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Wal-Mart May Face Considerable Fines, Reputational Issues

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NEW YORK -(Dow Jones)- Wal-Mart Stores Inc. (WMT) potentially faces major fines and another setback to its reputation as a result of allegations of widespread corruption at its Mexican unit.

The retailer is already feeling some of the ill effects. Its stock, which usually trades in a narrow range, has fallen as much as 5.3% Monday, its biggest one-day drop in two years. Shares were recently off 4.7% to \$59.47.

The retailer is under a cloud of suspicion as a result of allegations that its Mexican operation engaged in widespread bribery to expedite expansion in the country. Wal-Mart de Mexico SAB (WALMEX.MX) is now the retailer's largest international unit, operating about 2,100 stores. Along with China and the United Kingdom, Mexico contributed the highest dollar increases to Wal-Mart international's sales growth last year, according to the retailer's annual report.

Now, it is being alleged that Mexican operations grew so large through a bribery campaign to secure permits and other considerations. The assertions were contained in a lengthy investigation by The New York Times. Wal-Mart has said it is investigating the allegations.

The situation involving Wal-Mart, whether it is guilty or innocent, demonstrates the pressures that all retailers are under as they expand overseas, where ways of doing business can differ markedly from the U.S. Corruption can be an easy way to make things happen fast and even government agencies can participate. It ultimately falls to corporate governance at home, by the company's board and top executives, to keep operations on the right track.

Wal-Mart has opened the door to a probe that could turn up violations under the Foreign Corrupt Practices Act, or FCPA, the U.S. law that prohibits paying bribes to foreign government officials, analysts said.

The largest fine under the act was \$1.6 billion paid by Siemens AG (SI, SIE.XE). Other companies that have been fined under FCPA include BAE Systems PLC (BAESY, BA.LN), Halliburton Co. (HAL) and Alcatel-Lucent SA (ALU, ALU.FR).

Under the anti-bribery law, the fine can be twice the benefits received by the company, said **Usha Haley**, a professor of international business and a research associate at the Economic Policy Institute in Washington, D.C. Given the potential benefits to Wal-Mart of the alleged illegal activity, ranging from access to choice real estate to expedited permits and licenses, "I would think fines could at least approach \$1 billion," Haley said. A Wal-Mart spokesman declined to comment.

UBS Investment Research said a lot of settlements under the anti-bribery law are in the range of 1% to 2% of sales. Each 1% of Wal-Mart's sales is \$4.4 billion, or about 77 cents a share in annual per-share earnings. FCPA investigations have taken anywhere from two to six years to be resolved.

Wal-Mart may find things will go easier with regulators if it removes executives who were involved in the alleged bribery or cover-ups, a step that could lead to a more expedited out-of-court settlement with the U.S. Justice Department, analysts said.

But it may not be Wal-Mart that bears the brunt of the payback. Given the company's position as the world's biggest retailer and its \$444 billion in annual sales, "What kind of penalty can you levy that really hurts them," said David Strasser, retail analyst at Janney Capital Markets.

"This is going to probably be more about individuals at Wal-Mart paying the price," Strasser said. "There may be legal issues and career issues for them."

There are also reputational ramifications for Wal-Mart, which in the past has been criticized for allegedly driving small rivals out of business, alleged gender discrimination and unionization issues. Those matters had largely died down recently and the retailer was saying it was on the road back in terms of building sales at its troubled U.S. unit.

While low prices are likely to stay paramount in customers' minds, "It's always bad when you see a company's name in the press for potential criminal activities or civil actions by their executives," said Andrew Stoltmann, principal at Stoltmann Law Offices.

Also, "In [the wake of the FCPA investigation] are sure to follow lawsuits from a variety of government agencies, would-be competitors, and Wal-Mart shareholders," said James Post, a professor with Boston University School of Management. "The company, many of its senior executives, and members of the board of directors all risk civil and criminal litigation."

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