

Comparative Analysis of Business Strategy and Compensation System in the U.S. Retail Industry

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Abstract. With the development of today's world, all kinds of different life products and daily appliances are integrated into people's lives, and the recent boom in the retail industry is noticeable. With the development of the retail industry, this study would like to explore whether management compensation in the retail industry is reasonable. The paper selects three representative companies from countless retail companies to analyze whether their compensation standards are reasonable based on their performance in the industry and how their board compensation has changed over the past five years. The research chooses three representative companies, Costco, Target, and Walmart, listed the performance of their basic salary system in the past five years, and made a simple speculation based on the current situation of the retail industry. The research finds that the three enterprises have made corresponding salary system standards according to their different positions in the industry and, combined with their future development, make more reasonable salary standards.

Keywords: Director compensation, business strategy, compensation, retail industry.

1. Introduction

The retail industry is a fundamental pillar of the modern economy, serving as a pivotal bridge connecting producers and consumers. As this industry continues to evolve within the dynamic sphere of commerce, significant attention has been directed toward the formulation and execution of compensation systems within retail enterprises. This paper conducts a comprehensive analysis of the present status and the trajectory of compensation system development in the retail sector, underscored by a detailed exploration of three prominent retail companies. By delving into both the broader retail landscape and the compensation systems of the selected companies while considering their economic and organizational interplays, this study aims to provide valuable insights into the strategies and trends that underpin effective compensation practices in this ever-progressing field.

2. Overview of the U.S. Retail Industry and Its Representative Companies

The retail industry is a highly competitive, dynamic industry that incorporates a wide variety of products and services. With the conclusion of the COVID-19 pandemic, the retail sector has finally emerged from a difficult period. The global retail market generated more than 27 trillion U.S. dollars in sales in 2022, with an expected increase to more than 30 trillion by 2024. The United States is the largest retail market on the globe, accounting for approximately 26.2% of total retail sales worldwide in 2022. In particular, retail sales in the United States totaled an astounding \$7,096.88 billion, representing an 8.1% increase over the previous year, 2021 [1]. The paper chose Walmart, Costco, and Target because they are the three largest retailers in the United States. These three companies have distinctive business models, strategies, and performance metrics that reflect their prominence and influence in the retail industry.

Walmart is by far the world's largest retailer by revenue and market capitalization, as well as the largest private employer with over 2.2 million employees, due to its strategy of offering everyday low prices on a comprehensive assortment of goods and services. It maintains 10,623 stores in over 20 countries under a variety of banners, in addition to e-commerce websites and mobile applications.

Walmart's total revenue in 2022 was \$572.75 billion, a 2.43 percent increase from the previous year. Walmart reports sales for the U.S., Walmart International, and Sam's Club; the U.S. represents 69% of total sales. Walmart International (17%) and Sam's Club (14% of total revenues) represented the remaining portion [2]. Walmart's net income decreased by 19.0% from the previous year to \$11.29 billion, primarily due to higher operating expenses and income tax expenses. The return on assets (ROA) for Walmart was 5.67%, and the return on equity (ROE) was 17.10% [3].

Costco is the largest warehouse club operator in the United States and the third-largest retailer in the world based on revenue. Costco operates 861 warehouses in 12 countries and e-commerce websites in a number of markets. Costco's strategy is to offer a limited selection of nationally branded and private-label products across a broad range of product categories in order to achieve high sales volumes and rapid inventory turnover. Costco's total revenue in 2022 was 226.95 billion dollars, a 15.83% increase from the previous year. The United States contributed 72.83 percent of its revenue, while Canada contributed 13.96 percent, and other countries contributed 13.21 percent. Costco's net income increased by 16.72% from the prior year to \$5.84 billion, primarily due to higher sales and membership fees. The ROA of Costco was 9.10%, and the ROE was 27.12%.

Target is the seventh-largest retailer in the United States by revenue and one of the country's premier general merchandise retailers. Target maintains over 1,958 stores and an online platform that provides delivery, pickup, and drive-up services in the United States. Target's strategy is to differentiate itself from its rivals by providing a curated selection of exclusive and national brands across various product categories and augmenting its digital capabilities and fulfillment services. In 2022, Target's total revenue increased by 2.97 percent from the previous year to \$109.12 billion. Other revenue (primarily from credit card operations) contributed 3% to the company's total revenue. Target's net income decreased by 59.98% from the prior year to \$2.78 billion, primarily due to increased merchandise costs, supply chain expenses, and inventory attrition. The ROA for Target was 6.30%, and the ROE was 29.43%.

In a nutshell, Walmart is the undisputed leader in the global and U.S. retail markets due to its enormous magnitude, scope, and market share. With a large membership base and high sales volume, Costco is the dominant participant in the warehouse club segment. Target is a distinguished retailer of general merchandise that focuses on offering exclusive and national brands and enhancing its digital and fulfillment capabilities.

3. Compensation and Development of Representative Companies

3.1. Compensation System

This study selects three representative companies in the U.S. retail industry, Target, Walmart, and Costco, to speculate and analyze the relationship between the compensation system of the U.S. retail industry and the development of the retail industry. Target takes control of 1.2% of the whole U.S. retail market; Walmart occupies 2% of the world's retail market and 6.6% within the U.S.; Costco controls 13.1% of the retail market in the U.S. At the same time, it is believed that the different operating models between these three companies can cover most of the retail industry stores in the United States, which is more representative and referenceable. Target and Walmart do not require membership for customers to shop in their stores, while Costco operates on a membership-based model, where customers pay an annual fee for access to its store and exclusive discounts. Another main difference between them is the different pricing strategies. Target offers a mix of branded and private-label products, often at a competitive price. Walmart is known for "Everyday Low Prices," which will offer a low price for a wide range of products. Costco focuses on selling products in bulk, aiming to provide value to its members through lower per-unit prices. Undoubtedly, each of them is a successful company and a reasonable sample for us to use in the paper. The following data will introduce the director compensation of each company within the past five years.

Walmart has the most complicated director compensation system of the three companies. They offer each of their directors an annual cash grant of \$175,000 from 2018 to 2022 with no change.

Furthermore, they offered their directors a cash retainer of \$90,000 in 2018 and \$100,000 from 2019 to 2022. Also, they offered their Non-Executive Chairman another cash retainer of \$200,000 in 2018 and \$225,000 from 2019 to 2022. Lead Independent Director can get an additional cash retainer of \$30,000 in 2018 and \$35,000 from 2019 to 2022. The cash retainer increased by 11.11% in the past five years [4].

Costco has a similar director compensation system. It separates the payment into two parts: stock awards and cash retainers. Costco offers its director \$270,000 in stock awards from 2018 to 2022 and a \$30,000 cash retainer from 2018 to 2021. The cash retainer increased 23.33% from \$ 30,000 to \$37,000 in 2022. Moreover, Costco offers each of its directors \$1,000 meeting fees for each meeting they attend [5].

Finally, Target allows its directors to choose whether to be paid by cash and RSU or RSU only. In 2018, they will receive a \$90,000 cash retainer, which increased to \$100,00 in 2019 and then to \$115,000 in 2021. The RSU they can get is \$170,000 in 2018 and increased to \$180,000 in 2019, and they maintain this number until 2022. If their directors choose to be paid by RSU only, they will receive \$260,000 in 2018, \$280,000 in 2019 and 2020, and \$295,000 in 2021 and 2022 [6]. They can get the total amount of the first payment method. The increased rate of the total payments each director might gain is 13.5% in the past five years.

3.2. The Nexus Between Compensation System and Corporate Performance

The company's scale and global influence are reflected in the pay scheme. The increased financial retainer implies that the board's significance and responsibilities are recognized in light of Walmart's continuous development.

The remuneration scheme may incentivize directors to contribute to the company's market share and worldwide presence by maintaining and developing its market share and global presence. Pay and benefits are a combination of a pay system that is a bundle of incentives from the business and an employee who receives the rewards from the organization [7].

Compensation is a type of incentive that a company provides to directors and employees in both financial and non-financial extrinsic forms for the time, professional knowledge, and contributions made by them to meet work requirements aimed at achieving organizational goals. In previous data, the compensation of Walmart has been on the rise, which can be seen as the attraction of Walmart for directors is gradually increasing, and directors are also encouraged to make more significant contributions to the operation of the company. In Walmart's most recent quarterly report for 2023, 10Q, Walmart Inc.'s total revenues, which include membership and other income in addition to net sales, grew \$10.7 billion or 7.6% [8]. The three months ending April 30, 2023, compared to the same time in the previous fiscal year.

The company's development trend aligns with the compensation system, and the number of Walmart stores has been stable. As Figure 1 shows, although the number of stores declined after 2021, this was due to the termination of Walmart's operations in the United Kingdom and Japan in the first quarter of fiscal 2022. As of January 31, 2023, Walmart had 10,623 retail shops worldwide. In addition, the firm had 380 distribution centers. Walmart had a total of 11,003 stores [9].

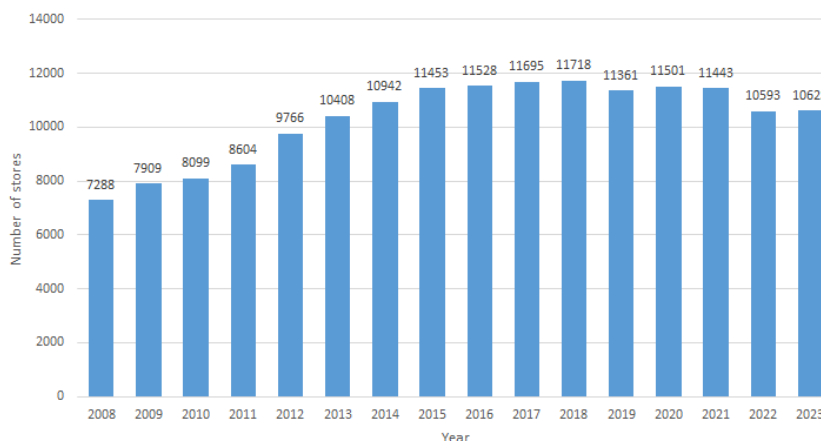


Figure 1. Number of Walmart stores worldwide from 2008-2023 [9]

Costco's pay scheme comprises stock awards, cash retainers, and meeting fees. The cash retainer climbed by 23.33% during five years, showing the company's performance and financial stability. Costco controls 13.1% of the US retail market. The remuneration strategy, which includes stock awards, is anticipated to motivate directors to focus on long-term value creation and sustained profitability, which aligns with Costco's bulk-focused business model. Meeting fees give an extra incentive for directors to actively engage in and contribute to the company's strategy. Yermack discovers statistically substantial evidence that outside directors enjoy favorable performance incentives from remuneration, turnover, and the opportunity to seek new board seats (2014). These incentives, when combined, reward outside directors in their fifth year with wealth gains of around 11 cents for every \$1,000 growth in business value. This equates to a \$285,000 change in director wealth for every one standard deviation (SD) difference in the performance of the median sample business [10]. Target's unique pay system, which allows directors to select between cash and Restricted Stock Units (RSU), not only distinguishes it but also correctly corresponds with the company's development trajectory, industry standing, market share, and profitability targets. Target demonstrates its commitment to building a boardroom climate that appreciates individual viewpoints as well as financial objectives by allowing directors to choose their preferred remuneration model.

This customized strategy demonstrates Target's knowledge that directors' objectives and risk tolerances vary. Furthermore, this adaptability is highly aligned with the retail industry's ever-changing market, where adaptation and customized tactics are critical for long-term development. Target's 1.2% market share demonstrates the connection of this remuneration scheme with industry position. Target's strategic choice to empower directors to personalize their remuneration underlines the company's adaptability and concentration on attracting and maintaining top-tier people who can assist in leading its focused strategy to success in a field dominated by larger rivals.

In conclusion, while the pay plans of the three businesses varied, they all appear to be in line with their respective industry rankings. Walmart's extensive pay system may reflect the company's size and complexity as a worldwide retailing behemoth, and its significant market dominance and global presence are critical factors in its consistent and generous remuneration, with an emphasis on cash. Costco's emphasis on stock awards may represent a dedication to long-term wealth generation, which is consistent with its bulk sales strategy. Its significant market share in the United States may be motivating its generous stock awards and cash retainers to keep directors motivated to maintain the company's success. Finally, Target's flexible pay structure may be a tactic to recruit directors who understand and can contribute to the company's distinct market positioning. Although Target's market share is decreasing, it may explain its remuneration strategy, which offers flexibility and incentives to experienced directors.

4. Conclusion

On the basis of the analysis of key metrics such as revenue growth, profitability, market share percentage, customer acquisition costs, and employee turnover, the study determines that Walmart has the most complex and generous compensation system of the three companies, which may be appropriate given its size and complexity as a global retail giant. However, the study have also suggested that Walmart may need to modify its compensation system in order to reduce its operating expenses and income tax expenses, which have adversely impacted its net income and profitability. Costco has a straightforward and consistent compensation system that emphasizes stock awards and cash retainers, which may be suitable for its membership-based business model and volume sales strategy. To attract and retain more consumers and employees, Costco may need to diversify its compensation system to include more performance-based incentives and benefits. Last is Target. This company's compensation system is unique and flexible, allowing directors to choose between cash and restricted stock units (RSU), which may be suitable for its differentiated market positioning and exclusive brand offerings. Nonetheless, the study have also suggested that Target may need to increase its compensation system to align with industry standards and benchmarks, which could assist it in competing with larger competitors and expanding its market share.

Authors Contribution

All the authors contributed equally and their names were listed in alphabetical order.

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