Q4 2022 Earnings Call

Company Participants

- Richard A. Galanti, Executive Vice President and Chief Financial Officer
- Unidentified Speaker

Other Participants

- Brandon Cheatham
- Chuck Grom
- Greg Melich
- John Heinbockel
- Kelly Bania
- Oliver Chen
- Peter Benedict
- Robert Ohmes
- Rupesh Parikh
- Scot Ciccarelli
- Simeon Gutman

Presentation

Operator

Thank you for standing by, and welcome to Costco's Fourth Quarter Fiscal 2022 Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speaker presentation, there will be a question-and-answer session. (Operator Instructions)

I would now like to hand the call over to CFO, Richard Galanti. Please go ahead.

Richard A. Galanti {BIO 1423613 <GO>}

Thank you, Latif, and good afternoon to everyone. I'll start by stating that these discussions will include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, and these statements involve risks and uncertainties that may cause actual events, results, and our performance to differ materially from those indicated by such statements. The risks and uncertainties include, but are not limited to those outlined in today's call, as well as other risks identified from time to time in the company's public statements and reports filed with the SEC. Forward-looking statements speak only as of the date they are made, and the company does not undertake to update these statements, except as required by law.

In today's press release, we reported operating results for the fourth quarter of fiscal 2022, the 16 weeks ended this past August 28. Net income for the quarter was $1.868 billion or $4.20 per diluted share compared to $1.67 billion or $3.76 per diluted share a year ago.

Last year's fourth quarter was negatively impacted by an asset write-off of $84 million pre-tax or $0.14 per diluted share. Net income for the fiscal year totaled $5.84 billion or $13.14 a share compared to $5.01 -- $5.01 billion or $11.27 per diluted share the prior fiscal year. Net sales for the fourth quarter increased 15.2% to $70.76 billion as compared to $61.44 billion reported last year in the fourth quarter.

On a comparable sales basis from the fourth quarter, U.S. for the 16-week period on a reported basis had comp sales of 15.8% when you exclude gas inflation and FX or we wouldn't be in a FX gas inflation, it'd be 9.6%; Canada 13.4% reported, 13.7% ex-gas and FX; other international, 2.9% reported, and 11.3% ex-gas and FX. So, also total company was a reported as 13.7%, and excluding gas and FX plus 10.4%, separately e-commerce 7.1% reported, and again excluding FX 8.4%.

In terms of the Q4 comp sales metrics, traffic or shopping frequency increased 7.2% worldwide and up 5.2% in the U.S. Our average transaction or ticket was up 6.0% worldwide and up 10.0% in the U.S. during the fourth quarter. Foreign currencies relative to U.S. dollar negatively impacted sales by a little over 2% and gasoline price inflation positively impacted sales by approximately 5.5%.

The best performance in the quarter -- the best performing core categories in the quarter were candy, frozen, kiosks, tire, lawn and garden, jewelry, toys, bakery, and deli. In terms of ancillary businesses, the best performers were gas and food courts; and in other businesses, travel and business centers performed best relative to the prior fiscal fourth quarter results.

Going down the income statement to membership fee income, on a reported basis, our membership fee income came in at $1.327 billion or 1.88%, that was up $93 million or 7.5% on a reported basis, again with weaker foreign currencies relative to the U.S. dollar. That number excluding the impact of FX would have been $29.8 million higher than the 7.5% reported increase would have been a 10% increase.

In terms of renewal rates, we again hit all-time highs. At Q4 end, our U.S. and Canada renewal rate came in at 92.6%, which is three-tenths of a percentage point higher from 16 weeks earlier Q3 end when we were at 92.3%. And -- our worldwide renewal rate came in at the end of the fiscal year at 90.4%, up four-tenths of a percentage point from Q3 end when it was 90.0%.

In terms of the number of member households and cardholders, at Q4 end, we ended the fourth quarter with 65.8 million paid household members and 118.9 million cardholders, both up 6.5% from a year earlier. And that's 6.5% increase in member of members and cardholders is on a -- about a just under 3% increase in the number of locations. During the year, we opened 23 locations on a base that began the year with 815 warehouses.

At Q4 end, our paid executive memberships totaled 29.1 million, an increase of 1.2 million or 74,000 per week during the 16 weeks since third quarter end. Executive members now represent over 44% of our members and just under 72% of our worldwide sales.

In terms of membership fees and a possible increase, there are no specific plans regarding a fee increase at this time. We're pleased with our growth in both, top line sales and membership households over the last several quarters, and member loyalty is reflected in increasing member renewal rates. We'll let you know when something is about to happen.

Moving on to fourth quarter gross margins; for the quarter, gross margin on a reported basis came in at 10.18% compared -- down 74 basis points from last year's reported gross margin of 10.92%. Now the 74% -- the 74 basis-point year-over-year reduction is on a reported basis. Excluding gas inflation, it was minus 22 basis points. And as we normally do, we actually jot down a few numbers, and then we'll elaborate a little bit more on margin. So, the two columns would be reported year-over-year change and the second one would be ex-gas inflation, net year-over-year change.

So, the core merchandise margin on a reported basis, minus 67 basis points year-over-year; ex-gas inflation, minus 23 basis points; ancillary and other businesses, the second line item, plus 20 and plus 34; our 2% reward, 0 and minus 5; LIFO, minus 27 and minus 28; and all told, total minus 74 reported as I mentioned and minus 22 on -- excluding gas inflation basis.

Starting with the core; core merchandise's contribution to gross margin was lower by 67 basis points year-over-year and by 23 ex-gas inflation. The sales mix negatively impacted the core, primarily from the lower sales penetration of total core sales relative to our increasing and outsized gasoline sales.

In terms of the core margin on their own sales, in Q4, our core and core margins were lower by 26 basis points. That's pretty much in line with each of the last three quarters when it ranged from minus 39 basis points year-over-year in Q3, minus 28 in Q2 and minus 18 in Q1 on a year-over-year basis. So, again, for the quarter, it was minus 26 quarter-on-quarter.

Ancillary and other businesses gross margin was higher by 20 basis points and higher by 34 basis points ex-gas-inflation in the quarter. Gas, of course, as well as business centers and travel were better year-over-year, offset somewhat by e-com, pharmacy, food court and optical, but overall, a positive year-over-year change.

Our 2% reward, as I mentioned, on an ex-gas inflation basis was higher or down 5 -- lower or down 5 basis points, implying higher sales penetration coming from our executive members.

In terms of LIFO -- LIFO, as you know, with inflation has been increasing. It was 27 basis points, down year-over-year -- or higher year-over-year. LIFO charge this year on an ex-gas inflation basis, 28 basis points higher, and that represented a $223 million charge in the quarter. Recall that our LIFO charges were relatively small in the first part of the year at $14 million; last quarter, in the third quarter, $130 million; and then as I mentioned here, $223 million for the quarter.

Moving to SG&A, we showed good results. Reported SG&A came in at 8.53% compared to last year's 9.22% or an improvement of 69 basis points. But again, ex-gas inflation, the improvement was still good at 26 basis points lower year-over-year.

Again, charting down a few numbers here, charting down the numbers on a core operations basis, on a reported basis, that was plus 50 basis points or positive reduction of 50 improvement; ex-gas inflation, plus 12 basis points; central, plus 2 and minus 3; stock compensation, plus 2 and plus 1; preopening expense, plus 1 and plus 2; other, plus 14 and plus 14. That gets you down to again on a reported basis, year-over-year SG&A was improved by 69 basis points; and ex-gas inflation by 26 basis points.

In terms of the quarter year-over-year, the core operations was, again, better by 12, excluding the impact of gas inflation. Keep in mind, these results include the starting wage increases we instituted in October of 2021, so in the first quarter of this fiscal year -- this past fiscal year, as well as new wage and benefits increases implemented during the third quarter in March of this year as well as the impact of 8 weeks in this quarter as we increase the top-of-scale increase that went into effect July 4th. So, a few increases that we've done this year. And still, we feel pretty good SG&A improvement given our sales strength.

Central was lower by 2 basis points and higher by 3 basis points ex-gas inflation. Nothing big to talk about there. Again, stock compensation I mentioned. Preopening, I've just -- we've noted that since we now include preopening on the income statement as part of SG&A instead of a separate line item. And other, again, the 14 basis points, recall that that included that last year's write-off in the quarter, totaling $84 million. All told, reported operating income in the fourth quarter increased 10%, coming in at $2.497 billion, a little of that benefit was that asset write-off last year.

Below the operating income line, interest expense was $48 million this year versus $52 million last year, relatively similar. Interest income and other for the quarter was lower by $1 million year-over-year, coming in at $67 million this year versus $68 million last year. Interest income was actually higher, but that was offset by unfavorable FX impact, which pretty much offset each other to be roughly flat year-over-year. Overall, reported pretax income was up 10%, coming in at $2.516 billion this year, up from $2.291 billion a year earlier.

In terms of income taxes, our tax rate for the fourth quarter was 25.4% compared to 26.1% in Q4 last year. The fiscal '23 effective tax rate, we estimate, is currently projected to be approximately 26%.

Net -- one thing I'll mention, we haven't mentioned in the past, net income attributable to Costco, that line item was up 12%. Recall that on June 30th this past year, we acquired the 45% minority interest from our JV partner in Taiwan. So, we now own all of Costco Taiwan. As a result, net income attributable to non-controlling interest was better by $14 million in the quarter. The non-controlling interest line will become zero going forward, essentially, a small amount, but pretty much zero.

A few other items of note in terms of warehouse expansion. In the fourth quarter, we opened 9 net new warehouses. So, for the full year, we opened 26 warehouses, but that included 3 relocations, so a net increase during the year of 23 locations. In the fourth quarter of the 9 we opened, 5 were in the U.S., 2 were in Canada and 1 each in Korea and Japan. In fiscal '23, we expect to open 29 new warehouses, including 4 relos, so for a net of 25 new warehouses. These 25 planned net new openings are made up of 15 in the U.S. and 10 in other international, including our first locations in each of New Zealand and Sweden, and our third and fourth locations in China.

Regarding capital expenditures, our fourth quarter Q4 spending CapEx was approximately $1.26 billion. And for the full year, CapEx expenditures was $3.9 billion. Our estimate for the upcoming year fiscal '23 CapEx to be approximately the same in the $3.8 billion to $4 billion range.

In terms of e-commerce business, e-com sales in the fourth quarter ex-FX increased 8.4%. Stronger departments in terms of year-over-year percentage increases were tires, lawn, patio and garden, prescription pharmacy and health and beauty aids. The largest e-com merchandise department in dollars, what we call majors, which includes everything from computers to appliances to TVs to audio, et cetera, was up in the high single digits. And Costco Grocery, including our third-party delivery, two-day dry, fresh and frozen, continue to grow. They were up 20% in the quarter.

An update on Costco Logistics; with Costco Logistics, we continue to transition from vendor drop ship to direct ship from our own inventory, particularly in big and bulky items. Overall, this lowers the cost of the merchandise and improves delivery times on service levels to our members, and I'll share with you some statistics to that in a minute.

Prior to this acquisition in the U.S., we were completing a few years ago about 2 million big and bulky deliveries and installations per year. In fiscal '22, we completed 4.3 million big and bulky deliveries and installation. Previously, all of those 2 million deliveries and installations were made by third parties. In fiscal '22, about 70% or a little over 3 million of the 4.3 million were done by us. In the fourth quarter, in fact, that percentage of deliveries and installations done by -- performed by us was 81%.

Pre-acquisition, the estimated average days to deliver was above 15 days, and we were working with over 100 delivery partners. Today, our average delivery time for big and bulky is just under 5 days, and we're continuing to work to improve that. And we were down to 8 delivery -- primary delivery partners.

A few comments regarding inflation. We've seen minor improvement in a few areas. But all in, pressures from higher commodity prices, higher wages and higher transportation costs and supply chain disruptions. They're still present, but we are seeing just a little light at the end of the tunnel. And if you recall in the third quarter, we indicated that price inflation overall was about 7% plus for us. For the fourth quarter and talking with our merchants, the estimated price inflation overall was about 8%, a little higher on the food and sundry side, a little lower on fresh foods, and both higher and lower on the nonfood side.

We're seeing commodities -- some commodities prices coming down, such as gas, steel, beef, relative to a year ago, even some small cost changes in plastics. We're seeing some relief on container pricing. Wages are still the higher thing when we talk to our suppliers. And as we all know, wages still seem to be the one thing that's still relatively higher. But overall, some beginnings, some light at the end of that tunnel. And of course, that could change each week.

In all, despite current inflation levels, we believe we continue to remain competitive versus others and able to raise prices as cost increases, hopefully, of course, a little less than others with who we compete.

Many of you have asked about private label with the recent inflationary environment and what's happening, are people trading down. And of course, our first response, of course, is they're not trading down. They're trading up or certainly trading the same.

In terms of Kirkland Signature merchandise penetration, and excluding gas and other businesses that carry the Kirkland name. Kirkland Signature merchandise is up just under 1% in terms of penetration compared to a year ago. Our KS merchandise penetration is about 28% for the year. This is similar to historical trends where it's increasing slowly and steadily over time. So, no big dramatic change from the past there.

In terms of supply chain; generally, supply chain has improved a little, including on-time deliveries. We started seeing container prices coming down. First place you see it, of course, is in the spot market and then you'll start to see it hopefully in some other contracts as they continue. No longer any big capacity issues or container shortages. Domestically, port delays have improved. And while the rail strike that was in the news a few weeks ago was thankfully averted. In anticipation of strike, there were some rail ramp closures and delays in restarting that. But the view from our buyers is that this should be eliminated for the most part towards the end of this week.

Switching over to inventory levels; our total inventory at Q4 end was up year-over-year, just -- was up just under 26% year-over-year. At the end of the third quarter, it was up just over 26%. Of the 26% increase, an estimated 10 to 11 percentage points of it is inflation. That's that 8% number. And new warehouse growth, that's that 3% number in terms of unit growth over the last year, but still up year-over-year.

Additionally, we're lapping some low stocks in certain departments as a result of last year's high demand, specifically in nonfood areas, where last year we were about 90% of our targeted inventory levels. Food and sundries and fresh are in good shape, we feel. Our week supply is comparable year-over-year.

In terms of nonfood inventories, it's up in certain categories. Again, this is in part a result of being light in certain departments last year as mentioned earlier. The good news so far, initial seasonal sales seem to be going well as evidenced in our monthly sales reports.

And all told, we would expect the 26% year-over-year increase to start to head down as it has in just the past few weeks a little bit.

Lastly, as a reminder, in terms of upcoming releases, we will announce our September sales results for the five weeks ending Sunday, October 2nd, this next week on Wednesday -- in two weeks, on Wednesday, October 5th, after the market closes.

With that, I will open it up to questions-and-answers with Latif. Thanks.

Questions And Answers

Operator

(Question And Answer)

(Operator Instructions). Our first question comes from the line of Simeon Gutman, Morgan Stanley. Your line is open. Please go ahead, Simeon Gutman.

Q - Simeon Gutman {BIO 7528320 <GO>}

Good afternoon, everyone. Richard, I want to ask a couple of questions about membership fees. So, first of all, if -- you said you were comfortable with sales. So, I'm questioning if your tentative -- you're worried about the sales rate if you raise it. And then, is it fair if you don't raise it? It means you're also comfortable with the rate of EBIT growth in the business, because there's been a tool for the business over time. And I know you don't guide, but I'm obviously trying to get you to answer that.

A - Richard A. Galanti {BIO 1423613 <GO>}

Sure. Well, nice try. No, look, at the end of the day, we've always been told and we've told you guys that we're a top line company. We're looking to always drive sales. Certainly, as we've increased member fees historically about every 5, 5.5 years, we've turned around and used it to drive more value; and whenever we do it, we'll do that.

I think at the end of the day, it's -- and I also want to point out, of course, if you look at the last three increases, on average, they were 5 years and 7 months apart. If you look at June of '17, plus 5 years and 7 months, you're talking roughly January '23. Now, I'm not suggesting it's January '23. I'm just saying it's not there yet anyway. And our view is, is we are confident in our ability to do so and at some point, we will. But it's a question of when, not if.

And given the headline of inflation and concerns about recession, we feel quite comfortable driving sales and earnings the way we are right now. And we still have that arrow in our quiver as we go forward.

Q - Simeon Gutman {BIO 7528320 <GO>}

And then, maybe the follow-up, same topic, still. The way -- your new fiscal year, you've obviously planned a year. Do you cut back or you curtail spending or investments in any way that runs through the P&L if you're not planning to do it or if you are planning to do it?

A - Richard A. Galanti {BIO 1423613 <GO>}

Not at all. I mean, it's steady as she goes in terms of CapEx and what we want to do, and what we want to do with pricing and competitive pricing. And we're not the only company out there, but as we've seen some slight declines in reported gross margin not only this quarter, but in the last several quarters, part of that was just the upsized improvement in margin during the first year of COVID. But we are not -- as you know, we're not shy about doing what we have to do to drive the top line, and we'll continue to do that.

Q - Simeon Gutman {BIO 7528320 <GO>}

Thanks, guys. Good luck.

Operator

Thank you. Our next question comes from the line of Rupesh Parikh of Oppenheimer. Your line is open. Please go ahead, please, Rupesh Parikh.

Q - Rupesh Parikh {BIO 22151706 <GO>}

Thanks for taking my question. So, Richard, I guess just going back to your expense commentary, there was a sequential pickup in your expense growth versus Q3. Besides the wage increases, was there anything else that was unique to the quarter that you'd call out?

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, other than it was -- it was 16 weeks versus 12 weeks, but are you talking about on a year-over-year basis?

Q - Rupesh Parikh {BIO 22151706 <GO>}

Yes. Year-over-year. Yes. I think it's --

A - Richard A. Galanti {BIO 1423613 <GO>}

I think the outsized thing is just that. I mean, are utilities costs up? Sure. But the outsized thing would be the wage increases. But I'm sure IT is up -- IT is always up a little more as everybody is doing more technology-wise.

Q - Rupesh Parikh {BIO 22151706 <GO>}

Okay. Great. And then just on the health of the consumer, just given many concerns out there, anything to know, like any change in consumer behavior or even in your majors category, are you guys seeing any changes versus maybe your expectations there?

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, I think I mentioned -- or we've mentioned when we've talked to some of you over the various months was there -- when beef prices skyrocketed, now they're coming down versus a year ago, but when they skyrocket, you see a change. And irrespective of the state of the economy, you see some changes from beef up to poultry and those examples. Somebody made -- one of the buyers had made a comment a few months ago that they saw some increased penetration of canned chicken and tuna for that reason. But at the end of the day, we haven't seen any big changes in that. Part of it is hard to see, because we -- during these two years of COVID, we enjoyed such strength in big ticket items. And if -- like consumer electronics, if it's up a little versus up a lot the last two years, incrementally, we know in each of those cases, our numbers relative to industries comparisons are still -- we're still beating the rest of the industry in terms of sales growth.

Is the sales growth is slower than it was last year? Yes. It still has a positive plus in front of it, and it's still better than the industry as a whole.

Q - Rupesh Parikh {BIO 22151706 <GO>}

Great. Thank you. I'll pass it along.

Operator

Thank you. Our next question comes from Chuck Grom of Gordon Haskett. Your line is open, please go ahead, Chuck Grom. Chuck Grom, your line is open.

Q - Chuck Grom {BIO 3937478 <GO>}

Hey. Thanks. Sorry about that. Richard, on the core-on-core three-year -- on a three-year basis, it looks like you guys showed a nice improvement from the last quarter. Can you unpack that for us a little bit across the four major categories?

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, I don't have all that detail in front of me. But generally speaking, the thing that was outsized in the biggest way in the first year or so of COVID was fresh. As you'll recall, with fresh, you had virtually no spoilage, and you had much higher labor productivity. So, you had huge -- you had 3-digit improvements in margins there. So, that's the comparison. And we've talked about that in the last several quarters on a year-over-year basis compared to those two years, it's come down as a percent, still up from where it was pre-COVID.

Other than that, there's all kinds of things that impact other departments. At the extreme, you have a small business, but in terms of our income statement, travel. Travel is almost a brokerage business, where it's all margin -- a lot of it is margin. And that went way down, and now it's improving from where -- it's gone way down. So that helps you a little bit, but there's a lot of moving parts to that.

I think fresh was the biggest outlier. Then during supply chain things and everything else, there were impacts in certain departments or allocations, things like that. There was less -- I'm just shooting from the hip here. There was less promotional activity in consumer electronics because of shortages of chips or electronics. And so, there's a lot of puts and takes. But overall, I would say fresh was the one that was most meaningful in that regard.

Q - Chuck Grom {BIO 3937478 <GO>}

Okay. Good. Thank you very much. And then on the LIFO charge, 28 basis points, I think you said last quarter, it was 25. I guess, I was surprised that it wasn't higher given how much prices have moved up over the past 3 to 4 months. Can you just maybe just give us a refresh on the accounting for that? And what happens in the coming quarters as we start to lap the big charges from this year?

A - Richard A. Galanti {BIO 1423613 <GO>}

Sure. Well, two things. Again, if you look sequentially in Q1, it was sub-$20 million; in Q2, it was sub-$40 million -- $30 million something, then $100 million something, then $200 million something. Part of that is, is -- the way we account for it is, at the end of the Q1, when we saw what the trend was, you then estimate what you believe it's going to be for the year, and pro rate a quarter of that or 12 weeks of that to that quarter. And that as it continues to increase, you -- adjusted on a year-to-date basis. So, that skews that a little bit. That's the way we've done it historically in prior inflationary times.

The other comment you asked about is it seemed like it'd be even higher in Q4. The fact is, is we, too, thought halfway through the quarter, it would be higher than this. Part of that was if I bifurcated Q4 into the first 8 weeks and the second 8 weeks, the first 8 weeks showed a level of increase that would have required a larger LIFO charge. It seemed to, in some cases, flatten out a little bit during the last several weeks of the quarter, which meant that it came down from what our expectation was.

So, again, I think that is consistent with I mentioned about we're seeing a little light at the end of the tunnel. I'm not just -- and there's little -- some of the buyers about a couple of items going down in price. And you can rest assured that our partners are calling the suppliers. As you said, the price went up because of steel prices, well, steel prices are down; what gives? And so, we'll continue to do that, but it's a slow road. And -- but we are, again, seeing a little bit of improvement at least in the second half of the fourth quarter and we'll see where it goes from here.

Q - Chuck Grom {BIO 3937478 <GO>}

Okay. Thanks very much.

Operator

Thank you. Our next question comes from Paul Lejuez of Citi. Your line is open. Please go ahead, Paul Lejuez.

Q - Brandon Cheatham

-- Cheatham on for Paul. Thanks for taking our question. I wanted to dig in on the inventory piece a little bit, up about 26%. How much of that is you categorize as general merch? You had some pretty big competitors that have been trying to clear some of their general merch as I'm sure everyone knows. So, as you kind of reach holiday, can you give us a sense of where you are for general merch inventory? Any plans to kind of further discount there to try and get leaner? Thanks.

A - Richard A. Galanti {BIO 1423613 <GO>}

Sure. Well, first of all, without being too specific, there's a decent chunk in there that I would call deep freeze from last year. My example I've used when talking to people is the Christmas trees that retail for $150 to $400. And they came in after Christmas or essentially after Christmas. And the good news is that they don't really change in style. And they're now -- and if you go to Costco, you're going to see them on the floor. And the -- if you add in the cost of holding them and a little cost of interest, I think they're still a little cheaper than the ones we added to the inventory this year. So, in a perverse way, that one didn't hurt us that example other than we don't like to have extra inventory. And so, there are some seasonal things that came in late. Probably a bigger piece of the delta is us building up inventory, particularly on big and bulky and fulfillment -- both e-com fulfillment and big and bulky.

The last part is early holiday. We did consciously bring in some stuff. Part of it was not knowing what was happening with supply chain and how many weeks of delay at each item was. We bought stuff in consciously a little early. And then as I mentioned, supply chain has improved a little. That's helped you. So, again, there's things that have helped it and hurt it -- increased it or reduced it.

The other thing that's increased a little bit, even some things like seasonal things like air conditioning and fans, which was -- we had a very strong season, but there were some delays in getting that stuff in. That will be a small impact from a seasonal standpoint going forward. But net-net, I think that while the 26% number was relatively same at year-over-year Q3 end -- Q3 year-over-year and at Q4 end, again, in talking with Ron and Claudine and the merchants, and again, seeing what we've seen just in the last 2 or 3 weeks, it's going in the right direction and nobody likes it.

I think that one other difference is that -- compared to some of the other bigger retailers, our inventory is more specific. Like if we get a lot of -- if we have a bunch of air conditioners or a bunch of furniture, it's -- we may have to hold on to it, but it's not a whole variety of different things. And so, we -- while we have had some additional markdowns, nothing huge -- no big outsized numbers relative to what we would normally expect. So, a little bit increase, but nothing material.

Q - Brandon Cheatham

Got you. And so, you're bringing holiday up a little earlier than you otherwise would. And some of that more seasonal air conditioners and fans you mentioned, you might hold those over to spring time? Is that right?

A - Richard A. Galanti {BIO 1423613 <GO>}

We will. Yes. That's easy. And the good news, again, call it, lucky, 2.5 years ago when we acquired Innovel, which is we call Costco Logistics, we added 10 -- or 20 million square feet between the MDOs and DCs, but added 10 million of big space, the million square foot space to the roughly 10 million or 12 million of depot space we have. So, we were -- that was fortuitous in that regard.

Q - Brandon Cheatham

Understood. Thank you.

Operator

Thank you. Our next question comes from Kelly Bania of BMO Capital Markets. Your question, please, Kelly Bania.

Q - Kelly Bania {BIO 16685675 <GO>}

Hi. Thanks. Kelly Bania from BMO. Richard, just wanted to touch on executive penetration. Line item continues to impress. I think it's the biggest quarterly jump in the model that I can see. But I guess my question is as you look at that kind of cohort of Gold Star customers today, is there anything different about that customer profile, demographics or otherwise that makes you can't -- makes you think you can't have the same success in converting those customers up to executive over time?

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, I think -- we think we will. I mean what used to be asked -- the question that used to be asked about millennials or Gen X and then millennials and the Gen Z, we tend to see the same type of trends that are age and arguably, income-dependent. Also, during these last several years, we've continued to get better at talking you into signing up -- selling you on the value of that executive member upfront. So, we've seen increased penetration there, too.

The other thing, of course, that helps is when we add it to a new country, I think in the past 2 years, we added it to Japan and Korea. And so, we have it, of course, in the U.S., Mexico, Canada, and the UK. And so, we've already gotten the big countries, if you will, in terms of number of locations. And I'm sure there'll be another country too, we add it to over time as those countries grow. So, no, I think we've done a better job of doing it, starting with. Years ago, you came in and we asked you what you wanted and if you said Gold Star, that's what you got. Now we actually try to share with you what's the value of it, and we've done a better job with that.

Q - Kelly Bania {BIO 16685675 <GO>}

And just to maybe follow up on the container pricing, I think you mentioned maybe some relief starting there. I guess the question is just, have you learned anything about your business over the past few years, really kind of focusing on discretionary imports and the strategy, the charter ships that you might keep longer term, or do you expect to kind of go back to kind of everything you were doing pre-pandemic from that perspective?

A - Richard A. Galanti {BIO 1423613 <GO>}

I think the biggest thing we've learned is that really from the source of origin of these items. If you go back to even when tariffs were placed in whatever '16 or '17 or whenever that was on China, and there were certain items that were moved from manufacturers in China, those same manufacturers, who may have had facilities in other neighboring countries. Where we could and where they could, that was moved to get around some of those tariffs. And so, you learn through that process.

We certainly learned through the last couple of years the challenges with containers, not to say that we can change some of it. But I think we try to -- to the extent you can, you try to spread it out a little more. You try to not depend on one port. And certainly, we've learned all those things. And we learned that we can continue to make mistakes along the way too.

Q - Kelly Bania {BIO 16685675 <GO>}

Thank you.

Operator

Thank you. Our next question comes from Oliver Chen of Cowen. Please go ahead, Oliver Chen.

Q - Oliver Chen {BIO 15320650 <GO>}

The industry is seeing so much inventory and the wrong kind of inventory. What are your thoughts on the promotions that you're seeing? And how you're thinking about pricing? And any thoughts on the nature of your portfolio? You always offer such sharp prices. On inflation at the end of the tunnel, second, Richard, maybe you could elaborate on that. That sounds very nice.

And lastly, on --

A - Richard A. Galanti {BIO 1423613 <GO>}

Hold on. Hold on. Let's do one question at a time, so I don't forget.

Yes. Supply becomes more plentiful. There's more promotions. I remember last year or the last couple of years, again, given shortages in electronics, we saw -- we and the industry saw a lot less promotional activity being afforded retailers from the manufacturers on TVs. There was no need to do that. And we're starting to see some of those promotional activities come back.

Other than that, also, one of the things that we like is our multi-vendor mailer, both the existing one as well as other promotional things, we do like that online and direct. And those had to be changed in some ways because of shortages or allocations of inventory.

A lot of times in those types of MVMs, you've got a lot of high items like promotional things like TVs as well as huge high sales volume items like paper goods and things like that. And you're looking at the paper goods as well. There were shortage of those along the way. So, we've learned how to change those and maximize them in the ways -- in the best ways we can and figure out how to use those monies -- work with the vendors as well, the suppliers to figure out how to use that money in the best way. And we -- that's again an iterative evolving process.

Second question?

Q - Oliver Chen {BIO 15320650 <GO>}

Okay. Yes. On inflation, just light at the end of the tunnel and some green shoots there that you're seeing.

A - Richard A. Galanti {BIO 1423613 <GO>}

Yes. Well, again, anecdotally, when we talked to the buyers, they're starting to see a few examples, whether it's something like outdoor, patio, furniture or barbecue grill where steel prices are coming down, and we're reminded by Craig and Ron or the buyers reminded at the budget meeting when prices were going up, make sure you understand why they're going up. Is it -- what piece of it is raw material costs? What piece of it is freight costs? And when these things come down, you better be on the phone with them calling them saying, when are we going to get a reduction.

And so I think in part because of our limited selection -- our limited number of SKUs and a huge volume, I think our buyers know pretty darn well a lot of the cost components of these things. And that, I think, bodes well for us. But again, at the end of the day, we are seeing -- I think it is a little light at the end of the tunnel.

Certainly, container rates have come down. Container shortages have improved. The port delays have improved, all that things go into it. And as raw material prices come down -- and FX generally helps you and hurts you. When we report a foreign company's earnings in U.S. dollars, and the currency has gone down 10%, it's 10% less earnings that we report. But at the same token, since we're using U.S. dollars in a lot of things, not just in the U.S. to buy different supplies and raw materials from other places, that helps you a little bit.

And again, I think it's -- could something happen tomorrow to change this? Sure. But at least we're seeing the things going -- starting to go in the right direction. Hopefully, that bodes better for not just us, but everyone.

Q - Oliver Chen {BIO 15320650 <GO>}

Okay. And lastly, now it's time to talk about Generation A, analysts. What about the data science team, Richard? And I know you hired that team and what kind of progress or things we should look for there as well as any highlights you want to give us for your digital strategies on the horizon?

A - Richard A. Galanti {BIO 1423613 <GO>}

You know what, I -- in my old age, I forgot to get any detail on that, but I'll do that on the next quarter. But generally speaking, it's been a couple of years since we brought in a VP of Data Analytics, and he has built a sizable team. And a lot of things they're working on is to have better visibility. As simple as we are, we still need visibility into things that we have done historically, just not on the sales side, but on the operating our business side, greatly reducing -- the intent is to greatly reduce the buyer's time and doing their own spreadsheets, if you will, and simplifying that. And so, we're doing a lot of activities like that.

And in terms of the data analytics to drive more business, that's still to come. We think we're doing okay right now with -- but the first effort of this area is on improving the data that both our data -- our operators, our buyers, our traffic people get.

Q - Oliver Chen {BIO 15320650 <GO>}

Okay. Thanks very much. Best regards.

Operator

Thank you. Our next question comes from Greg Melich of Evercore ISI. Your line is open, Greg Melich.

Q - Greg Melich {BIO 1507344 <GO>}

Two questions, first on gas and then the credit card; on the gas, I guess, I'm curious, it looked like it's -- well, we know it's a negative mix shift, really helped ancillary. That was the one thing, where gas profit or penny profit was up. Can you just remind us of that dynamic that as gasoline prices fall, how high penny profit can go during that period? And also remind us the traffic-driving relationship to gasoline.

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, the old story was as when prices -- given that we turn our inventory about every day on average and the average in the U.S. gas stations is like every 8 or 9 days. So, on average, we're buying -- the other guys buying it four days -- four days earlier. So, when prices are going up each day, when spot prices are going up each day, it's costing us a little more, because we bought it today at the highest price versus four days ago. I'm being very simple here. And when it's going down, just the other happens that we make more money when it goes down.

I think part of that story has been thrown away, because it seems that not only us, but the supermarket retailers and other discount retailers that operate large numbers of gas stations, they've been able to use it to -- as prices went up or went -- even went down a little bit, they didn't go down as fast as perhaps they could have been, which gives us, in our view, an ability to make a little more and still be the most competitive, in fact, in our view, gotten a little wider.

So, I think overall gasoline as a retail business has gotten more profitable in the last couple, three years. And it's -- that profitability has been even exacerbated a little bit by what's going on with inflation and the headline news that prices are skyrocketing. And even when you see gas -- while the gas prices have come down at the pump, it seemed like that lagged -- crude oil coming down. Why isn't it coming down faster? And so, we still are very much, in our view, the most competitive out there. And arguably, we've been able to use that to be -- continue to be more competitive elsewhere as well.

Q - Greg Melich {BIO 1507344 <GO>}

And is it still 50% roughly that you think go to the club when they get gas?

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, historically, a little over 50 of every people -- what? Yes. Historically, a little over 50 of every 100 people that filled up with gas came in to shop. That actually right when gas peaked right after the Ukraine-Russia thing, for a couple of weeks there, it went down to like 20%, 25% because people are topping off their tanks for fear that there was going to be a gasoline shortage. If you're as old as me, you remember the mid-70s, but memory utilization also went up. What we're seeing now is that a little slightly over 50 or slightly under 50.

Q - Greg Melich {BIO 1507344 <GO>}

Got it. That's a normal --

A - Richard A. Galanti {BIO 1423613 <GO>}

But more members are using it. Yes.

Q - Greg Melich {BIO 1507344 <GO>}

Got it. And then my last is on the credit card. Just update us on anything you can on the credit card penetration, the behaving of the portfolio, the sort of lift percentage of tender on the card, sort of the lift you get outside of the club with it, just given it seems to be a key part of the renewal rate, I would imagine, continuing to enhance --

A - Richard A. Galanti {BIO 1423613 <GO>}

Sure. Auto renewal -- it's not just on the Citi Visa co-brand card. It's on any Visa card here and on a Mastercard that we worked out a deal with a bank and Mastercard in Canada. So, on co-brand, not only the fact that we do it exclusive, which, arguably, gives us purchasing power to lower the merchant fee and to drive the reward to the member. There's typically co-brand cards, there's revenue share. So, every time that card is used outside, we share in that revenue. While we pay for some of the rewards, that's more than offset -- that's offset by the revenue sharing. So, it continues to be -- fiscal '22 is a great year for the card in terms of increasing penetration and increasing rewards to our members and very -- in our view, a very favorable effective merchant fee to us, which we don't disclose.

Q - Greg Melich {BIO 1507344 <GO>}

And the auto renewal is up to what percentage?

A - Richard A. Galanti {BIO 1423613 <GO>}

Auto renewal, I don't --

A - Unidentified Speaker

Mid to high-50s in the U.S.

A - Richard A. Galanti {BIO 1423613 <GO>}

In the -- U.S. number, mid to high-50s signed up for auto renewal.

Q - Greg Melich {BIO 1507344 <GO>}

Great. Thanks and good luck.

A - Richard A. Galanti {BIO 1423613 <GO>}

Thank you.

Operator

Thank you. Our next question comes from Peter Benedict of Baird. Your line is open. Please go ahead, Peter Benedict.

Q - Peter Benedict {BIO 3350921 <GO>}

Hey, Richard. Thanks for taking the question. You kind of ended your prepared remarks, you said kind of seasonal going well. Maybe you can elaborate on that. Are you talking about fall seasonally, talking Halloween? Just what were you trying to express with that?

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, part of what I'm trying to express is, is that while inventories were up 26% year-over-year, we're starting to feel good that they're going in the right direction with the efforts that we put forth. And part of the -- by the strength is, once we also indicated -- I mentioned in the call or somebody did that seasonal -- we brought in, in some cases, seasonal early just because the nature of the delivery dates, so we want to make sure we add it in. What we've seen so far is Halloween is doing well, and Christmas is doing well. And so, we're encouraged by what we've seen in the last few weeks.

Q - Peter Benedict {BIO 3350921 <GO>}

Okay. Perfect. And then just kind of maybe a bigger picture, maybe historical question. Just talk to us about how your business has kind of performed in past recessions. And maybe what do you see from your members as you think back? What are the early indications when we're going into a tougher environment? Is it the business member that starts to slow? Is it traffic? Is it certain categories? I don't know. Just curious kind of your perspective as we're in this unique time in the economy.

A - Richard A. Galanti {BIO 1423613 <GO>}

Look, I don't remember all of them, but I remember the '08, '09 one was that at the end of that year, which went from a recession to the Great Recession. It lasted for 4 or 5 years.

And that -- as we entered it, and it was pretty quick when it happened. We saw some, like, a slowdown in seasonal things, which were, like, barbecue grills and patio furniture and things like that. Big ticket -- those kind of big-ticket items slowed.

And if I go back to my notes, I'm sure we've talked about we had an extra x million dollars of markdowns, just -- to get through that stuff, so we didn't have it lingering after the first of the calendar year.

Other than that, generally speaking, one of the nice things about our model is, is we've done well in good times and bad times. And in good times, of course, people have money to spend. And in bad times, people want to save. And in a perverse way, while none of us ever wish COVID on anybody, from a bottom line standpoint, while it impacted some businesses negatively, it's impacted many more of our businesses positively, and we've seen to keep some of that market share. Restaurants are reopening. People -- as what I read that people are still eating more at home than they did pre-COVID. And -- but even within that, we felt that we built some additional market share during that.

So, I think overall, we did find -- and I think the good news is, even in bad times, we don't view ourselves as having to be as conservative as perhaps others might be. We don't take big reductions in buying -- and open to buys or anything in that regard.

If I have to remember, back in '09, '10, or '08, '09 with the barbecue grills and patio furniture, midway through the new year, and it was clear it was going to continue to be a recession, whether it was Craig or Jim, prior to Craig or both, the reminder to the buyers was don't bring down price points. We've driven value at greater value and greater price points, if we want to be a little conservative, fine, but don't think it's not going to do, go forward based on the assumption that we're providing the best value out there.

Q - Peter Benedict {BIO 3350921 <GO>}

Right. No, no. That's helpful. I think -- as I recall, maybe your renewal rates actually went up during that Great Recession as well. So, definitely resilient. Last question just on --

A - Richard A. Galanti {BIO 1423613 <GO>}

Yes, they certainly have now -- auto renewal is certainly a piece of that.

Q - Peter Benedict {BIO 3350921 <GO>}

Yes. Exactly. Last question just on traffic, Richard. I think, 5% or so on the quarter. I think August maybe was maybe a shade below 3% in the U.S. just how do you guys think about that? I mean, is there a traffic level that you guys don't like to see it go below, obviously, more traffic better than less? But just kind of curious how you're thinking about that.

A - Richard A. Galanti {BIO 1423613 <GO>}

Yes. Part of the challenge of -- in the last couple of years is every time something happens, some of it hits the fan. And it was like the Omicron surge, the Delta surge, and you'll see things change dramatically in a short period of time.

Look, at the end of the day, whenever we see any possibility of something weak, we figure out how to drive sales. And you usually drive sales by greater values, hot items. And that goes back to the comment I made earlier about the multi-vendor mailers. That's the one thing I think we're good at, is figuring out how to drive people into the door with hot items, and that's helped us as well.

David here just shared with me. One of the other interesting things, we see more Monday through Thursday shopping than on the weekends -- vice versa. We see less Monday through Thursday and more on the weekends, because people are going back to work. But -- so during the week, we go, what's going on? And then by the end of the week, we go, phew.

Q - Peter Benedict {BIO 3350921 <GO>}

Okay. Good enough. Thanks very much. Good luck.

Operator

Thank you. Our next question comes from John Heinbockel of Guggenheim Partners. Please go ahead, John Heinbockel.

Q - John Heinbockel {BIO 1508150 <GO>}

Do you guys have any sense of demographics by Gold Star versus executive? And the thought being, when you think about the structure going forward, could you leave Gold Star where it is, take executive up and maybe at an executive plus, right, that either has more than 2% or some other features, right, so you're catering to people through the income spectrum?

A - Richard A. Galanti {BIO 1423613 <GO>}

Yes. I think we try to -- as you know, John, I think we try to keep things simple. We talk about all kinds of things, but we always come back home and say, let's do this and keep it simple. One of the issue -- one of the other issues about doing a higher level of membership than the executive is the sales taxability in some states that is currently non-sales taxable, but at a certain level, states say it's sales taxable, not just the increment, but the whole membership fee. So, that's something we take into account also. At this juncture, I think we still went towards simple.

Q - John Heinbockel {BIO 1508150 <GO>}

Okay. And then secondly, when you think about -- I think somebody asked right about inflation going forward. A lot of what we hear is that it'll be sticky, right? Higher for longer. As it comes down, what -- how do you think vendors are likely to respond? We're not going to see list price decreases, right? We're probably going to see more trade money step up. So, when you think about your participation in that and your ability to take advantage of that, how do you guys think about that?

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, again, I think, again, in terms of the stickiness, wages are still the culprit. I think, again, we're in as good a position, if not better than anybody, given that our buying power per item is off the-charts high compared to anybody else and our buyers focus on the detailed components of it. So, there will be stickiness. Read articles every day or on television or in the periodicals, the journal about some CBG companies that just raised their prices, and they're sticky. Well, we'll try to unstick them, but I'm sure some of it will stick and some of it won't.

But I think, again, we're in the best position when you're thinking about we've got lots of $50 million and $100 million and $200 million and even higher items and even a handful of billion-dollar SKUs. So, we think we are pretty good at figuring that out with our suppliers, not only just to say, hey, the price went down on this commodity or this supply cost component, but also on figuring out how to make things more efficient.

I think, we all -- one of the things somebody asked earlier about what have we learned on the freight and trade side, container side, port side, I think we've learned through manufacturing as good as we think we are. There are things that I hear at the budget meetings all the time about how on $100 million, $200 million, $500 million SKUs, how they're taking costs. So -- which right now meant that the price increase was lower than it would have been. But now they took cost out by changing the production line or eliminating some of the insight packaging. And that's part of ESG as well as you know how to lower the cost. And again, I don't know if anybody does it as well as we do, given that we're focused on such bigger volumes of an item.

Q - John Heinbockel {BIO 1508150 <GO>}

Okay. Thank you.

Operator

Thank you. Our next question comes from Robby Ohmes of Bank of America Securities. Please go ahead, Robby Ohmes.

Q - Robert Ohmes {BIO 1541955 <GO>}

Maybe a follow-up on John's question. So, the kind of signs of relief and inflation you're seeing, can you give an example as -- in the kind of food and sundry side of the business? Are you seeing some relief on the food inflation side?

A - Richard A. Galanti {BIO 1423613 <GO>}

Yes. I'm getting some help here.

Certain commodities, like corn, are coming down. I mentioned -- resin is coming down a little bit. So, all these things are impacting a little bit. But in some cases, the supplier are committed at the higher priced -- we work with our suppliers. The more transparent they are with us, which we feel they are very transparent, we work together on that.

In some cases, even when commodity price has gone down fast, if they've committed to the next three months at a higher price, because they -- we all were fearful it was going even higher, we work with them on that. But -- so I think, again, it's -- at this juncture, anecdotal, and I can't give you any specific examples.

Q - Robert Ohmes {BIO 1541955 <GO>}

Got you. And then just a quick follow-up. I think you mentioned optical was down. I apologize. Has optical been weaker for a while, or what -- or did something change there?

A - Richard A. Galanti {BIO 1423613 <GO>}

I think the big thing there was a promotion we did a year ago in the quarter.

A - Unidentified Speaker

We did another.

A - Richard A. Galanti {BIO 1423613 <GO>}

Okay. So, we did a big promotion a year ago. And this year, we did -- we do a big promotion on lots of things all the time. But we did a big promotion this year on -- at a slightly later date. And so, we're now seeing it.

Q - Robert Ohmes {BIO 1541955 <GO>}

Got it.

A - Richard A. Galanti {BIO 1423613 <GO>}

Yes. So, it's more timing than anything on that example.

Q - Robert Ohmes {BIO 1541955 <GO>}

Got it. Thanks so much.

Operator

Thank you. Our next question comes from Scot Ciccarelli of Truist Securities. Your line is open. Please go ahead, Scot Ciccarelli.

Q - Scot Ciccarelli {BIO 1495823 <GO>}

Thanks and hi, guys. So, Costco tends to put a line in the sand on pricing with some items. Obviously, the hot dog and soda versus chicken offerings, for example, despite today's inflationary pressures. But your margins are actually holding in pretty well. So I guess, the question is, are there other areas where you're being even more aggressive than normal on the pricing side? And then, the flip side of that is, what categories are you guys using to maybe harvest some extra margin to offset the presumed margin squeeze from holding the line of sand on pricing?

A - Richard A. Galanti {BIO 1423613 <GO>}

Lightning just struck me. No. We don't -- we really don't look at it that way. I think, the thing I mentioned earlier about there are some businesses that are doing well with margin like gas business on a smaller way -- in the travel business, those things help us be more aggressive in other areas, or as you mentioned, hold the price on the hot dog and the soda a little longer, forever. And -- but at the end of the day, no, I don't think we necessarily look to find places where we can harvest margin. But we are -- there are different areas.

Again, the fresh foods business -- the strength in sales for a two-year period, where over two years, you had 30% and 40% -- 20-plus-percent increase each year. The abnormity of the improvement in the bottom line, even now as we're getting some of that back now, still net-net, we're better than we were two years ago. So, all those things help that process.

Q - Scot Ciccarelli {BIO 1495823 <GO>}

But on a go-forward basis, if you're really not looking to take any extra margins some other categories, should we presume that margins may actually start to drop on a year-over-year basis?

A - Richard A. Galanti {BIO 1423613 <GO>}

Well, we don't provide guidance, but we look at the bottom -- the top line first and how does that impact the bottom line. And historically, years ago was we want to raise margins by lowering prices, but keeping a little of it. That was the old saying, you're in an inflationary environment, and that changes a little bit. But at the end of the day, it's all about driving volume. If we can incrementally get another percentage point of comp sales that does more than any kind of harvesting we would ever want to do, which we don't do.

Q - Scot Ciccarelli {BIO 1495823 <GO>}

Understood. Okay. Thanks, guys.

A - Richard A. Galanti {BIO 1423613 <GO>}

Okay. I think that's it on our end. Thank you very much, everyone. We're all here to answer some additional questions, and talk to you soon.

Operator

And this concludes today's conference call. Thank you for participating. You may now disconnect.