Costco Wholesale (NASDAQ:COST) F3Q 2013 Results Earnings Call May 30, 2013 11:00 AM ET

Executives

Richard Galanti - CFO

Analysts

Deborah Weinswig - Citigroup

John Heinbockel - Guggenheim Securities

Paul [Trestle]

Sandra Barker - Montag & Caldwell

Joe Feldman - Telsey Advisory Group

Chris Horvers - JPMorgan

Dan Binder - Jefferies & Company

Mark Miller - William Blair

Brian Nagel - Oppenheimer

Jason DeRise - UBS

Bob Drbul - Barclays

Peter Benedict - Robert W. Baird

Greg Melich - ISI Group

Operator

At this time, I would like to welcome everyone to the third quarter FY13 operating results conference call. [Operator Instructions] Thank you, Mr. Richard Galanti, CFO, you may begin.

Richard Galanti

Thank you, operator. Good morning to everyone. This morning’s press release reviews our third quarter operating results for the 12 weeks ended May 12.

As with every call, let me start by stating that the discussions we're having will include forward-looking statements within the meaning of the Private Securities 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 third quarter. For the quarter, earnings per share came in at $1.04 per share, up 18% from last year’s third quarter earnings per share of $0.88. For the third quarter, total sales were up 8%, and our reported comparable sales figure was up 5%.

During the quarter, sales were impacted by both gasoline price deflation and by weakening foreign currencies relative to the U.S. dollar year over year such that the 6% U.S. comp sales increase in Q3, excluding gas deflation, would have been 7%. Our reported international comp figure, assuming flat year over year FX rates, would have been plus 7%. And total company comps, again reported for the quarter, at 5%, excluding both gas deflation and FX impact, would have come in at 7% as well for the quarter.

In terms of new openings, after opening 14 new locations during the first half of the fiscal year, we opened 5 additional Costcos in the third quarter, two in Japan in Kitakyushu and Hiroshima, and one each in Chihuahua, Mexico; Wheaton, Maryland; and Southampton, U.K.

All told, that puts our fiscal year 2013 openings through the third quarter at 19 new locations, and we now operate 627 Costco warehouses around the world. Between now and September 1, the end of our fiscal year, we expect to open an additional 9 locations, 3 in the U.S., 3 in Japan, and one each in the U.K., Taiwan, and Australia, such that we'll most likely end the fiscal year with 28 new openings for the year. That's up from 16 net openings in fiscal '12.

Also this morning I'll review our membership trends, our ecommerce activity, and of course additional discussion about margins and SG&A. For our third quarter, again, sales were up 8% from $21.85 billion last year in the third quarter to $23.55 billion. Again, comps on a reported bases were plus 5.

Five percent reported comp sales results were a combination of a flat average transaction for the quarter. Of course that included the detriment from both the FX and gasoline, which together represented about 1.5 percentage points and an average shopping frequency increase of about 5.5%. That compares to a fiscal year to date shopping frequency number up about 4.5%. So a pretty strong frequency there.

Cannibalization for the quarter was pretty similar to what it was the prior quarter. That negatively impacted sales by approximately 60 basis points. And given our expansion, I don't anticipate much change in that.

In terms of sales comparisons by geographic regions, all U.S. regions were in the mid to high single digit comp increases, with Texas and the Southeast being the strongest. Internationally, expressed in local currencies, Korea and Taiwan were on the weak end of that range, with Canada and Mexico being the strongest in terms of comp sales increases.

In terms of merchandise categories, in terms of sales by merchandise category for the quarter, for the third quarter, within food and sundries, mostly in the mid single digit range, with deli, beer and wine, and candy being the relative standouts.

Within hardlines, overall in the high single-digit range. And departments with the strongest results were hardware, lawn and garden, and consumer electronics. Consumer electronics, sales were in the mid to high single digit range for the quarter.

For softlines, up about 10%. Small electrics, housewares, jewelry, and apparel were standouts, with media, as expected, continuing to be on the relatively weak side. And within fresh foods, where comp sales were in the high single-digit range, deli and produce showed a little better results than the other areas.

Moving to the line items of the income statement, membership fees came in at $531 million, up 12%, or $56 million, from last year's $475 million, also representing about an 8 basis point increase year over year.

In terms of membership, we continue to enjoy the strong renewal rates, and I'll go through that, continued increasing penetration of the executive membership, and of course, as I've mentioned for several quarters now, we're still benefitting from the $5 and $10 membership fee increases that began in November 2011 in the U.S. and Canada for new signups and in January 2012 for renewals.

Due to deferred accounting treatment for membership fees, of that $56 million increase during Q3, a little over half of it was due to that annual fee increase and how that rolls into the book P&L over about just under a two year period.

And as previously mentioned, membership fee income will continue to benefit from this deferred accounting for that fee increase throughout the fourth quarter of 2013 and to a lesser extent into the first fiscal quarter of 2014 this fall.

New membership signups in Q3, company-wide, were very strong, up 19% year over year. That strong performance is mostly reflective of the very strong signups we've had in our Asia openings this past March in Japan.

In terms of number of members at Q3 end, at Q2 end we had 27.8 million gold star members. At Q3 end, 12 weeks later, that was 28.2 million. Primary business went from 6.5 million a quarter ago to 6.6 million. Add ons remained at 3.5 million, and you add those numbers up, at Q2 end we had 37.9 million member households and 38.3 million at the end of the quarter. With the extra spouse card, 69.1 million at Q2 end and 69.9 million at Q3 end.

At May 12, the third quarter end, paid executive memberships were 13.3 million. The vast majority of that, of course, is in the U.S. and Canada. We also offer it now in the U.K. and Mexico. That 13.3 million, by the way, during the 12-week quarter, represented an increase of just under 250,000, or about 21,000 additional paid executive members per week increase.

Executive members are just over a third of our member base, and a little over two-thirds of our sales. On a year over year basis, the percentage of members being executive members was up about 1percentage point, which of course will translate into about a 2 basis point hit on margin with reward.

In terms of renewal rates, they continued strong. Again, going back a quarter ago, business renewal rates were 93.9. At the end of the quarter, they remained at 93.9. Gold star went from 88.8, tweaked up a little bit to 88.9. So total in the U.S. and Canada, these are United States and Canada numbers, was 89.8 at the beginning of the quarter, or at the end of last quarter, and tweaked up to 89.9 at the end of the third quarter.

Worldwide, at the end of the second quarter, I mentioned last quarter we were up at 86.5, and that tweaked down one tick to 86.4. Again, when you open new warehouses, you tend to start off with a lower renewal rate, particularly in countries outside the U.S. and Canada. And so that’s to be expected.

Going down the gross margin line, our gross margin in the third quarter was higher year over year by 12 basis points, coming in at a 10.67 in Q3 versus last year’s 10.55. As usually, I’ll ask you to jot down a few numbers. We’ll just do the third quarter here. Two columns, reported and without gas deflation. And the line items would be core merchandising. The second line item would be ancillary businesses, the third line item would be 2% reward, the fourth item would be LIFO, the fifth item would be other, and then the total, of course.

So, the two columns, across, the reported core merchandise margin was down 5 basis points, and without gas deflation, down 11. Ancillary businesses were plus 6 and plus 5. Two percent reward was minus 2 in both columns. LIFO was a credit of plus 6 in both columns. And other, which is a nonrecurring lawsuit recovery, which benefited margins this quarter by 7 basis points, so plus 7 and plus 7.

If you add the two columns up, the first column, of course reported, comes up to the plus 12 basis points that we reported. And without gas deflation, plus 5. The core merchandise component, again, was minus 5 on a reported basis and a minus 11, excluding the benefit of gas deflation.

The four core categories, food and sundries, hardlines, softlines, and fresh foods, each showed lower year over year gross margin percents as we continue to invest in price, both in our domestic and in our international operations. And as I've stated before, this is Costco playing offense. It's driving sales, member shopping frequency, member signups and renewals, and market share.

Ancillary business gross margin, as I mentioned, was up 6 or 5 without gas deflation, basis points. Margins were stronger in the one-hour photo mini labs, the optical, and the hearing aids. Slightly lower in pharmacy and gas was slightly positive.

The impact, as I mentioned earlier, on the executive membership increased penetration was minus 2 basis points. And as I mentioned, LIFO, the year over year is a 6 basis point swing. Basically we recorded an 8 million or 3 basis point pretax credit during this quarter. And lastly, other, as I mentioned, that's a nonrecurring legal settlement that we received in Q3.

Moving to reported SG&A, our SG&A percentages Q3 over Q3 were lower or better by a reported 3 basis points, coming in at a 982 this year versus the 985. And again, the two columns, reported and then without the gas deflation, and five line items: core operations, central, RSUs, quarterly adjustment, and total.

In terms of core operations, the reported piece was plus 2 basis points. Without gas, it would have been plus 7. And plus means lower or better. And so we had 7 basis points of positive there. Central was plus 2 and plus 2. RSUs was minus 1 and 0.

Quarterly adjustments, actually, was 0 and 0, such that total, we reported a plus 3, SG&A lower by 3 basis points. Again, in our view, on a more normalized basis it would have been lower by 9 basis points if you exclude the fact of gas deflation.

And a little editorial on SG&A, again, the reported 3, excluding inflation, would have been better by 9. The core operations component was better or lower by 2 year over year, and again 7 excluding gas deflation.

Within core, our payroll as a percent of sales improved year over year by 4 basis points. Total payroll dollars actually increased about 6.5% in the quarter compared to the 8% total sales increase.

This is due to an improvement in payroll. We were able to leverage benefits, including healthcare and worker's comp. They were leveraged during the quarter by a few basis points. Actual healthcare costs in the U.S., which is the key driver of this area, eased a little bit, up around 6% in dollars during the quarter. That's down from low double-digits in the past couple of quarters.

Our central expenses, as I just mentioned, was better or lower by 2 basis points. That's, by the way, notwithstanding the fact that the ongoing IT modernization costs, which I talked about in the last few quarters. During the quarter that represented about a hit to SG&A, or higher SG&A, of about

5 basis points. So notwithstanding that impact of minus 5, in the central category, we still showed a lower by 2 there.

So overall, I think, pretty good expense control and certainly helped by strong sales results as well. Next on the income statement, pre-opening: $6 million last year, and $10 million this year. We opened four net openings last year in Q3 and five this year. All told, operating income in the third quarter was up $100 million, or 16%, from $623 million last year to $722 million this year.

Below the operating income income line, reported interest expense was $6 million higher year over year in the quarter, coming in at $25 million versus $19 million a year ago. If you recall, last year on March 15, until a little over a month into the fiscal quarter, we paid off a $900 million fixed rate 5.4% interest debt. This represented about a $4 million reduction in interest expense year over year in the quarter.

Offsetting that $4 million reduction, of course, was our December offering of a $3.5 billion debt offering in late November, of senior notes with a weighted average interest rate of just under 1.25%. For the 12 weeks, that's about a $10 million increase, of course, in interest expense. The [full] reduction and the 10 increases [unintelligible] net increase that we're talking about here.

Interest income and other was lower year over year by $3 million, coming in at $15 million this year versus $18 million a year ago. About two-thirds of that $3 million delta is actual interest income being lower this year, coming in at $9 million this year compared to $11 million last year. And other rounded to the last million, both relatively similar numbers within the interest income and other line.

Overall, pretax earnings were up $90 million, or 14% from $622 million last year in the quarter to $712 million this year. In terms of our income tax rate, very close to being the same in both third fiscal quarters, 34.81% this year, down just a tick from 34.84% last year. So essentially the same year over year.

Overall net income was up 19% from $386 million last year to $459 million last year. While the balance sheet is included in this morning's press release, a couple of items I usually point out. Depreciation and amortization for the quarter totaled $221 million, and that brings year to date for the three quarters to $651 million.

If you look at the balance sheet, of course, if you look at accounts payable as a percentage of inventories, on a reported basis it was 104% a year ago and 102% at Q3 end. That includes payables for things other than merchandise, most particularly all the construction and expansion activity we've got going on. So if you look at just merchandise payables to actual inventories, it was 92% last year and a tick down at 91% this year.

In terms of average inventory per warehouse, I think in the last several quarters on a year over year basis, we've generally shown numbers in the $600,000 to $700,000 increase range, or 5-7%. This quarter, on a year over year basis, it was up $400,000 or 3%, coming on an average $12.2 million versus $11.8 million a year ago.

Just over half of the $400,000 increase related to higher levels of merchandise in food and sundries, scattered among various subdepartments. About $100,000 was consumer electronics, with the balance spread over a variety of other non-foods departments. Overall, inventory is in good shape. As well, our mid-year physical inventories, which were taken back in January and February, were our best ever, so we continue to do well, in our view, in terms of inventory control and how that relates to operations safety as well.

In terms of capex, in Q1 we spent $488 million. In Q2, $455 million. And the quarter just ended, $435 million. So to date, at just under $1.4 billion. Our estimate for the year is right at $2 billion, and that of course compares to fiscal '12 expenditures and capex of $1.5 billion, and of course reflects the fact that we're opening quite a few more units than we did a year ago.

In terms of Costco Online, we currently operate Costco ecommerce activities in the U.S., Canada, and more recently in the U.K. For the third quarter, sales and profits were up nicely over the last year. Q3 ecommerce sales were up over 20%, both in the U.S. and Canada and, as I mentioned, Costco U.K., which started less than a year ago.

In terms of expansion, as you'll recall, in the last two full fiscal years, in '11 we opened 20 net new units. In '12, 16. To date, for the first three quarters this year, 19, and our plans are to open 9 in the quarter. That would put us at 28 for the year. So, as compared to fiscal '12's expansion of about 3% in square footage growth, this year's 28 units, on a beginning base of 608 would be about 4.5%.

New locations by country, for the year, of the 28. Assuming the 28, it would be 13 in the U.S. and 3 in Canada, 3 in the U.K., 7 in Asia, one in Taiwan and Korea each, and 5 in Japan. And then as well, one additional unit in Australia and one in Mexico. As of Q3 end, our total square footage was 89.709 billion square feet, so again an increase of about 4.5% year over year.

In terms of common stock repurchases, as you know we purchased a small amount in Q1, about $34 million worth, and that's all the activity we've done so far. We did no additional repurchases in the second and third quarter.

In terms of dividends, our current quarterly dividend stands at $0.31 a share. That was recently increased about a month ago. Up 13% from the previous $0.275 a share. This annualized number of $1.24 per share represents a total cost to the company of about $550 million a year.

These quarterly dividends, of course, are in addition to the $7 per share special dividend, which totaled just over $3 billion that we paid out to shareholders back in December of 2012 or in the second quarter.

The usual supplemental information will be posted on the Costco investor relations site later this morning. Lastly, our scheduled earnings for Q4, which is the 16-week quarter that ends September 1, is currently planned for Wednesday, October 9. And again, that will be for the 16-week fourth quarter ending September 1. Mind you, last year was a 53-week year, and therefore a 17-week fiscal fourth quarter. So that was about 6% more days in the quarter, if you will.

With that, I will turn it back to the operator and be happy to answer any questions.

Question-and-Answer Session

Operator

[Operator instructions.] You have a question from Deborah Weinswig.

Deborah Weinswig - Citigroup

Can you talk about your frequency, which was obviously very strong in the quarter, on an absolute and relative basis? Can you talk about any unique drivers behind that?

Richard Galanti

Not really. We're not doing anything different other than continuing to be aggressive on pricing. And if you haven't tried our rotisserie chicken, that's the new hot dog in terms of $4.99 chickens. There's not been a lot of difference year over year in any of the [MVM] mailers, the coupon mailers. So not really.

We certainly are getting our share of free press out there, whether it's the late night talk shows or the morning business shows. But that's all anecdotal, of course. There's nothing specific that we have done different of late.

Deborah Weinswig - Citigroup

And then can you also discuss your [unintelligible] network as it stands right now?

Richard Galanti

You know, in talking to the buyers, there's not a lot of anticipatory inflation with the exception of some aspects of protein. They continue to see inflation in some of those items, beef, poultry, and pork. Some of what we call limited resource commodities like nuts, because of increased world demand, with the increasing middle class, if you will, those have spiked up. With those few exceptions, there's not a lot.

I think to date, if you used as your benchmark the LIFO calculation, which uses what our U.S. inventories, by item at cost, were and how those costs have changed from the beginning of the year to now, again, an ever so slight credit in each of this quarter and last quarter. I think together, if 100.00% was the base as of the beginning of the fiscal year, as of Q3 end, it was 99.41%, so 0.06 of a percent lower cost inflation. Now, again, that's one measurement that's easy to look at, because it's basically our U.S. LIFO inventory counts.

But that wasn't that discernibly different than a quarter ago. But we don't really see a whole lot of trend upward beyond those small areas that I mentioned. I think gas is always, who the heck knows.

Deborah Weinswig - Citigroup

And then on the executive membership side, which has obviously been incredibly successful in the U.S., beyond Canada, the U.K., and Mexico, how should we think about the growth there?

Richard Galanti

Well, we continue to look at it in all countries. I think we seem to like it, it works for us. Generally speaking, we like to have a core number of locations there and start off with some small number, but more than one of two, of services that we can provide under the executive member format. So the number of services where the executive members, in some cases, get a better deal on some of those services.

So, you know, I would guess over time we'll continue to roll it out to other countries. I mean, again, the 13.3 million, all but about 400,000 of that are in the U.S. and Canada, which of course is roughly 80% of our company in terms of sales or locations or what have you, and well over 95% of the executive member base. But that's because it started here.

Operator

Your next question comes from John Heinbockel.

John Heinbockel - Guggenheim Securities

The price investments, is there more of a skew toward consumables, or no, it's more broad-based than that?

Richard Galanti

It's more broad-based than that. Given just the sheer volume of items, what we need to make sure is we don't want to spread it out. You've got to be "wow" if you will, on items, and not just spread it across all categories and all items. And so we try to do a pretty good job of that. But it's spread among categories. I, a little tongue in cheek, talked about the chicken. I mean, as protein prices go up, our costs go up, and we've been very successful, we think, in driving sales and if we can get you to go to the back of the location and get that great chicken for $4.99, you're going to shop doing other things. So it's across the board.

John Heinbockel - Guggenheim Securities

So no matter what department you're talking about, the idea here is not so much where you can get your costs down, but where you can make a clear impression on the customer perception-wise?

Richard Galanti

Sure. Ultimately, it's an art form, and it's merchandising, and it's just across the board. Sometimes we work with vendors, and sometimes we rotate items in and out. It's not unlike what we do, historically, on the fence or endcaps. You're always going to see us try to create some excitement as you walk down those larger aisles, down the main aisles.

John Heinbockel - Guggenheim Securities

Do you think the price gap has changed, or widened, versus your various competitors, or no, it's about what it was?

Richard Galanti

I think it's been pretty similar over the last few years. We don't see any dramatic change in it. If anything, we tend to sincerely play offense and irrespective of what's going on out there. I mean, you're always going to see, be it our direct competitors such as Sam's and BJ's, or other category dominant retailers, items and departments. But for the most part, when we do our weekly by location market baskets on key competitive items, those ranges, in our view, of our competitiveness, is pretty similar to what it has been, if not a little higher, a little better.

John Heinbockel - Guggenheim Securities

More favorable to you?

Richard Galanti

Yeah.

John Heinbockel - Guggenheim Securities

Then just two last things. Is there about $30 million left of incremental benefit on the membership fee increase? Is that about the residual number?

Richard Galanti

It had a 3 in it. It's a little higher than 30. It starts with a 3.

John Heinbockel - Guggenheim Securities

And then lastly, when you look at Kirkland, where are you roughly now with SKU count? And do you think, as a percent club SKU count, that inevitably goes higher? And I know you don't want to force it on people, but obviously you continue to find value-added items. Does that just go higher over time as a percent of total SKU count?

Richard Galanti

Yes, absolutely. I think it's still in the low to lower mid 20s, but it keeps going up incrementally. Part of that is the increased penetration of some of those items overseas, where whatever extreme value we are, it's even more extreme on those kinds of things. We have items that do $2,000 and $4,000 a pallet position in the U.S. that do 5 and 10 times that in some of the Asian countries, simply because it's a great value on great stuff. And we can be even more extreme over there versus brands.

So yeah, we continue to look at different areas, and in this past year, I know we've put it on some women's exercise apparel, active wear, which has been very successful. I know we have several men's summer items, whether it's shorts, performance polo shirts. And so it's food and non-food. I don't see any discussion of putting it on a television or anything anytime soon. But certainly there's a lot of categories. You know, all the low-lying fruit, paper goods, water, those are all done. But probably the lowest lying fruit in the last few years was probably the disposable diapers.

But there's lots of things, it always amazes me when individual food items, the cashew clusters or something innocuous like that, is a $15 million item and $25 million and $30 million a year later. All of a sudden you've got those types of things out there. So, you know, I think it will scale slowly through the 20s and upward, but it's not like we have a concerted effort to try to get to a number by next year.

Operator

Your next question comes from Paul [Trestle].

Paul [Trestle]

Just with the price investments, you've had a very consistent message over the past few years in terms of Costco being on the offensive in terms of making consistent pricing investments. So should we look at the core being down this period compared to being more flattish the past two quarters as a signal that this is incremental, that this is, you know, in addition to what you've kind of done over the past few periods? Did you go deeper or wider? And how should we think about the next few quarters?

Richard Galanti

In all honesty, I don't think we're that smart about it, strategic about it. I think our strategy is to constantly drive it downward, and the more we can do that, the bigger gap we have with our competitors and the more our traffic grows, and the more our sales grow, and good things happen.

I remember somebody a few years back asking what happens if a month into a fiscal quarter you're not doing well, what do you do? And we say, we don't change what we're doing. I think that given our strength of late, we look at it and say this is a good time. When we look at certain countries where we're very profitable bottom line, as a percentage of sales, relative to the U.S. and Canada, and Canada a little more than the U.S., we're our own toughest competitor when things get too good.

And so again, I can't suggest that it's a trend. I think there were three or four quarters prior to the last three quarters, so all of last fiscal year, comparing those quarters to their respective comparable quarters a year earlier, it was down, and we were talking about investing in price. And then the last quarter or two was relatively flat, so does that suggest it's going to continue to be flat? Well, Q3 says no, it doesn't. But I don't think you could use that as a trend line either way.

We’re going to continue to do things to drive our business, and we’re fortunately in a positive way. We’d rather be aggressive on pricing and see the benefits of SG&A, which always has been a challenge for us. But margins are not a problem.

Paul [Trestle]

And international is becoming a bigger penetration of your business overall, and currently that segment has a few hundred basis points higher margins than the U.S. Is that sustainable? Or is there any changing dynamics that you see that might alter that?

Richard Galanti

Meaningfully higher, yes. Is it sustainable at this rate? Probably not. We know ourselves that as we take a $300 million unit in Taiwan or Korea or Japan and put a new unit 10 miles away, we’ll do $450 the next year between the two, but it’s going to hit the P&L for a couple three years. So part of this ramp up overseas is going to impact that a little bit, and as we’ve constantly been reminded, originally by Jim and now you can be assured by Craig, is let’s not have the illusion that we can just continue to be strong numbers.

Again, I think some of what you saw was a little bit of margin reduction year over year this quarter. There was a little more so internationally, and part of that is the things I mentioned, a little bit of the increased expansion and sitting in the meetings, saying guys, these numbers are growing pretty fast, let’s make sure we’re giving back price, in terms of price. So it’s our doing.

Operator

Your next question comes from Sandra Barker.

Sandra Barker - Montag & Caldwell

I just wanted to clarify, on the price investment internationally, don’t you have less competition there? I’m just wondering, I would imagine as you talk about the extreme value on some of the private label, I would think you already had a very large price gap versus the competition. And I had another question also.

Richard Galanti

We do, but again, if you look at a company that has a pretax return on sales in the three-ish range, very high twos or three, or whatever it is now, and then you look at that U.S. column and extrapolate from the operating percentages, that it's in the low to mid twos in the U.S., better in Canada, and a lot better in other countries, we're very good at looking at something and saying, guys, we're making too much here. And so we want to keep driving it in the right direction.

Sandra Barker - Montag & Caldwell

And then also, just some illumination on buyback and how you think about that in the future, since it seems to have dwindled away this year.

Richard Galanti

We look at it as between the regular dividend and the special dividend, and even assuming just the $34 million in stock buyback this year, we've still essentially, between the two, given back a lot of $3.5 billion to shareholders this year, virtually almost all in the form of dividends. But we look at both, and over a longer period of time we would expect to continue to buy back stock as well. But, again, we don't suggest it's going to be a certain number. Clearly, given the relative strength and, importantly, the fact that we did the special dividend, we don't feel any exterior pressure to just do it on a regular basis. We'll continue to do that over a period of time, though

Sandra Barker - Montag & Caldwell

And any commentary on any impact from Target in Canada?

Richard Galanti

Really, no. And without disrespect, there's really not been, in our view… Now, our margins in Canada have come down, and again, that's more us than that. Certainly, as I've mentioned over the last year and a half, we've been preemptive knowing that they're coming in. But we also have had very strong numbers. Our local currency comps up there are in the very low double digits in local currency. So it's a strong economy.

We're doing very well, and again, it's one of those things where Craig in the budget meeting says guys, let's not close our eyes and turn around one day and find out that we're not special, and let's get pricing back where it needs to be. And what that means is we're making good money up here, it's growing well, so let's make our competitive posture stronger. But a lot of it has to do with us, not really a lot of promotional pricing issues from what's going on with them. Keep in mind that they haven't opened a lot of units yet either.

Operator

Your next question comes from Joe Feldman.

Joe Feldman - Telsey Advisory Group

So just wanted to drill down on inventory again. I know you had mentioned you feel like you're in pretty decrease shape with inventory, but are there areas where you could be adding more or maybe where you're actually missing a sale because of not having the right product? Or just the opportunities within inventory management, I guess, and assortment planning?

Richard Galanti

Well, again it's part science and a lot of art form. As you probably know, over the last 10 years, we have consciously reduced our active SKU count in our warehouses from 4,100-4,200 down to 3, 700-3,800. And that's, in our view, driven sales because we could double [mass out] something versus taking out an item and replacing it with more of the other item. In that double space you will do more than you would have done with two items. So it's always that intelligent loss of sales.

I can only tell you that in the 26 days a year that we spend in a budget meeting, a third of which is merchandising discussions, and part of the operations discussions are also merchandising discussions, I hear many more comments from Craig and others when we have too many of something. You know, five varieties of cordless phones, or whatever it might be. So if anything, we continue to look to see how we can reduce our selection a little bit.

Now, we're also mindful it's the buyer's and the operator's responsibility, as they're visiting competition, to identify what they perceive as hot items. Not only at Sam's, but at other forms of retail, be it Home Depot or category dominant retailers or specialty retailers. And so we're constantly trying to figure out what we're missing. Generally, it's more the opposite though. What do we have too much of, too much selection of?

Joe Feldman - Telsey Advisory Group

About the traffic trend, which has just been so strong for so long, I guess I'm curious, how do you sustain it? Because people are coming in, it seems, at a pretty frequent pace, 4-5% every month, and it's better than grocery, it's better than most anybody else out there right now. And is it just the fact that you have a membership fee, so people feel like, well, I may as well get my money's worth and go to Costco? How you sustain it? I know it's a tougher, bigger-picture question, but just any thoughts on that?

Richard Galanti

Well, first of all, this is one person's view here, but I certainly believe that two big things that have occurred over the last four or five years in this bad economy is gas prices and the fact that 10-11% of our sales are gas, and that clearly drives people into the parking lot. And 30 or so of every 100 that pump gas go to shop. Clearly, even if one of those 30 is incremental, that's good, aside from having a profitable gas operation.

The other is fresh foods. All the statistics I've read is that when the economy got hammered, people ate out less, not just the steak houses for business travel, but families with neighborhood restaurants. While it's come back, it's not back to where it originally was, and clearly our strength in fresh foods, I think, has helped a lot. That, again, is a driver, in my view, of more frequency.

But I get back to the mission of constantly coming up with wow items and getting brands that refuse to sell us to sell us, and diverting more of stuff when they won't want to sell us if we can get it. All those things are what we're about, and again, I'm probably a little biased, and my antennae are a little stronger in looking, but it seems like every day there's something on television about us, whether it's a national talk show or a news item or a late night talk show, you name it. All that stuff, I think, is reinforcing.

The last thing, of course, is the ramp up and expansion outside the U.S. and Canada, our most mature markets. Clearly you have higher frequency numbers in newer markets. So that's got to help a little bit too. I don't think that's as big a factor, because it's still a small percentage of how many total units we have. I think the bigger factors are that constant lowering of price, and the gas and the fresh foods.

And look, we've all seen what's happened of late with some of the relative strength in companies like Home Depot and Lowes and the housing market. I think I mentioned some of the category areas where we've been strong. So we get a little benefit there as well. But that frequency has got to be more that.

I have no illusions that it can sustain itself. Seemingly for 20 years prior to late '08, on average the number was in the 1-1.5% range, and ranged generally from minus 1 to plus 2, with the exception of a couple of outliers based how Easter or July 4 or something falls year over year. So we're in uncharted territories.

I remember a year and a half into this recession, after having maybe a 4 for all of calendar '09, reminding people that if we're zero in 2010, that's still a 2 and a 2 for 2 years, and not ever thinking we could accomplish what we have. And so we've certainly benefited by our model and perhaps by the demographic of our member and by the other things I just mentioned.

Operator

Your next question comes from Chris Horvers.

Chris Horvers - JPMorgan

Wanted to follow up on the international margin side. The ramp in expansion, understanding that your investing in price internationally because you're more profitable there, and you're not resting on laurels, and also densifying the base. And that brings down existing profitability, but what's the other side of it? Does opening up new stores that are inherently more profitable relative to domestic, is that a net positive to margins for the company?

Richard Galanti

I'd have to honestly pencil it out. Probably a little, but I'm shooting from the hip on that one.

Chris Horvers - JPMorgan

Okay, I can follow up. And then also, a lot of retailers have talked about pressures from the weather and variability to the weather. You had a great quarter on the traffic side and on the comp side. But did you see much variation around weather? You saw strength in lawn and garden. Do you think it would have been better ex the weather impact, suggesting that maybe there's some pent up demand here that could flow through?

Richard Galanti

Fortunately, we're in, I think 41 or 42 states and Puerto Rico in the U.S., if you will, and so when the weather was bad in one part of the country, it wasn't bad in the other part of the country. I don't have the numbers in front of me, but I know over the last few months, when the regions got up and spoke, some of the regions had incredible strength when expected in seasonal items like seasonal clothing and seasonal patio furniture and what have you, whereas other regions it came a little later. I don't have the detail in front of me, but if there's a little pent up demand, it's in a few of the regions, and some of it's already happened in the third quarter. So maybe there's a little bit there, but I don't see a whole lot of that.

Chris Horvers - JPMorgan

Is that, in a similar vein, that the high exposure to California buffered your weather sensitivity?

Richard Galanti

Again, all the eight regions in the U.S. were pretty good. But they were actually at the low end of that range of I think I said mid to high single. It was still positive, but no.

Chris Horvers - JPMorgan

You mentioned about healthcare costs up 6% year over year versus low double-digit in the past quarters. What's changing there? Are you doing something? Is this in anticipation of Obamacare next year and that's blowing through early? And what's the outlook there?

Richard Galanti

You know, I wish I knew. For the 12-week quarters, when I looked each week at what we pay out in U.S. healthcare costs, which is the thing that drives that line item, it, generally speaking, was pretty consistent, in the mid, little higher, single digits. And so we didn't have any outliers.

Sometimes when you see a week or two that's a 3% or 5% increase year over year, the next week's 12% or 14%. And so the average was still 10% or whatever ex is.

And there's not a lot of new things we're doing. We're doing a couple of little things, but nothing that would have driven this. We're hopeful that it will continue, but we still budgeted up a little higher than Q3.

Operator

Your next question comes from Dan Binder.

Dan Binder - Jefferies & Company

First, any early view on how real estate is lining up for next fiscal year? Secondly, you commented on the seasonal business being lumpy. Was there any kind of gross margin hit related to seasonal businesses in the quarter?

Richard Galanti

Nothing out of the ordinary, on the latter question. And what was the first question? Real estate, yeah. Our forecast right now is right at that 30 number, with half or probably a little over half of it outside the U.S.

Dan Binder - Jefferies & Company

And of that 30 number, how many re secured or definitely going to fall into the year versus what might still be at risk?

Richard Galanti

I think there's more than 30 on the list, and you kind of just use a little guestimate by location, and we come up with a number that's close to 30. So it's a little too early to tell. If you asked me for a range, I'd probably say three less and five more than 30, so 27 to 35, but I'm guessing here. But 30's probably a good number.

Dan Binder - Jefferies & Company

And on membership fee growth, recognizing, due to the accrual accounting the tail end of benefit that you're getting from the membership fee increase, when we take that into account and the one less week in the quarter, any color you can provide from the impact of those two things versus the 11.8% growth rate that you were at here in Q3?

Richard Galanti

I think you can say, yeah the deferred accounting over the last three quarters, the number's in the 6-7% range probably in dollars. And when we look at Q4 last year, 17 weeks versus 16, one seventeenth is about 6 percentage points. So I don't have any Q4 estimates in front of me, but just those two simple math items would tell me that anything at or slightly above zero would be expected. But I haven't looked at it.

Operator

Your next question comes from Mark Miller.

Mark Miller - William Blair

I think you said payroll was up 6-plus percent in the quarter, and so if your dollar per hour wage increase is I think around 3%, that's implying your hours worked per club would be flattish. Is that correct? And if so, how are you managing that with the mid single digit traffic increase? I know you've got a signature change you put in with Amex, but what are the other key initiatives that are helping here?

Richard Galanti

Cutting overtime I think has helped a little bit. I've used the word focus before. I've also talked about, when people asked me a year ago, what's different about Craig? I mean, it's not a question of what's different about Craig versus Jim, but Craig would say himself his strength is he grew up in operations. So I think there's focus on that. SKU count management, going from X to a lower number means you're [unintelligible] out more stuff. I think it’s all the little things. You commented on the signatures being captured. Certainly yes, can that shave of seconds in a transaction? All those things help. But a lot of it is the pallet presentations and what we do.

Mark Miller - William Blair

And then can you give us some perspective on your efforts to get global pricing terms with suppliers? Are you getting traction on this? In the numbers it doesn’t necessarily look like we’re seeing it yet.

Richard Galanti

Yes, we are getting traction. It’s still not material to the size of our company. But again, every month, when the country heads from each country are here for two days, part of their presentation, and part of their offsite additional meetings with our merchants here, is getting, on a global basis, our buyers here to work with multinational vendors to make sure we’re getting better pricing. And in some cases, better availability of certain items. It’s a process.

Mark Miller - William Blair

What was the one-time legal settlement?

Richard Galanti

I can’t say what it is, but it’s a few year period of time where we picked up money that totaled about 7 basis points in the quarter. It was good, but it’s nonrecurring.

Operator

Your next question comes from Brian Nagel.

Brian Nagel - Oppenheimer

I wanted to focus on unit growth. A couple of questions. Someone asked you about the number for next year, and it sounds like you’re intending to open new units at a pace next year that’s consistent with this year. The question I have is what's allowing you now to more rapidly open units? Has something changed in the marketplace? Or was it a decision internally to do it? And as we look at beyond just this year and next year, is the company committed to continuing to open new units at a kind of longer term pace consistent with what we've seen this year?

Richard Galanti

To answer the last question first, yes. We've got literally more real estate people on the ground in more countries. The pipeline has taken time to fill up, but it's filled up. If you look back a few years ago when we had, just as an example in Korea, Taiwan, and Japan, 6 or 7 units in each of Korea, Taiwan, and maybe 8 or 9 in Japan, we've ramped that up.

And so we're going from opening, between those three countries a few years ago opening up a couple of units a year between the three countries, to opening up 5-8 between those three countries a year. But again, that's partly that conscious effort, both in the real estate area under Jeff [Bratman] and his people and Craig also pushing that. Yesterday and today, they're both out looking at sites in different parts of the country.

Our goal over the next five years, I think I've said, is about 150 buildings. And if we get a little better than that, great. But that's certainly a good starting point given where we've come over the last few years.

Brian Nagel - Oppenheimer

The unit growth numbers didn't hit your targets, or maybe what investors were thinking, and now you're showing a faster growth. So it sounds to me like you've kind of made the internal decision to grow faster. To any extent is it a competitive response? Are you seeing a need to jump out in front of a competitor? Or is it just internal decisions?

Richard Galanti

Sometimes it's competitive only from the standpoint that as we look at our success in other countries. We have a competitor in Korea. We recognize that. We're successful in several countries where we're the only one, and we want to do more of that.

We think that if you look back at the history of Canada, there was a competitor there that chose to not stay there. And I can remember the time when we had probably 55 or 60 units in Canada, thought one day we might have 75. Now we have in the high 80s, and we think we can get to a little over 100. So we'll keep doing that to drive our business.

So mostly it's not a reaction to others, it's a reaction that we're doing well and we want to keep ramping it up a little bit. And yeah, the decision to ramp up, as an example, internationally, given there is a longer timeline to get a unit open many times, was really made two or three years ago, and it's now coming to fruition this year.

Operator

Your next question comes from Jason DeRise.

Jason DeRise - UBS

Wanted to ask a bit more about the membership fees. Could you maybe share about how the membership grew without FX for this quarter, an organic number? And then if you could talk about how membership grew internationally versus U.S., that would be helpful.

Richard Galanti

Again, I think of the $56 million or whatever number increase, a little over half of it was the deferred accounting. And I think it was a 12% dollar increase, so that would imply about a 6% rounded dollar increase ex that deferred accounting. Overseas, I don't have the detail in front of me. My guess is that it's higher in local currency, but it was a little lower because of the fact that on average, on a weighted average, foreign currencies weaken relative to the dollar, so when you convert everything to report in U.S. dollars, it was actually a slight negative.

So you just made a light bulb go off. Actually, the underlying number, ex deferred accounting, in local currency probably would have been a little better, but again, the numbers we speak about when we show the membership income was including the detriment of weaker FX.

Jason DeRise - UBS

Right, the FX would be similar to the FX you see on your net sales, is that right?

Richard Galanti

Yeah.

Jason DeRise - UBS

And then I guess understanding the members from another point of view in terms of the traffic, obviously you give an all-in number. Do you have how international traffic is actually doing versus the U.S.? I know you alluded to that it's been good.

Richard Galanti

It's actually very similar to the U.S. But we're not going to go down the road of detailing it, because I always find as I try to put more out there then I've got to give it for the rest of my life.

Jason DeRise - UBS

Obviously, U.S. fee increases are very invisible to most of the investor base, but what's happening elsewhere in the world in terms of fee increases? And anything in the pipeline there?

Richard Galanti

We’re driving the business. Historically, we’ve shown that we’re prepared, and we will increase fees, but we’ll take that one step at a time. Again, I don’t want to suggest that we have a plan to do it tomorrow or a year from tomorrow, but I would guess over time you would start to see fees continue to go up. But then recognize what we do. When we have increased fees we get more competitive.

Operator

Your next question comes from Bob Drbul.

Bob Drbul - Barclays

Over the next several years, I know you talked about like 150 clubs. How many do you think you can have in the U.S. and how many of those clubs would you expect to be in the U.S. of the 150?

Richard Galanti

I think on our cheat sheet from last year it was 55 out of 150 were in the U.S. And my guess is it will be a little bit more than that. And if we open what we say we’re going to open this quarter, we will end the fiscal year with 636 units, of which 452 would be in the U.S. And if you add 50 or 55 to that, you’re at 505 or 510. And my guess is the five years after that, it’s not 50 more, but it’s 20 to 30 more, who knows?

So I think what we have found over almost 30 years, and what I assume we’ll continue to find, is we’ll always end up opening a few more than we thought were possible.

Operator

Your next question comes from Sean.

Sean

I guess on the international front, you talked about Mexico a little bit, and that does sound like one of the strengths in the international business. Can you just give us a little bit of an update on that business and how that market is performing? And is there an opportunity to grow a little bit more aggressively in this market, and how the productivity is doing in those boxes?

Richard Galanti

For the five years up to when we acquired the remaining 50%, last July, I think in the five years we opened a total of three units, so less than one a year. I think this year we're opening one. And my guess is that will quickly go to two to four, who knows? But we'll wrap it up. Keep in mind, we have 32 or 33 units there. Sam's has well over 100, and we think there's plenty of opportunity there. It's very profitable. And expressed in dollars, its average unit does about half the dollar volume because of just the relative currencies.

But it's growing nicely. Its bottom line is much stronger than the company as a whole. But so are a few other countries, in terms of the bottom line with a much stronger top line. So Mexico's great. It's been a healthy growth for us, and if anything, for unrelated reasons we hadn't grown a lot for those four or five years, and we're starting to invest more now.

Sean

And I guess from a category perspective, consumer electronics has been an area of strength. I think it inflected about maybe 12 months ago. And it sounds like the inventory is up a little bit on a per-warehouse basis. I guess can you talk about the strength, kind of what's driving that in this category? And then is the opportunity still there moving forward? And then is this an increase in the SKU, or is this more ASP related?

Richard Galanti

Yes, and yes, and yes. There’s a little bit more presence out there. We have done very well not only within TVs, but higher end TVs, the 60 and 80-inch TVs and the smart TVs. We’ve also done well on a much smaller scale dollar-wise, on cellphones. And doing much better in things like tablets, because we’re selling some. We’ve got all but one of the main brands names out there, and those are really starting to pick up for us. But you know, TVs dwarf everything else, just in sheer dollar volume. And again, they were up low double-digits this month. And I think in the last year have probably been up on average in the mid to high single-digits in dollars.

Operator

Your next question comes from Peter Benedict.

Peter Benedict - Robert W. Baird

Just back to the traffic question, can you give us a sense of maybe which member group is driving more of that traffic, if there is a difference? Is it the business member or the gold star member? Is there anything discernible there?

Richard Galanti

It’s executive. If you put it in simple sequence order, you’ve got your regular gold star, you’ve got your regular business, you’ve got your executive of either of those categories, and then the triple play, if you will, would be you’ve got the executive business member with the cobranded Amex card. All those things lend itself toward higher frequency and higher total purchases. But executive members clearly a driver.

Peter Benedict - Robert W. Baird

And then onto the SG&A, the 5 basis point headwind that you called out from the IT modernization efforts. How does that compare to the last few quarters? I don’t know if you can quantify the impact, but just wondering if that’s kind of typical, if that’s what it’s been running. And how long do you think it will persist, and when do you think we start to see some payback from those investments.

Richard Galanti

I think it's been probably a range of 4 to 6, but it's been pretty similar over the last few quarters. I think that will still be incrementally up over the next four quarters, but probably not 5, lower than that. And then hopefully it will subside a little bit. And hopefully then you get some benefit from it as well from more efficient operations, whatever we're putting out from it. But for those of you who have known us for a long time, we pride ourselves on keeping things simple.

And we are basically a legacy shop. We wrote our own GL years ago. And so this is new for us, and it's taking a lot of effort, and for us, a lot of money. Fortunately it's divided by a lot of sales of dollars. So 5 basis points is still a lot this year. I don't know if it's 2 or 3 next year, but it's going to be lower than 5 is my guess. And that will then not be a discussion topic in terms of SG&A basis points.

Peter Benedict - Robert W. Baird

And then just on the clubs left in the U.S., what do the markets look like that you're going to, the next 50 or 80 or so Costcos in the United States? How are they different than your existing footprint? Is there certain regions where you're going? Or is it different types formats, malls, etc.?

Richard Galanti

Quick back of the envelope guess would be half of it's in strong, existing markets and then half of it's in newer markets. I'm just looking at the opening schedule this past year. It's been everything from another unit in Washington, DC and Maryland in the U.S., to one last fall in Huntington Beach, California, which is clearly in-fill, to several units in the Dallas and other Texas markets, which I would say have gone from new markets to very clearly good in-fill markets. In Chicago as well, in-fill. To markets like

Knoxville, Tennessee, New Orleans, Louisiana. So a combination of both. Baxter, Minnesota. I'm not sure if that's an in-fill or an extension of Minneapolis. Just off the top of my head.

Operator

Your next question comes from Greg Melich.

Greg Melich - ISI Group

Wanted to follow up on the inflation in the quarter, or lack thereof. If I've got it right, gas and FX was 100-150 basis points, so ex those, ticket was up 1-1.5. How does that break down? Was there any inflation? Or was it all just items in the basket and mix that actually got some basket growth?

Richard Galanti

Very little inflation.

Greg Melich - ISI Group

I'm saying with LIFO gain, there might have been a little deflation, and maybe items in the basket or mix helped a couple hundred basis points.

Richard Galanti

[unintelligible] LIFO deflation, just from as of the beginning or the end of last fiscal year, not just this quarter. But yeah, literally it's a couple of basis points on our LIFO inventories in the U.S. So very little deflation, other than gas.

Greg Melich - ISI Group

What behavior have you seen with the dotcom sales up 20%? Who's driving that? Is it a small group of members that are using it a lot more? Or do you find that a lot of your members are trying the online site?

Richard Galanti

I think it’s a little of both. We’re still doing it the old fashioned way, and some would say the stubborn way. We are doing a few more things. Clearly replatforming, the dotcom people feel that’s helped. Mobile has helped a little. The apps are driving people to it. I forget what percentage of the total sales are coming on apps. It’s small, but it’s growing. And again, we don’t do a lot of stuff. Our MVMs probably, in our view, have had as much effect as anything, when we have some of those exclusive online-only MVM coupons in the physical mailers. Social network is up. We’re getting the name out there a little more. It’s nice to see some increases that didn’t have one digit or a one in front of it, two digit.

Greg Melich - ISI Group

And then lastly, on the cash flow, even with the capex up, do we still expect free cash flow to be around $1.5 billion, even with capex up this year? Can payables actually get to inventory? And then also, is it still the plan to buy back enough stock to make sure that there’s no option dilution. Now that you did the big special dividend, how are you thinking about that?

Richard Galanti

Clearly the special dividend had some impact on that. Clearly the very ramp up in strength in our valuation. But our view is we’re still, on average, a stock buyer over time. We don’t feel pressure that we’ve got to do a certain amount by a certain date. In terms of cash flow, you take your estimates for net income, take depreciation up, the 9% or 10% it’s up. Regular dividends, pretty close to what our 8-year average is, about 13%, or whatever. Your regular dividend is about 550 a year.

And assuming capex went from the $1.5 billion to the $2.0 billion, you’re going to cash flow a little higher than you suggested. But that assumes no stock buyback. And we’ll see. I would hope, and I can’t say expect, because we don’t look at it that formally every day, but over a period of time, we clearly want to cover our issue dilution, but we don’t feel compelled that we have to do it by year-end for this year.

Getting to 100 is tough. Seasonally, it gets over 100, sure, but I think on average it's probably 94-95 during the year. Maybe 93-94. And one of the things that happens, particularly in this low interest rate environment, and particularly since we have a lot of cash, we'll offer vendors, particularly medium sized vendors that might need to clean up a balance sheet at quarter end for certain covenants, we're being pretty aggressive on what will you give us if we pay you a little early on something? Outside the regular terms. These are not big numbers, but you turn around and its hundreds of millions of dollars.

I'm not sure if it ever gets to 100 unless the turn goes from the 12-13 up to 15 or something, and that's going to be tough. But we'll keep working at it.

Greg Melich - ISI Group

And how does international affect that payables? Maybe look at merchandise payables inventory? Does that sort of force it down a little bit?

Richard Galanti

I think it's higher volumes, but I think the payables percentage is a little lower in some of the countries. But part of that is timing, you know. Of a bunch that you ship to Asia, if 25-35% of our sales over there are U.S. sourced goods, and with the exception of probably fresh food items that have to be airfreighted, a lot of that stuff could be on two-week plus containers. Sometimes you're able to negotiate with a vendor to socialize that, and sometimes you're not.

I think I mentioned it was 91 for the quarter, merchandise payables, and that 91 there were two countries that were over 100 outside the U.S., and there were two countries that were below 80, and one in the 80s and a couple in the 90s. Of course, the U.S. and Canada are on average a shade above the 91 average. And us is right on it, so it's a little bit all over the board. I would guess Australia would be near the lower end, and that's because it's the longest place to ship goods by sea.

Operator

You have a follow up question from Sandra Barker.

Sandra Barker - Montag & Caldwell

I don't want to beat a dead horse about the price investment, but I just wanted to clarify, can you explain the mix of the price investment and how much of it is going toward international versus the U.S.? Because I know in the U.S. you had a fee increase, and that would be sort of a logical assumption that you'd be offsetting that there, but if it's more skewed toward international, is this a different philosophy than you've had in the past? And how are you sure that you get back more than you're giving up if you are the only club in a country, or if you're still sort of new and you have a ton of traffic already? I'm just trying to understand the philosophy there.

Richard Galanti

You know, every action has a different reason. Sometimes it's emotional, and it's what we do for a living. Sometimes it's, certainly as you just suggested, given our membership fee strength in the U.S. and Canada, that allows us to be more competitive in other areas, and certainly that's part of it. Given our strength and profitability in some countries, that gives us an opportunity to be more aggressive on certain things.

So I do want to emphasize, it's not as scientific or as analytically thoughtful, but we know when sales are going in the right direction, we can be more aggressive, and we choose to be. And it has worked for us.

And so I'm sorry I can't shed more light on it. If I look at the core businesses, I think probably the one that was least impacted was the U.S. this last quarter. But if you look at all the other countries, every country has a different reason. And it's not every country, it's all over the board. And sometimes it's on hot items, sometimes we're trying to build something.

Okay, well thank you very much, and happy to take any calls. Bob, Jeff, and I.