policy and the international free trade agreements favour Wal-Mart’s imminent presence. Wal-Mart is determined to make its presence felt in South Africa, primarily because of its long-term intention of making a grand entry into the emerging markets of the rest of Africa (Marais, 2011).

However, it is early days to evaluate Wal-Mart’s success in its bid to enter and sustain itself in South Africa. Given Wal-Mart’s poor record in terms of its labour-relations, lack of social responsibility and overall exploitation of host economies, the South African government needs to ensure that it holds Wal-Mart to its promises, through legally-binding and water-tight contracts. What is certain, though, is that there will be winners and losers as Wal-Mart makes its entry into South Africa. We can only hope that for South Africa and its people, the gains outweigh the losses.

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