



### **South Africa: Inside The Wal-Mart-Massmart Merger**

We've been following the ongoing hearings at the **Competition Tribunal Of South Africa** – charged with adjudicating the nation's competition matters - on the **Wal-Mart-Massmart** merger and feel it is possibly the best barometer of the condition of the South African economy and its potential to serve as an unofficial proxy of the continent's growth this decade, particularly in the retail sector. The hearings are a nexus point for a confluence of forces, opportunities and challenges in SA and a bellwether on the country's growth this year with direct impact on the **Johannesburg Stock Exchange (JSE)**.

Last Fall, Wal-Mart Stores offered over \$2 billion for 51% of Massmart shares.

Today's *Wall Street Journal* article, "Wal-Mart's Africa Foothold Shaky as Job Worries Mount," is a broad-brush version of what is really taking place on the ground and we think reads a bit excessive in the doom and gloom category. We remain confident the Wal-Mart merger will be approved for two reasons: the fallacious reasoning against Wal-Mart (juxtaposed to the aspirations of South Africa's emerging consumer class) and the nature of the coalition against it.

Rather than delve into the details of the Tribunal hearings and the broad array of testimony presented within it, **the Journal's Devon Maylie** (and it appears with him all Western financial media) lifts one aspect, out of context, from the April 19, 2011 Report of **Genesis Analytics**, commissioned by the **Departments of Economic Development, Trade & Industry and Agriculture, Forestry and Fisheries** (<http://www.comptrib.co.za/assets/Uploads/73LMNov10-Genesis-Report.PDF>). While the report is an interesting read and depicts the impact of the merger in a negative light, it is hardly a proxy of the positions of the constituencies with the most at stake inside of South Africa – Massmart on one hand and labor unions on the other. For those more consequential viewpoints the witness statements with greater relevance were offered by **The Southern African Clothing & Textile Workers' Union (SACTWU)** (<http://www.comptrib.co.za/assets/Uploads/Case-Documents/73LMNov10-Supplementary-Submissions-by-SACTWU.pdf>) and that of **Mr. Grant Pattison**, former Executive Assistant to the CEO of Massmart (<http://www.comptrib.co.za/assets/Uploads/73LMNov10-Genesis-Report.PDF>).

The SACTWU testimony suffers from a bit of schizophrenia – struggling to depict SA as both an infant and mature adult in the trajectory of its economy growth path. It likens South Africa to **Mexico** (and claims it is therefore a developing economy) while asserting that South Africa's retail sector is a mature one (and claims it functions more like a developed economy). The report accurately frames the trade-off between an

indigenous small business decline in pursuit of broader employment opportunities provided by multi-nationals – and which commonly accompanies Wal-Mart’s presence. Yet it trips itself up when it describes that a flood of imports into South Africa has led to a 49% decline in jobs in the clothing and textile sector (which employed 206,900 jobs in December 2002 versus 106,300 jobs in September 201 – a loss of 100,600 jobs in 8 years). SACTWU says the reason for dramatic surge in imports are the overvalued **Rand**, lower tariffs (which have made it more lucrative to import clothing and textile products), the emergence of **China** as a major clothing, textile, and footwear producer and the fact that South African retailers are increasingly turning to goods made outside South Africa. It argues that South Africa’s exports have decreased from \$300 million worth of clothing in 2002 and have slumped down 65% to \$86 million in 2009. Then the report very vaguely acknowledges the broad impact of the global recession on spending and credit in South Africa before providing a rough cost-benefit analysis against the merger “...the results of the low cost goods at Walmart ultimately come at a high social and economic price: lost jobs, lower wages, and a growing wage deficit.” The witness testimony even throws in warnings against the possibility of obesity and more impoverished workers (as a result of working at Wal-Mart) which it documents from case studies of Wal-Mart workers in the United States (the most economically developed country in the world). In conclusion it asserts that Massmart’s becoming a ‘foreign’ entity (as a result of Wal-Mart’s 51% ownership) “will reduce levels of black economic empowerment and the likelihood of empowerment procurement within the retail sector.”

SACTWU is part of a vanguard ‘anti-Wal-Mart’ coalition which consists of various trade unions, including the SA Commercial, Catering and Allied Workers' Union (Saccawu), The Congress of SA Trade Unions (COSATU) and civil society organizations all in alliance with the UNI Global Union, an umbrella organization with 20 million workers worldwide. That the opposition is part of a larger global movement against Wal-Mart as much as a protector of domestic concerns is abundantly transparent

The testimony and the coalition composition show the shaky ground the opposition to the merger stand on. The allegation that Wal-Mart’s ownership could lead to 4,000 jobs lost in SA industry is a drop in the bucket when compared to the acknowledged loss of over 100,000 jobs over the last 8 years which pre-date Wal-Mart’s presence. And the combined blame pointed to by SACTWU to be shared by China, a strong rand, the financial crisis, and domestic retailers seeking foreign products makes it clear to any observer that Wal-Mart’s merger of Massmart takes place in the context of factors well beyond its control and which it can neither solve nor dramatically worsen.

In addition, as Grant Pattison’s testimony makes clear, *only 38% of Massmart’s total workforce is unionized* – with decentralized negotiations taking place across 4 of the company’s divisions. The fact that Wal-Mart is buying a simple majority share of an existing retailer makes the comparison of what Wal-Mart might do with Massmart in relation to unions not uniformly analogous to Wal-Mart’s relations with unions around the world. Massmart already has a history of union relations in SA that can more easily be evaluated - and not as easily demonized - than a Wal-Mart yet to hit the continent.



We are keeping our eyes not only on Wal-Mart's stock price which initially sagged on the negative depiction of the Tribunal hearings:

- [S.Africa union may mull legal action on Wal-Mart deal](#) at Reuters(Tue 10:12AM EDT)
- [Massmart says supply targets could jeopardize deal](#) at Reuters(Tue 7:42AM EDT)
- [Massmart Says Imposing Procurement Goals May Lead to Job Losses](#) at Bloomberg(Tue 7:10AM EDT)

As we noted last year (see *APB* Newsletter Dec. 8, 2011) with Wal-Mart's growth in the U.S. slowing its interests in Africa are significant and can't be overlooked. Massmart has 263 stores in South Africa and 25 stores in 14 other African countries, growing even in rural areas yet to be exploited by mass retailers. By contrast, Wal-Mart has 300 stores in **China** and 450 in **Brazil**. Africa, not this decade but *now* is absolutely going to weigh on or boost Wal-Mart's stock price, earnings estimates and valuations in future years.

We see the news that Massmart itself is worried about the deal being approved[ [UPDATE 1-Massmart says supply targets could jeopardise deal](#) at Reuters(Tue 6:39AM EDT) ] as posturing designed to send a warning signal both indirectly (through capital markets) and directly to the SA government of possible negative consequences to South Africa's reputation as the gateway to the entire continent if the merger doesn't go through.

We don't think any of the objections to the merger can't or won't be addressed by Wal-Mart or Massmart and for how that might take place, the Pattison testimony is most instructive and the Genesis report – far from deal-breaker – actually sets the criteria.

The combined forces of increased consumer expectations and aspirations; government recognition of the need for foreign capital and job growth; and appreciation of the leadership position of SA as the vessel for pan-African portfolio investing [93% of purchases of Sub-Saharan African (SSA) companies by other SSA firms feature South African businesses as the buyer] in concert with the relatively weaker arguments and membership of the anti-Walmart coalition give us little pause as we look forward to a successful merger. We think the sentiment of both the broader electorate and government – with no interest in demonizing Wal-Mart and more pressing issues to concern themselves with - will win out.

Those looking to benefit in the short-term should keep an eye on the **Shoprite Holding ADR (PNK)** which has been trending upward. Shoprite is the largest food retailer in South Africa whose leadership position is likely to face a challenge from a Massmart expansion into food retailing backed by Wal-Mart's deep pockets

(see 'Mass Mart takes on Shoprite':

<http://www.businesslive.co.za/Feeds/businessetimes/2011/02/26/massmart-takes-on-shoprite> ).

With a geographical spread into 16 African countries

(<http://www.shopriteholdings.co.za/pages/1019812640/about-our-company/Geographical-spread.asp> ) and

the increased visibility as a result of its inclusion in the new **S&P CIVETS 60** index last week, there is a lot to like about their business – whether Wal-Mart comes to town or not.

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