Costco Wholesale (NASDAQ:COST) Q2 2012 Earnings Call February 29, 2012 11:00 AM ET

Executives

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

Analysts

Deborah L. Weinswig - Citigroup Inc, Research Division

Charles X. Grom - Deutsche Bank AG, Research Division

Robert W. Carroll - UBS Investment Bank, Research Division

Brian W. Nagel - Oppenheimer & Co. Inc., Research Division

Adrianne Shapira - Goldman Sachs Group Inc., Research Division

Gregory S. Melich - ISI Group Inc., Research Division

Christopher Horvers - JP Morgan Chase & Co, Research Division

Mark Wiltamuth - Morgan Stanley, Research Division

Robert F. Ohmes - BofA Merrill Lynch, Research Division

Charles Edward Cerankosky - Northcoast Research

Mark R. Miller - William Blair & Company L.L.C., Research Division

John Heinbockel - Guggenheim Securities, LLC, Research Division

Operator

Good morning. My name is Dawn, and I will be your conference operator today. At this time, I would like to welcome everyone to the second quarter and year-to-date operating results for fiscal year 2012 and February sales conference call. [Operator Instructions] Thank you. Mr. Richard Galanti, CFO, you may begin your conference, sir.

Richard A. Galanti

Thank you, Dawn. Good morning. This morning's press release reviewed our second quarter fiscal year 2012 operating results for the 12 weeks ended February 12 and our February sales results for the 4 weeks ended this past Sunday, February 26.

As with every conference call, let me start by stating that the discussions we're having will include forward-looking statements within the meaning of the Private Securities and Litigation Reform Act of 1995 and that these statements involve risks and uncertainties that may cause actual events, results and/or 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.

To begin with, our 12-week second quarter results, for the quarter, earnings per share came in at $0.90, up 14% from last year's second quarter earnings per share of $0.79. This was on a 10% sales increase and there weren't any big unusual items either in this year's or last year's second quarter earnings. But as we go through our note, you'll note comparison includes not only a 10% overall sales increase, an 8% comp sales increase and normalized 7% comp increase, excluding gas inflation and FX impact.

The FX impact on our foreign operations year-over-year in Q2, assuming flat year-over-year FX rate, essentially hit us by about $5 million pretax earnings in the second quarter. We had an 8% increase in membership fee income. This included very little impact from the recent announced fee increase, a little less than $1 million. This is due to the nature of deferred accounting, and I'll talk about that in a minute.

We had a lower year-over-year gross margins as we continue to invest in pricing. We had good SG&A expense improvement and we had a smaller year-over-year LIFO charge, $6 million last year in the quarter versus $2.5 million and we had a favorable year-over-year income tax rate comparison.

In terms of sales for the second quarter, reported total sales were up 10% and our 12-week reported comparable sales for the year was up 8%. For the quarter, both total sales and comp sales were positively impacted by gas price inflation, offset a little bit by the slight weakening of foreign net currencies relative to the U.S. dollar year-over-year. On a comp basis, the 8% U.S. sales increase reported in Q2, excluding gas inflation, would have been 7%. The reported 8% international comp figure, assuming flat year-over-year FX rates, would have been plus 10% and total company comps reported again at 8% for the quarter, excluding both the gas inflation and FX, would have been plus 7% for the company. And this plus 7% quarterly comp sales increase figure, it's the same level of increase achieved in each of the past 3 fiscal quarters, again on a normalized basis, including the effects of gas pricing and FX.

In terms of sales for the 4-week month of February, it's pretty similar to the quarter. Excluding gas inflation, the 8% reported U.S. comp was 7%; the 8% international comp was plus 9% in local currency and excluding both of those, total company reported comp of 8% would have been a plus 7%.

Other topics of interest are opening activities. After opening 4 new locations in the Q1, which ended last November 20, one each in Pennsylvania, Texas, Wisconsin and Georgia, we opened 2 new locations in the second quarter, both in Japan, one in Yawata, near Osaka; and one in Zama, near Tokyo. Since Q2 end, on February 12, we opened last week one new location in Kobe, near Osaka, Japan. And also, last week, we reopened our Tamasakai warehouse in Japan. This had been closed since the tragic earthquake last March 11. All told, that would put our fiscal 2012 expected opening schedule at 17 net new units, the 8 we have opened fiscal year-to-date and 9 more to open by fiscal year end. And these 17 consist of 10 in the U.S., 1 in Canada, 2 in Korea and 4 in Japan. With the opening last week, the 2 openings last week, we now operate 600 locations around the world. I'll also touch on costco.com, membership results, additional discussion about margins and SG&A and our recent stock repurchase activities.

So on to the results. Sales for the quarter were $22.5 billion, up 10% from last year's $20.4 billion. Again on a reported comp basis, Q2 sales were reported at plus 8% and plus 7%, what I'll call normalized after excluding gas and FX. For the quarter, our 8% reported comp figure was a result of a combination of the average transaction size of plus 2.4% and an average frequency increase of plus 5.2%. The frequency trend during the past 3 months of December, January and February was plus 5%, plus 5.5% and plus 5.3% and, again, for the 12-week quarter it was plus 5.2%.

We're now going into our fourth calendar year of year-over-year frequency increases over 4%, and that, of course, is after years of frequency increased figures generally in the 0% to plus 2% range.

For the February reporting month, much like the quarterly comp figures, our plus 8% recorded comp was a combination of an average transaction increase of 2.9%. It's a little higher than the 2.4% for the quarter overall and an average frequency increase of 5.3%. In terms of sales comparisons by geographic region, our first for the quarter, in the U.S., the Midwest, Northeast and Southeast regions were the strongest. Overall, U.S. was very similar to the total company. Internationally, in local currencies, we had the same comp percent increase, about 10%, as the 10% in our prior 2 fiscal quarters, both Q4 of last year and Q1 of 2012, what I'll say is in local currencies international comp was also 10%.

For February, on a U.S. regional basis, our strong results were in the Midwest, Texas and both the Northeast and Southeast. And internationally, for February, again, in local currencies, the plus 9% result for February compared to a plus 9% in January and a plus 11% in December going back a couple of months.

In terms of merchandise categories for the quarter and month, excluding the impact of FX, I'll just talk about February here since we do this monthly. Within Food and Sundries, all subcategories were positive for the month and averaged in the high-single digits. In terms of Hardlines, the comp was in the low-single digits as it has been for the last several months and a couple of quarters. Within Hardlines, the strongest subcategories were hardware and automotive, with electronics just below flat for the month.

Within the low-double digit Softlines comps, the strongest subcategories were small appliances, domestics and special events. And within Fresh Foods, positive high-single digit comp and all Fresh Foods subcategories were positive.

Now moving on to the other line items in the income statement, membership fees, $459 million this year or 2.04% compared to $426 million or 2.08% last year in the second quarter. In dollars, that's up $33 million or 8% and as a percent of sales, down 4 basis points. We continue to enjoy strong renewal rates and increasing penetration of our Executive Membership. Our new member sign-ups in Q2 company-wide were up 11% year-over-year, mostly due to the strong international openings this past year and this past 12 months in Asia and Australia.

In terms of members at Q2 end, Gold Star, 25.9 million, up from 25.5 million at the end of the first quarter. Business primary remained at 6.4 million. Business add-on was 3.7 million, down from 3.8 million. A lot of that again has to do with as add-ons become executive, they go into the other 2 categories. All told, 36.0 million versus 35.7 million at the end of Q1 and including add-on spouse cards 65.7 million total versus 64.9 million at the previous -- the first quarter end, so up about 800,000. At Q2 end on February 12, our paid Executive Memberships were 12.15 million, an increase of a little over 100,000 since Q1 end, and that's about 8,400 a week.

In terms of membership renewal rates, they continue strong. Our business membership renews and this is U.S. and Canada, which was the bulk of our business for a long time, was up 93.5%, up from 93.3% at the end of Q1; GoldStar 88.4%, up a little bit from 88.2% at the end of Q1; so total 89.4% compared to 89.2% at the end of Q1 end; worldwide, 85.6% at the end of Q2 versus 85.4%, so up a little bit. That number fluctuates a little bit because of the small base in many of these international countries and you're always going to have much lower renewal rates in the first year or 2 of a new warehouse and in a new market many cases.

As you all know, we recently increased our annual membership fees in both the U.S. and Canada. The annual fee for the GoldStar and Business add-on members are now at $55 in US dollars and Canadian dollars. An annual fee for the Executive Membership in the U.S. and Canada now stands at $110. These increases became effective November 1 for new members and effective January 1 with regard to member renewals, which of course, is the bulk of our membership data. In all, approximately 22 million members will be impacted by this increase over the 12-month period that people renew, approximately half of whom are executive members, so roughly half at the $10 rate and half at the $5 rate.

In terms of the timing of these increases hitting the income statement, please remember that membership fees are accounted for on a deferred basis. So just using the example of one member who paid an extra $10 for an Executive Membership and, let's say they renewed in January, that $10 would be then spread over the next year, in our case, the next 13 4-week periods. And so the full impact or benefit to the membership income line will be over essentially about 23 months, peaking at 12 months out. Of course, the 23rd month will have the last remnant of the renewers that were just notified of their renewal 12 months into this announcement.

So in terms of -- given the deferred accounting, there was essentially no impact in Q1, as I mentioned last quarter. There's very little impact in Q2, just under $1 million pretax; a small amount in Q3, about $7 million pretax or about $0.01 a share; much more meaningful starting in Q4 and beyond. Q4 of course, is a 17-week fiscal quarter. It's always been a 16-week quarter, but this is a 53-week year and into Q1 and 2 of next year, we'll see that impact be more meaningful. The full impact of these increases, as I mentioned, is 23 months and we'll see that when we see it.

With regard to Executive Membership, the 2% reward, along with the increase -- the 2% reward associated with the Executive Membership was increased up from $500 per year to $750 based on eligible purchases. That's about a $4 million, $5 million annual impact. A small amount of that was accrued for this quarter to catch up for -- we're going to do it on -- based on whatever the renewal rate is. While it's still very early to see any impact on renewals from the fee increase, as we only have really one month, January, and even in January that's partial data, based on our limited data and in our judgment from the marketing people here, we don't expect any issue.

Going on to the gross margin line, the gross margin year-over-year was down 30 basis points from a 10.83% last year to a 10.53%. Get to do the little matrix here. Four columns. Columns 1 and 2 will be Q1 '12 and column 1 will be the reported figures and then column 2, we take out gas inflation because I think it makes it more meaningful without the impact of gas inflation on these percentages. So reported and without gas would be Q1 '12 and Q1 '12 again. Columns 3 and 4 would be for Q2 both reported and without gas inflation.

The line items, merchandising core; second line item, Ancillary; third line item, 2% Reward; fourth line item, LIFO; and last line item, total. So going across the core merchandising, we reported in Q1, as we report in Q1, it was down year-over-year 32 basis points, but without gas inflation, down 10 basis points. In Q2, reported down 25; and without gas, down 16; Ancillary, minus 2 and then plus 2; and for the second quarter, minus 5 and minus 4. 2% minus 1 and minus 3; and for Q2 reported minus 2; and Q2 without gas, minus 3; and LIFO, 0 and 0 in the first quarter; and in Q2, reported plus 2 and without gas inflation, plus 2. When you add those line items up in Q1, as you recall, we had reported year-over-year gross margins down 35 basis points; without gas inflation, down 11; for this quarter, the reported down 30 basis points; adjustment for gas inflation would be down 21. As you can see, again, our overall reported gross margin, well, it was down 30. Within that 30, our core was down 25%, but again, our lower gross margin Gas business, and in fact, increasing Sales Penetration, I guess, business as well caused that impact of 9 basis points so that, again the 25, looking at it without gas inflation impact, was minus 16.

Now while gross margins in our core business, which is Food and Sundries, Hardlines, Softlines and Fresh Foods, were still lower year-over-year in Q2 by 16 basis points, in the quarter Hardlines and Fresh Foods were about flat year-over-year and one a few basis points higher and one a few basis points lower year-over-year. Food and Sundries and Softlines were down year-over-year a little bit more than that, again for an average of that minus 16.

As we continue to invest -- again we continue to invest in price to strengthen our business long-term and we think it's doing what we want it to do. Ancillary business's gross margin as reported was down 5 basis points year-over-year in Q2 partly due to gasoline inflation and slightly lower year-over-year gas margins in the quarter, as well as quite a bit lower year-over-year gross margins in our food court. This continues to be due to our decision to hold prices on many items even as some commodity costs have increased. You've heard that again and again. That's what we do and we do it not only there, but in a few other areas as well.

The impact from increasing Executive Membership represented a 2 basis point hit to gross margin, again due to the 2% Rewards featured in the membership, including that small amount of annual expected increase due to the increasing the maximum from $500 to $750. And LIFO benefited us in terms of P&L benefited by $4.5 million, $6 million pretax charge last year compared to $2.5 million this year.

Moving down to SG&A, our SG&A percentage Q2 over Q2 was lower or better by 29 basis points, coming in at 9.67% this year compared to a 9.96% last year. Again, the matrix, 4 columns, first 2 columns for Q1 with and without gas inflation and the third and fourth columns for Q2, again with and without gas inflation. Reading across, and pluses here mean good, mean lower as a percent of sales, lower SG&A as a percent of sales, core op plus 28 reported in Q1; plus 9 after gas effect taken out; in Q2 plus 25 and plus 18 without gas; central, plus 4 and plus 2; and for Q2, plus 5 and plus 4; equity, minus 6 and minus 7; and for the second quarter, minus 1 and minus 1; and total, again last -- first quarter, we reported year-over-year, 18 basis points improvement or plus 18. Without gas inflation, it was actually minus 4 or lower by 4. I'm sorry there was an adjustment last quarter that I forgot to mention, the 11.83, that Washington State initiative. That was 8 basis points to the negative. So the minus 4 reported without gas inflation in Q1 also had the impact -- that minus 4 is after the impact of the minus 8.

For Q2, again, we reported 29 basis point improvement year-over-year; and without gas inflation, plus 21. In terms of a little editorial on SG&A, again the operations component of plus 25 was 18 without gas; and so about a 7 or 8 basis-point improvement, 7 basis-point improvement on core operation that, that helped us with, but 18 without gas.

Our payroll percentage year-over-year benefited the SG&A comparison by more than 11 basis points. Total payroll dollars in our company increased 6.5% in Q2 compared to the 10% total sales increase. As well, increases in health care costs were a little lower than we anticipated. Hopefully that's a trend, but you never know. Central expenses better lower year-over-year in Q2 by 5 basis points, and as you saw, stock compensation expense was about 1 basis point higher. Overall, we consider Q2 a good performance in SG&A, and hopefully, that can continue.

Moving down the income statement, preopening, $4 million last year in Q2; $6 million this year, so $2 million higher or 1 basis point. In both fiscal quarters, we had 2 openings. The bigger difference has to do with when they open and where they open. Some countries have much higher preopening per unit. And is also based on remodels and other expansion activities. In terms of provision from period assets and closing costs, in both Q2 '11 and in Q2 '12 we had a charge of $2 million. All told, operating income in Q2 was up $48 million from $596 million last year to $644 million this year.

Below operating income, reported industry expense was about the same year-over-year, with Q2 '12 coming in at 27 compared to 27 a year ago as well. Now these amounts mainly reflect the interest expense on our $2 billion debt offering we completed in February of 2007. As I mentioned last quarter, and probably the quarter before that, that this month -- next month on March 15, in about 2 weeks, we'll pay off $900 million of this debt, the anticipated annual pretax interest savings to Costco, assuming we're paying 5.3% coupon and a small amount of amortized -- amortization of issuance costs of about a 5.4% hit of benefits -- hit to the P&L currently. And we'll be foregoing interest income on our cash in the 20 to 30 basis point range. That's about $46 million pretax per year. For Q3, given that we're doing this effective March 15, we'll get a pretax positive ramp of about $7 million. For Q4, and again it’s 17 weeks, not 16, the pretax positive ramp about $15 million. And again, you could divide that by the number of weeks in Q1 and 2 next year, so it'll be 12 weeks each.

In terms of interest income and other, it was higher year-over-year by $6 million, $10 million this year in the quarter, $4 million last year. Of that $6 million increase, actual interest income was higher year-over-year by $2 million, a reflection of higher cash balances. However, the biggest component of the $6 million change was interest income and other, and it is [indiscernible] from another was related to the FX impacts on our business. It was much this positive or much bigger in Q1 year-over-year. But as I explained last fiscal quarter, we consider this part of our gains and whether the gains and losses as these contracts are done mostly by our merchants and are offset or in addition to their merchandise margin, which is recorded up in gross margin.

Overall pretax income was up $54 million or 9.5%. Last year, it was $573 million; this year, pretax income, $627 million. In terms of income taxes, our tax rate was a little lower, 34.2% versus 35.5% last year. Our lower effective tax rate is due to a few discrete Q2 items that -- any number of things, whether it’s state or federal and audits going on and whatever, the sum of which reduced our Q2 taxes. This is about 1/3 of that’s lower, in our view, a lower tax rate increase versus last year in Q2 and the rest of it mostly related to decreases in foreign tax rates or overall average foreign tax rate.

Now for a quick rundown of other topics, I'm always asked about depreciation and amortization. For Q2, it was $209 million giving a year-to-date D&A of $414 million. Our accounts payable as a percent of inventories. Last year, we reported it was 97%, 87% if you just looked at merchandise payables, not construction and other payables. This year, the reported number was 91%. That compares to 97% a year ago, but again, looking truly at merchandise inventories and payables. This year, the AP ratio was 86%, down just a little bit from 87% a year ago.

Average inventory per warehouse was up $1.1 million, $10.5 million last year in the quarter, $11.6 million this year. Very little, almost 0 impact from FX, really spread across many, many subcategories. Obviously, this includes the impact of inflation. As I mentioned in Q1, year-over-year, we were up just under $1 million, $900,000, almost $1 million. So pretty much in line with that level of increase.

That being said, there are no inventory concerns. We feel we did a good job of taking markdowns for the holidays and our inventories are in good shape as well as our midyear, we take fiscal inventories twice a year, midyear and year end. Our midyear physical inventories were our best ever for midyear. And in terms of CapEx, in Q2, we spent $234 million last year. In Q2 '12, we spent a little bit more, $289 million and year-to-date it’s $632 million. We would estimate for the year our CapEx will be in the $1.4 billion range.

In terms of costco.com, both sales and profits were up over last year in Q2. Our average ticket has come down a little bit, but our site traffic continues strong. It was up a little over 9% in the quarter year-over-year. We are transitioning to a new platform this summer, bet on mid to end summer. The new technology will give us greater visibility in the Internet and we hope will bring users to costco.com via search engines which our much older current system does not allow. And early summer, we'll launch the first app on smartphones and assume both, and over the course of the next few months a couple of those. We will introduce costco.com elsewhere later this calendar year and into next calendar year outside the U.S. and Canada.

The -- in terms of expansion, I mentioned 17 units this year. Now the 8 remaining that we have or the 8 that will be in Q4, this is down 3 from the previous 11 that I spoke about. These are all delays, they're still happening. They were all scheduled for August. They're now in either October or November so into Q1 of fiscal '13. Adding 17 units to the original base [indiscernible] of 592, that's about 3% unit growth and a little over 3% square footage growth. At Q2 end our square footage stood at 84,998,000 square feet.

In terms of stock repurchase, during the quarter, we spent $145 million. That's a little lower than Q1 of $173 million. We're generally buyers every day and, to date, since June of '05, we’ve bought back 111 million, a little over 111 million shares at about $56.74 a share for about $6.3 billion total dollars. We currently have, I think, $3.4 billion, roughly just under $3.4 billion of authorization left on our program. As I always mention, supplemental information will be shortly posted on our Investor Relations site, which has some additional information.

And lastly, our Q3 scheduled earnings call, earnings release date will be Thursday, May 24. That will be for the 12-week third quarter ended May 6.

With that, I'll turn it back to Dawn for questions and answers. Thank you. Dawn?

Question-and-Answer Session

Operator

[Operator Instructions] Your first question comes from the line of Deborah Weinswig with Citi.

Deborah L. Weinswig - Citigroup Inc, Research Division

As we look out for the rest of fiscal '12 and you start to cycle much easier gross margin compares. How should we think about gross margins for the rest of the year, especially as one of your competitors talking about very aggressive price investments?

Richard A. Galanti

Well, I think -- needless to say, I can't give you any guidance since we don't guide -- but clearly, I think our message has been that we continue to invest in price and I think we do it more than talk about it, frankly, and so we'll continue to do that. But that's what we do. And I think the other message that we are trying to convey over the last couple of quarters and will continue to do so is, well, there's certainly a lot of tough competitors out there. This is us, not them, in terms of what we do for a living and we're not -- in our view, while every day, every competitor responds to one another, but overall, we are responding to ourselves here more than anything.

Deborah L. Weinswig - Citigroup Inc, Research Division

Okay, and then can you talk about anything you're doing in terms of improving productivity on the floor?

Richard A. Galanti

Well, I mean it's a never-ending battle. I mean, we constantly are working to speed the front-end line, whether it's redoing the software for credit and debit, pruning out, all the things that all of us do out there. Just last year, I know one focus, and these are all anecdotal, has been in operations. Again, I think this is where Greg has put a lot of effort into, given his operations background, operators that put a focus on overtime hours. You're always going to have overtime hours whether it's because of weather or people didn't come in if they're sick or holidays where you misjudged something, whatever it is, or physical inventories. But that being said, with a focus on it, and I think that's the key word, focus, we saw just in the last couple of quarters a few million dollars just by having fewer actual hours. And so saying those hours, even if they were still worked, those hours worked as regular hours rather than overtime hours. That extra half was a reduction. So those are the types of things we're doing. I think we still get a lot of benefit from, again, what I talked about over the last couple of years, sustainability. Again, it's not all us; it's everybody. It's the vendors. We're all working towards this end, but it's taking grams of resin out of water bottles and packaging into square containers instead of round, and making liquid everything, detergents and the like, more concentrated. All those things are having, I think, real benefits to all of us. I think we do a good job of managing health care and worker's comp and relative to -- in our view, relative to what our third-party providers tell us they're seeing elsewhere. But it's a lot of blocking and tackling and trying to not do things that we're doing that we don't need to be doing. So in the last 3 or 4 years, our active SKU count has come down from 4,100, 4,100-plus down to 3,800, 3,750. That again was our doing a conscious effort to say if the top 200 items out of roughly 4,000 are 35% to 40% of sales, you can imagine what the bottom 200 are. And every time we can take a palette of something out, that doesn't make sense -- I mean, you’re always going to have some slow things because it makes sense for the small business owner, the restaurant owner, whoever it might be. But if every time you could take a palette out and mass quantity -- mass out something, some existing item bigger, you're going to have more productivity. So all those things that we do. I think for those of you who’ve followed us for many years, I feel that we have continued to do little things that have helped us and we’ve all been helped by what's happened in the economy and trying to be more efficient, but there's no one big thing.

Deborah L. Weinswig - Citigroup Inc, Research Division

Okay. And then lastly, throughout, I'd say this earning season, we've heard a lot about volume declines. Can you talk about maybe what's happening with the national brands and then maybe also with Kirkland signature?

Richard A. Galanti

Well, the first part of the question I heard the question, but what was the first part you said?

Deborah L. Weinswig - Citigroup Inc, Research Division

So we've heard a lot about volume declines throughout the quarter on the HBA [ph] and TPG [ph] side, so could you maybe talk about tapping national brands versus private label?

Richard A. Galanti

Again, sub-department-wise we haven't seen any of that kind of issue in general. I mean, you see the constant pressures on what we call media and 1-Hour Photo, but in terms of -- we see a continued increase in penetration of private label even within existing private label items, recognizing the bigger part of that increase tends, in my view, tends to be we continue to add items. In the last year, 1.5 years, we've continued to add some canned good items, as an example, canned vegetables, canned fruits and the like. We've got that great peanut butter pretzel that I love. So there's a lot of things out there that we're doing but we've not seen any giant change as it relates to the kind of impact we saw in the first half of calendar '09 right after the financial crisis. I think in a given year, we probably see 0.75 of a percent increase in penetration, maybe 0.5, maybe 1. But I remember in that 6 months, we saw 2 to 3 percentage points, just in 6 months. And again, that was again people's focusing on figuring how to save money. I think one of the things that we continue to see in backflow is when we introduce a private label item. It not only drives penetration to that item which generally is a better margin, but also gets the brand to choose and the answer is just to be more competitive because they're losing market share. So it's a win-win for us and our numbers.

Operator

Your next question comes from the line of Charles Grom with Deutsche Bank.

Charles X. Grom - Deutsche Bank AG, Research Division

Richard, just on the price investments that you're doing, I'm just curious, are the number of SKUs increasing each month that you're lowering prices on? Or is it the same basket of products each month? And I guess the second follow-up would be, how are you guys measuring the success of those price investments? Are you seeing a big increase in unit velocity when you do the price investments?

Richard A. Galanti

Well, we are not the most formal when it comes to trying to analyze did it work or not. I remember years -- when we had rampant inflation in the middle of '08 and we lowered the price of our chicken. At the end of '08, when we saw comps going towards 0 and I gave examples, I think over a 4-week period, we had about $32 million of actual markdowns on a limited number of highly visible items and one of them was the rotisserie chicken that had gone from $4.99 to $5.99 and we brought it back to $4.99. Well, if you put a dollar divided by 6, by the $5.99, that was very close, in my view, to the margin, the entire margin. So no matter how many more chickens you sold, it didn't help margin; it hurt it. So we're merchants at heart, and we attempt to drive the top line. I'll give you another anecdotal example. Last August or so, in Canada, where historically the soda and hotdog was at CAD $1.99. Well, many years ago the Canadian dollar was about $0.65 on the U.S. dollar. Well, in one fell swoop, Jim said take it down to $1.50. Well, that's just because that's the right thing to do. Clearly, that impacted the bottom line negatively. But I got to tell you, in a country where they've had a good economy and there's a lot of talk about inflation up there, we got national attention of being the only game in town that's lowering the prices on anything. So we saw increases in traffic and certainly increases in food court as well. So that's what we do and we feel good about the quarter in that we're getting our improvement from expense leverage and buying back a little stock and the like. And certainly, the membership fee as that improves in deferred accounting, that helps you. But we feel good about what we do with pricing and we'll continue to do it but we've really shown that when we need a little margin over time, we figure out ways to do it and do it the right way.

Charles X. Grom - Deutsche Bank AG, Research Division

Can you just remind me in late 2008, when you did do the price investments, did it last for more than a few quarters or was it longer than that?

Richard A. Galanti

Well, that was more of what I'd call back then the perfect storm. Again, we're heading towards 0 and we wanted to go into Christmas and early January with some -- driving it. And whether that was the reason, comps did turn around a little bit then. This is more that we feel that we're strong. We've got a lot of good things going on. We're always reminded by Jim and now by Craig, let's not get too ahead of ourselves in terms of our success and let’s keep driving that top line. So again, I can't give you guidance it's going to be for another 6 weeks or another 25 weeks or -- but we don't worry about it, honestly, and not because we're cavalier, because we know that we have the ability to continue to drive sales. And if we need a little margin over time, we feel we can get it.

Charles X. Grom - Deutsche Bank AG, Research Division

And then just a little surprised only $145 million of buyback in the quarter with the cash balance. I mean I know you got the $900 million tranche coming due in a couple of weeks. But what are the board's thoughts on accelerating the buyback here? Clearly, trying to open up more than 20 to 25 stores a year has been challenging because of delays and your cash position's only going to continue to grow. What are you guys going to -- I mean, what's the priority here?

Richard A. Galanti

Well, the board every quarter talks about it. Needless to say, what we do, they're certainly knowledgeable of and comfortable with. To do with the strength in our stock price and we kind of look at it on a -- periodically update it to kind of [indiscernible] pricing, buying more as the stock goes down and less as it goes up a little bit and then adjust that upward over time as the stock has gone up. There are a number of weeks in the Q, in the quarter, where again, on a given daily basis, we bought a little less. But we feel comfortable, we'll continue to look at it. I don't want to judge what I and the board will consider and do. We recognize that we have a high-quality challenge with cash. You've heard it before, but I still mean it. I am confident that we will continue to increase our expansion, and some of that expansion is going to be more expensive given the international rate of expansion. And over time, all things being equal, I would guess we'd increase it. But again, we're not going to feel pressure to do it this Thursday or next week. But you'll continue to see us buy stock back and the board is supportive of that. That's a vague answer, sorry.

Operator

Your next question comes from the line of Robert Carroll with UBS.

Robert W. Carroll - UBS Investment Bank, Research Division

Just drilling down on the pricing investment a little bit more. I know given kind of the 10 basis-point decline in kind of core business, I mean, is that at the rough level that we should think about until things start to anniversary in Q4?

Richard A. Galanti

Again, we can't guide you.

Robert W. Carroll - UBS Investment Bank, Research Division

Okay. All right. No problem. And then just in terms of the precedents, I guess, from this time last year when gas prices started accelerating meaningfully, I mean, are there any lessons learned from that period that you guys will be putting in place as we see, let's just say, gas prices catch a bit of a tailwind?

Richard A. Galanti

Well, I mean, I think the big thing is that our frequency. There's nothing -- it's a very low-margin business and to try to hedge yourself a little but all you're doing is, if you will, maybe smoothing the profitability out. But that there's a cost to that hedge on a low margin business, that's a big cost, so we don't. And so that's going to continue to be volatile. Whenever it's been a big year-over-year impact to earnings, we talk about it. It's a few cents better or worse or $0.05 better or worse. Clearly, I think last year, in the fourth quarter, we had a huge profits in gas and we shared that with you at the time. But when prices rise, we get more action. We're on the news more, people -- there's more frequency, I looked at some statistics recently in U.S. gallon consumption not just Costco but the U.S. consumers gallons consumption, which in good economies, is up a couple of percent, 1% or 2%, had been done 3% or 4% and of late, has been down 5% or 6%, I believe. I have to check that. And we're still up in the mid-single digits. So we're driving people into the parking lot, no pun intended, and a portion of them come in to shop. So we're -- it's just reinforcing that image.

Robert W. Carroll - UBS Investment Bank, Research Division

And then for the gas sales penetration I know you said it was up year-over-year. Do you have that number?

Richard A. Galanti

I don't -- gas sales penetration. I think it wasn't as much as Q1. I think it was up about 1%. I think it was around 8.5% and the low 9%s.

Operator

Your next question comes from the line of Brian Nagel with Oppenheimer.

Brian W. Nagel - Oppenheimer & Co. Inc., Research Division

I also had a question regarding the pricing actions you're taking and then the result and impact we've seen on your core gross margins. So we’ve seen it now for, I guess, a few quarters. First question I have is, as you think about the actions you're taking within your clubs, what's driving, so to say, the cadence of those? Are you going product category-by-product category? Or is it a reflection to some extent the underlying input costs in those products where you're deciding to make actions? And then the second question I have along those same lines is, after these actions are taken, how are you priced relative to some of your competitors? We’ve talked a lot about -- other questions asked you about competitive pricing out there, but are you, generally speaking, lowering prices below competitors or are you matching competitors, et cetera?

Richard A. Galanti

Well, first of all, we're always going to match or try to be lower than our competitors. Keep in mind, I don't know if it's half or more of our business are very competitive commodity items, whether it’s milk, cheese and butter or soda pop or Advil or diapers or you name it. Private label helps that impact with us and others as well. I really do mean it. It's kind of like all the merchants are -- going into Christmas as an example. The merchants were directed in every categories, come up with some ideas of where we could get sharper and be exciting out there and -- have hot buys and have hot items at hot selling prices. So that's what we do. When we do price comp, price shops and we do it most importantly, directly with -- Sam's and BJ's are the

2 warehouse club operators. We're not comparing every price. Are the fresh food buyers looking at the ground beef ads and the chicken dryer ads or whatever else? Yes. But we're not comp shopping supermarkets. Because keep in mind our margins are, on average 11% and theirs are in the mid-20s or more in some cases; or the home-improvement retailers in the low to mid-30s. So but when you look at the most direct warehouse club competition where we're across the street from each other or down the road from each other, on key commodity items, which is, I don't know if it's 40% or 60% of our business, call it half, we're all very close. When we look at it on exact items, we're going to be lower. It could be a 0.25%. It could be 1.5%, 2%, but it's small. Where we find the big differences is on those non-commodity or highly competitive items. Where we're selling a better quality item, there's not as much of a price comp, a direct price comparison because it’s not the exact item on a lot of things like domestics and housewares, and that's -- or the quality of some of the home meal replacement items at Costco versus elsewhere. So that's where others we feel can make a little more margin and we can too, but not as much. And again, that's what we do is merchant stuff, and so it really is all over the board.

Operator

Your next question comes from the line of Adrianne Shapira with Goldman Sachs.

Adrianne Shapira - Goldman Sachs Group Inc., Research Division

Richard, if I recall, the last time you made some price investments, it was ahead of easing prices. You were the first to lower and it obviously paid off remarkably well with strong share. Is that true this time around as well? Maybe give us a sense of what you're seeing in terms of inflationary pressures potentially easing especially in food?

Richard A. Galanti

Again, the example that I talked about and as you've just mentioned as well is in late calendar '08, the economy crisis, the rampant inflation of mid-calendar '08 towards the -- the fall of calendar '08, there was rising gas prices, rapid inflation, that came to an -- that was coming to an abrupt end. Well, in many instances, our suppliers, who had committed to raw materials, it was going to be 4, 6, 8 weeks out before the underlying prices to us and to other retailers was going to come down. Well, we saw our comps heading towards 0 and again, I think, again we call it the perfect storm. That is completely different. That was a, hopefully, a onetime perfect storm and we acted upon it. I think this has more to do with the fact that we were very strong, we feel. We're driving sales and comps. We're seeing increasing relative levels of profitabilities in some of these other countries. And it's a constant reminder, constant internal reminder again for years and by Jim and now by Craig, let's not be too sure of ourselves. Let's keep doing what we’re -- as long as we're growing the company and growing earnings, we'll do that. As Jim used to say, we still, we think, we deserve to make more and we will.

Adrianne Shapira - Goldman Sachs Group Inc., Research Division

I understand it's different and that it's not as abrupt. But maybe shed some light in terms of are you seeing any easing of some of the inflation that we saw last year?

Richard A. Galanti

Oh, I'm sorry, yes, we are. As an example, while there's a very minor LIFO charge, I mean, I think using 100.00 as the starting point of the beginning of fiscal year for LIFO indices, I think we're up 11 basis points for the first half of the -- first 24 weeks of the year, so virtually nothing. And that includes gas, which is a chunk of that. So are we seeing some declines? I know as an example, cotton prices have come down from its peak. So we will see some declines going forward. So yes, there's some of that. Clearly, to the extent that we self-inflicted tend to lag when there is inflation -- even if there's less inflation that there's no lag to be lagging on. So did that answer it?

Adrianne Shapira - Goldman Sachs Group Inc., Research Division

I think the point is that, while we saw sequentially some degradation in core merchandise margins, if we're seeing some easing cost pressures, perhaps going forward, we shouldn't see as negative of a hit on the margins going forward if you're seeing some relief there.

Richard A. Galanti

Well, I'm going to bet on you then.

Adrianne Shapira - Goldman Sachs Group Inc., Research Division

Okay. And then my next question, as it relates to with gas prices, obviously, that would seem as if, as you mentioned, the frequency in the traffic should continue to at least hold, if not get better. How to think about -- are you starting to see -- how are you addressing the throughput issues? I would imagine some warehouse is given what is just unbelievable traffic trends, what are you doing to kind of accommodate this kind of frequency? I know Jim was very focused on making sure the lines were not too long. What, if anything, is going on to accommodate what's just fantastic traffic?

Richard A. Galanti

Well, there's pretty much 2 things you can do. Other than trying to speed up the register a little bit. You could put more people upfront which we do. The worst thing is, when you have long lines and registers that aren't open, and that's a no-no. Clearly, one of those slides we've shown at conferences that show the number of units that are doing 200 to 250 and 250 to 300 and more than 300, there are more of them. We look for more sites and we've taken a couple of units over in Asia that were in the 300-plus range and have opened sites. That impacts cannibalization, but that's what we have to do, and we'll continue to do that. So we recognize that's a high quality problem and we have to continue to address it. And again, those 3 things you can add more people, you can improve technology little bit -- that's an ongoing iterative thing, but not a lot, other than when you can just push the basket through the archway and it tells you what you owe -- and then open more units. We're also remodeling and expanding. I mean this is anecdotal, but an example is we're under construction in Maui. We're adding a significant amount of parking. I forget how many square feet we're adding to the physical building itself, and we're adding a gas station. But most importantly, we're adding parking. If any of you have been over there, it's approaching 300 million and it's mind-boggling how small the parking lot and the building is.

Adrianne Shapira - Goldman Sachs Group Inc., Research Division

And then just my last question as it relates to online, you talked a little bit, maybe give us a sense of where is that business in terms of sales profitability, how pleased you are with it. And you talked about some tweaks and some changes coming in this year, as well as sort of expansion overseas. Maybe kind of give us a sense of what we should expect online and what sort of trajectory you'd be pleased with as that channel continues to grow.

Richard A. Galanti

Yes, well, look, as you know, we are a little different than others. We have few items on it, more big ticket items. We cater mostly to our members. It's a product extension of what we do. We don't have 100,000 or a million items on there. I think the re-platforming is a no-brainer from the standpoint that I think I said it last call, you go online and punch in [indiscernible] or something, and you don't get costco.com and because our platform is an old platform that doesn't allow search engines to crawl on it. Well, that’s a duh. And that'll happen at the end of the summer. And then it takes several months for the hits to improve your pole position, if you will. Beyond that, we found success in, again, big-ticket items, white glove items, whether it's furniture or I like big-ticket electronics, and it's a lower gross margin business and a higher pretax as a percent of sales business. And so it feels small relative to our company. And for a company that's going to do $95-plus billion this year, it's 2.5-ish so it's small. And does it drive us crazy when others do a lot of business? Yes, but we recognize we do some things that they can't do and they do things that we're not going to do. So we want to do better, and we will, and we're growing, but we can always do better on it.

Operator

Your next question comes from the line of Greg Melich with ISI.

Gregory S. Melich - ISI Group Inc., Research Division

Just a follow-up on that last question, Richard, when you talked about dot.com, is that dynamic of lower gross margin, higher pretax profit, is that entirely because of mix or does it have to do with the business itself?

Richard A. Galanti

Say that again, Greg, I'm sorry.

Gregory S. Melich - ISI Group Inc., Research Division

That dynamic on dot.com that you described, lower gross margin rate, higher pretax profitability? Is that entirely driven by mix or is it something with the actual business?

Richard A. Galanti

Well, it's certainly bigger ticket items help but I think -- I would guess and I'm just shooting from the hip here, the biggest thing is lower operating cost. A high percentage of the items, I don't know if it's 70 or 80 today or more, is factory direct shipped, and so the cost is the electronics, is running the physical system and the buyers and not a hell of a lot more.

Gregory S. Melich - ISI Group Inc., Research Division

Got it, great. And then you mentioned inventory up $1 million for Club globally, FX not an impact, but inflation was key there. Could you help us quantify that a little bit more? Was inflation all of it, half of it?

Richard A. Galanti

Yes, well, on a year-over-year basis, my guess is inflation was 2 to 3, probably closer to 3. I don't have the exact number. And -- yes, 2.5, so call it 2.5, so that was rough number on $10 million, $250,000. The rest of it is, I know we tend to have more electronics right now, but a little bit. I mean, it really was across the board. Historically, it was in 1 or 2 categories, but I think it's partly driving the business.

Gregory S. Melich - ISI Group Inc., Research Division

And is that -- it sounds like with fewer SKUs, but then inflation being $250,000, it means there's $750,000 of actual more depth in the SKUs you have.

Richard A. Galanti

More depth and higher tickets. Not just because of inflation.

Gregory S. Melich - ISI Group Inc., Research Division

Got it. Okay, great. And then, lastly, on gasoline, could you highlight a little bit the -- I think you mentioned gas profitability in the Ancillary, I imagine that’s because of the rate of increase and the replenishment of your inventory? Could you just give maybe a little more color on that? But that dynamic, was that what hit you in this quarter?

Richard A. Galanti

In the Ancillary, that hit us. The food court I mentioned, I think, that's a big chunk of it as well and that's, again, that's I think I talked about that in a couple of the last 3 or 4 quarters. And again, that is clearly us. I mean we've held the price of pizza when cheese prices skyrocketed and again it's still profitable, needless to say, but it's at a lower level of profitability.

Gregory S. Melich - ISI Group Inc., Research Division

But that negative 4 bps to gross margin, you mentioned the food court, but the part that's gas margin, I imagine that's not -- that's not just the fact that gas mix went up. That's the actual top [indiscernible] profit of gas?

Richard A. Galanti

Yes.

Gregory S. Melich - ISI Group Inc., Research Division

Okay, great. And just given the cadence of what we're seeing, there's no reason to think that, that would change. In fact, could it get worse here before it gets better?

Richard A. Galanti

Well, first of all, with gas, who knows what happens? It was just a few days ago that everybody was talking about gas. There was speculators and there's no reason it should be going up so much, but then, in the same breath, everybody's saying that summer gas prices rise starting Memorial Day. And so when gas prices rise, our profitability lessens. There are weeks when we lose money in gas. And that being said, I mentioned I think last summer is when we made a lot of money, and I imagine prices were going down at the time. So it's hard to say. That's why we try to point out gas because it is such a volatile thing.

Operator

Your next question comes from the line of Chris Horvers with JPMorgan.

Christopher Horvers - JP Morgan Chase & Co, Research Division

So, Richard, continuing the long tread on gross margin, maybe going at it in another way. When we last met, you talked about how the first membership fee years ago, Jim basically said to all the merchants, hey we have an extra $20 million in price investment that we can create. So as you think about going forward and the fact that MFI growth really accelerates in the back half as you talked about, do you think that, that will allow you to accelerate the price investment?

Richard A. Galanti

Maybe yes, maybe no. We, as always, looked at it, again -- and I think the example you're talking about is probably something from 20 years ago literally. There's lots of reasons we are competitive on pricing. There's direct competition, private label, given competition geographically in a given state or country, our level of strong profitability I mean and -- is the success of our membership fee income a factor in how we operate our business? Yes, but by no means any different than all the other factors. Some are bigger than others and sometimes they're not. Again, I can't give you any direction. Our goal is not to drive you guys crazy with what we do. It's to drive our business in the right direction.

Christopher Horvers - JP Morgan Chase & Co, Research Division

Understood. And then is there any -- how much of the price investment maybe relates to what's going on in Canada? It seems like there's a war brewing with Wal-Mart accelerating and Target launching next year?

Richard A. Galanti

Well, again, I'm not going to comment specifically. What we do everywhere in the world as we enter a new state in the United States as somebody comes into one of our markets, we're more competitive. We respond -- usually, our most direct response and impact of that direct response is when it's direct warehouse club-to-warehouse club. And certainly, as Target, which is a new entrant into the Canadian retail market, and Wal-Mart, a very strong retailer up there as well, and other Canadian retailers, there's going to be a lot of pricing competition and advertising and certainly, we're going to continue to drive our business. So again, that's what we do -- that's one of the things we do but we do those things elsewhere as well.

Christopher Horvers - JP Morgan Chase & Co, Research Division

Understood. And final question on the weather, our other favorite topic. So it seems like there's some speculation out there whether or not this is core consumer getting better or maybe January and February is seeing a lift out of weather. Is there anything you can say to that topic or anything you're seeing on the category level that you think is instructive?

Richard A. Galanti

Bob was whispering that this year was a little better than last year weather-wise but not a big impact, in our view.

Operator

Your next question comes from the line of Mark Wiltamuth with Morgan Stanley.

Mark Wiltamuth - Morgan Stanley, Research Division

Richard, it's Mark Wiltamuth. I wanted to get your thoughts on foreign exchange drag that we could see in the second half of the year at this point.

Richard A. Galanti

Well, yes, who knows? I mean it depends on what's going on. I was looking back at the last several quarters. For a long time, the dollar weakened and then it strengthened dramatically and then it's coming off of that strength. Right now it's slightly negative. There's nothing giant brewing out there. The euro thing is less of an impact but who knows? I don’t know.

Mark Wiltamuth - Morgan Stanley, Research Division

Okay, and then looking back through the holiday period, you were clearly one of the holiday winners in terms of sales trend. If you look at those margin investments you did make, were those all planned investments? Or did you have any of that holiday promotion that was kind of reactionary?

Richard A. Galanti

I don't think anything we did was reactionary. It was all done in advance. I mean there may be 1 or 2 things, but I don't even remember thinking, hearing about that.

Mark Wiltamuth - Morgan Stanley, Research Division

Okay. And then as you look at how things are going on expenses right now, what level of comps do you think you need to lever SG&A in the back half of the year?

Richard A. Galanti

You know, for the last several years, we've tried not to predict because we realize we don't know. I think whatever x is, it's a little bit lower sales comp number than it used to be because we, like everybody, has gotten a little more efficient in the last few years with the economy. I hesitate to know what it would be.

Operator

Your next question comes from the line of Robby Ohmes with Bank of America.

Robert F. Ohmes - BofA Merrill Lynch, Research Division

Richard, just a couple of quick questions. I just want to follow up on your answer to Greg Melich's question where you said higher tickets but not just because of inflation. And I was wondering if you could just give us a little more insight to the type of category shifts that you've been seeing recently and what maybe you expect for this year that could be different from what you've seen in the last couple of years? Are you adding higher ticket items to the assortment broadly? Or is it on the Softlines category? Or maybe just a little help helping us see what you may be feeling. We won't hold you to it, but any changes you're seeing?

Richard A. Galanti

Look, it’s all over the board. I mean jewelry is up, needless to say, because of inflation. The average price point of a TV is up a little bit versus being down typically year-over-year. Cameras are up a little bit. Both of those have to do with the earthquake in Japan and the floods in Thailand I think in regard to cameras and hard drives or whatever. So some of those things haven't been deflationary. I noticed, again, I'm telling you this as a shopper. Some of the private label items we've had, canned goods, are 8 packs, not 6 packs. Those are things we do out there. And I know we have a few more home meal replacement items. So I think it's really all over the board. I would think some of it also is more physical units out there, because it can't all be [indiscernible]. But again, our inventories are clean and our shrink numbers midyear were great.

Robert F. Ohmes - BofA Merrill Lynch, Research Division

And just one other question, on the online, are you guys contemplating a change in how you charge for shipping related to this redo?

Richard A. Galanti

I'll tell you soon as I know. I don't know what plans that I have or haven't heard about yet. We keep doing what we do.

Operator

Your next question comes from the line of Chuck Cerankosky with Northcoast Research.

Charles Edward Cerankosky - Northcoast Research

Richard, first thing, just a data point, do you have the square footage at the end of the quarter?

Richard A. Galanti

Yes, it is 84,998,000.

Charles Edward Cerankosky - Northcoast Research

Alright. I want to poke around in another category, apparel. How did that behave during the quarter and any comments on what you might be doing there?

Richard A. Galanti

Apparel was up in the mid- to mid-high single digits and we get brands and we continue to try to divert brands that won't sell us, but no, it's been relatively decent.

Charles Edward Cerankosky - Northcoast Research

And then on the electronics category, you mentioned before on the comp commentary was, I think you said just below 0, but you had some dollar increases in TVs, so how are units tracking overall in electronics?

Richard A. Galanti

Well, needless to say, it's a little bit below "below 0." But I don't have that in front of me. My guess it's in the low to mid. It's not dramatically different than that.

Charles Edward Cerankosky - Northcoast Research

When you're looking at the cash the company has, you're going to pay down a chunk of debt. How about the dividend? What's the board's or management's thought on boosting the dividend meaningfully?

Richard A. Galanti

Again, we talk about it. There's a formal discussion every year in our April board meeting and but there's no -- again, I can't give any direction of what we discuss until we announce it.

Operator

Your next question comes from the line of Mark Miller with William Blair.

Mark R. Miller - William Blair & Company L.L.C., Research Division

On the club opening delays you're seeing, that was also down from the prior plan, but trying to think of many comparable situations for companies that have such strong consumer demand, high comps, great return on capital. I mean is it your fate at this point to be driving around 3% footage growth due to the size? Or are there any changes you can make to reaccelerate unit openings, expanding the real estate team or changes in property siting?

Richard A. Galanti

We have expanded the real estate team in the last year or so, including putting people on the ground in a few of these other countries, more so than we had in the past. We clearly are focused more internationally, which has a little longer time line. There is a lot in the pipeline. Craig clearly is committed to that and I hope we can all sit here soon and say, okay, it finally happened. One of the things that I've said before as we reflect on this question is that one of our -- in our view, one of our strengths, in some people's view relative to how quickly we open units, people think it's a shortcoming -- is we're very hands-on. And we, particularly in -- I kind of viewed it as a real positive in terms of rapid rate of expansion for years between the 3 countries and Japan, 3 in Taiwan. Between the 3 countries, we had about 20 units, so 6 or 7, 5 to 8 per country. And between those 3 units, we may open 1 or 2 a year in total between those 3 countries. That was 6 in the last year, I think, and it'll be more going forward. So we've got more in the plate and I think you should see that turn somewhat at least directionally upward. But I'm tired of listening to me also.

Mark R. Miller - William Blair & Company L.L.C., Research Division

On the pipeline, and that sounds encouraging, is that -- I mean is there I guess a figure you could share with us in terms of sites that have been approved or, I guess, some way for us to look at '13 and whether that number can push higher?

Richard A. Galanti

At the end of the day, I would assume, and I'm sure you [indiscernible], the number should be in the mid-20s, which would give me more comfort that at least it'll be in the low 20s but we'll have to see. We've got a lot going on, a lot more -- we have more going on now than we had a year ago or 2 years ago.

Operator

Your next question comes from the line of John Heinbockel with Guggenheim Securities.

John Heinbockel - Guggenheim Securities, LLC, Research Division

Richard, a couple of things. When you look -- I mean, obviously, your customer's very loyal. But when you looked at loyalty, is the Fresh Foods customer and/or the Kirkland customer, when you look at those 2, are they significantly more loyal than people that don't put as much Fresh Food or Kirkland in their basket? Have you looked at that?

Richard A. Galanti

I have not, so I'm happy to, but I have not.

John Heinbockel - Guggenheim Securities, LLC, Research Division

Secondly, with respect to real estate, is there more -- the sites you're looking at, because there's less -- there seems to be fewer people looking to grow as there had been, the quality of sites that you would look at, is that now opening up a bit or not? That's still not where you'd like it to be in terms of availability.

Richard A. Galanti

It's certainly up a bit from pre-financial crisis, but while there's some slowing, there are still people growing out there. And the other impact aspect of that particularly in, let's say the U.S. and Canada where we are, locations are more pinpoint shots rather than live blasts at geographic area, and anything within a 5-mile radius. We're looking within this mile radius because it's between 2 locations, 6 to 8 miles in each direction. So that becomes a little more challenging. But that's why there's more effort being put into it. And yes, the answer is yes, the economy has helped that process, but it's not like gone from difficult to easy.

John Heinbockel - Guggenheim Securities, LLC, Research Division

And do we ever get to a point where you think about playing around with the size of the box to open up the potential number of locations, a lot smaller or...

Richard A. Galanti

Not yet. Years ago, it was probably 15-plus, 15 or 17 years ago, in the Northwest, we opened 4 units: the coast, Astoria, Oregon; Juneau, Alaska; Kamloops, British Columbia; and one more, I can't remember which one. And they were 72,000-foot units. And over time, we've changed 3 of them into 140,000-, 145,000-foot units and they're doing quite well. And so again, our focus is keeping it focused on what we do.

John Heinbockel - Guggenheim Securities, LLC, Research Division

All right. And then finally, so are health care costs now into the single digits in terms of growth or not yet?

Richard A. Galanti

I think they actually were in Q2. I don't have the sheet in front of me, but as I -- given the total sales increase was 10 and we increased -- we had a basis -- a few basis points improvement, the answer is most likely yes.

John Heinbockel - Guggenheim Securities, LLC, Research Division

And that's not -- you haven't done anything differently with the plan? And I'm not talking about being less generous. I'm talking about just sort of being more diligent about how that money gets spent. Has that been the case or it's just more -- it's going to happen more naturally?

Richard A. Galanti

It's mostly more naturally. We haven't done anything to plan in terms of detriment-ing, improving the bottom line of the cost of it by casting something on to the employee. We have not done that. I think that we're always doing -- in the last several years, we focused a lot more on preventative stuff, needless to say, and getting people back to work and workers' comp. But beyond that, there's nothing to speak of. I know our, what we call high-cost claims, which are $100,000 and over, are down a little bit in terms of frequency.

John Heinbockel - Guggenheim Securities, LLC, Research Division

Then just lastly, wage growth in comparable stores that hasn't changed much during the last couple of quarters, has it? And I'm sort of thinking about within that 6.5% growth, wherever wages were growing [indiscernible], whatever, 3% to 3.5%, that hasn't changed.

Richard A. Galanti

I don't think it was. To the extent that we're opening more units overseas, some of those countries have a lower effective wage than the U.S. does, but still very well compensated relative to that country's regular retail rates. So that slight change there probably helps you a little bit.

Operator

And at your request, Mr. Galanti, there are no further questions. I'll turn the floor back over to you for any closing remarks.

Richard A. Galanti

Well, thank you very much. Bob and Jeff and I are here and we'll talk to you soon. Thank you.

Operator

This concludes today's conference call. You may now disconnect.