Costco Wholesale Corporation (NASDAQ:COST) Q4 2018 Results Earnings Conference Call October 4, 2018 5:00 PM ET

**Executives**

Richard Galanti - EVP and CFO

**Analysts**

Michael Lasser - UBS

Josh Kamboj - Morgan Stanley

Chuck Grom - Gordon Haskett

John Heinbockel - Guggenheim Securities LLC

Karen Short - Barclays

Christopher Horvers - JP Morgan

Edward Kelly - Credit Suisse North America

Paul Kearney - Wolfe Research

Jonathan Livers - RBC Capital Markets

Oliver Chen - Cowen and Company

Greg Melich - MoffettNathanson LLC

Matt Fassler - Goldman Sachs & Co

Peter Benedict - Robert W. Baird & Co.

Kelly Bania - BMO Capital Markets

Budd Bugatch - Raymond James

**Operator**

Good afternoon. My name is Britney, and I will be your conference operator today. At this time, I would like to welcome everyone to this Q4 Earnings Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

I would now like to turn the call over to our host, Mr. Richard Galanti.

**Richard Galanti**

Thank you, Britney, and good afternoon to everyone. I'll start by stating that these discussions will include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. 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. Forward-looking statements speak only as of the date they are made, and the Company does not undertake to update these statements except as required by law.

In today's press release, we reported our operating results for the fourth quarter of fiscal 2018 and the 16 weeks ended September 2nd.

Net income for the quarter came in at $1,043 million or $2.36 per share, a 13.5% increase compared to the $909 million or $2.08 per share in the 17-week fourth quarter last year. If you normalize the number of weeks, it's about a 20% increase.

In terms of sales. Net sales for the quarter came in at $43.4 billion, a 5% increase over the $41.4 billion last year, again 16 versus 17 weeks. On a comp basis which is on a like-week basis, comps were up 9.5% for the quarter. Sales for the 52-week fiscal year 2018, they increased 9.7% to

138.4 billion from $126.2 billion last year and the 53-week year; on a comp basis for the year as well, we reported a 9.5% comp.

Now, comp sales for the fourth quarter were as follows, and again from the press release. In the U.S. on a reported basis, was 10.8%; ex gas and FX, it would have been a 7.8. Canada, reported was a 5.7% for the 16 weeks; on a ex gas and FX was 4.6%. And other international 6.7% reported, a 6.9% ex gas and inflation -- gas inflation and FX. All told, total Company, as I mentioned, reported a 9.5%, ex gas and FX was 7.2%. As well e-commerce, which we have started reporting about a year ago on a monthly basis as well, e-commerce for the 16 weeks was a 26.2% comp, and ex gas and FX 26.3%.

In terms of Q4 sales metrics. Fourth quarter traffic or shopping frequency was up 4.9%, both on a worldwide basis as well as in the U.S. Weakening foreign currencies relative to the U.S. dollar negatively impacted sales by about 25 basis points and gas inflation benefited Q4 comps by about 260 basis points. Cannibalization by the way weighed on the comp by about 55 basis points negative. Our average frontend transaction was up 4.4% during Q4; and excluding the impacts of inflation and FX, our average ticket was up a little over 2%.

Next on the income statement line, membership income. We reported $997 million or 2.30% of membership fee income in Q4 of '18; last year in the 17-week quarter, it was $943 million, 2 basis points lower. So, about 54 -- on a reported basis, $54 million increase or up 5.7%, again on a like weeks basis up a little over 12%. Of this normalized 12% number increase year-over-year in Q4, a little over half related to membership fee increases, the majority of which came from the $5 and $10 annual fee increases taken last June 1st in the U.S. and Canada.

In terms of membership renewal rates. Renewal rates rose in Q4. In our U.S. and Canada membership renewal rate at Q4-end stood at 90.4%.

That's up from 90.1% at Q3-end 16 weeks earlier; and our worldwide rate improved from 87.9% -- improved to 87.9%, up from 87.5% at Q3-end.

In terms of number of members at Q4-end. At Q4-end, we had 40.7 million Gold Star households that's up from 16 weeks earlier 40.0 million; primary business 7.6 million, up from 7.5 million; business add-ons stood at 3.3 million, both at Q3-end and Q4-end. So, all told, we went from 50.9 million member households quarter ago end to 51.6 million at Q4-end. In terms of cardholders, we ended the year with 94.3 million cardholders, up from 93.0 million at Q3-end.

During the quarter, we had 13 net new openings. Also at Q4-end, paid executive memberships stood at 19.3 million that's an increase of 229,000 exec members during the 16 weeks or about 14,000 increase per week, which by the way is the same average for the whole year.

Related to the annual fee increases. The year-over-year quarterly fee income benefit peaked in this quarter, the fourth quarter. It will continue to be added to our numbers during the upcoming fourth quarters, very little in Q4 of '19, but during the four quarters, but will moderate each quarter. And this is due to the nature of deferred accounting treatment of the fee increases.

Going down to the gross margin line. Our reported gross margin in the fourth quarter was lower year-over-year by 35 basis points, coming in at 10.92%, down from 11.27%.

And that 35 basis-point negative, excluding gas inflation was minus 9 basis points. As I always ask you to do, go down two columns of numbers, one is Q4 '18 reported; and then, Q4 '18, ex gas inflation. The first line item would be core merchandise. On a year-over-year basis, on a reported basis, core merchandise was margin was down 44 basis points year-over-year, ex-gas inflation was down 22. Ancillary businesses were plus 14 reported and plus 21 ex-gas inflation; 2% reward plus 1 and minus 2 basis points. Other was minus 6 and minus 6 basis points year-over-year. If you add those two columns up, you'll get the 35 basis-point negative, which we reported and then minus 9 basis-point, which I just mentioned on an ex-gas inflation basis.

Now, the core merchandise component, again on reported basis was lower by 44 and lower by 22 ex-gas inflation; that still takes into account the sales penetration of the different categories. If you look at the core merchandise categories in relation to their own sales, core merchandise margin categories in terms of their own sales core on core, if you will, margins year-over-year in Q4 were lower by 2 basis points. Within the food and sundries and hardlines was up a little, softlines and fresh were down little. But all told, it was minus 2 on core on core.

Ancillary and other business gross margin, as I mentioned, was up 14 reported and up 21, ex-gas inflation. That's because of the extra good margins as well as the sales penetration. Other was minus 6, as was the case in the first three quarters of fiscal '18. I've mentioned to you that we're incurring some incremental costs, primarily related to the rollout of the centralized return facilities throughout the country. And during the quarter, that was a 4 basis-point detriment, which is relatively speaking, an improvement from the first three quarters.

In addition, we're cycling some one-time items that last year and the quarter -- which net-net benefited last year's quarter by two basis points with some positive legal settlement offset by some impact from last year's Hurricane Harvey.

Moving to SG&A. Our SG&A percentage was lower or better by 15 basis points; and on ex-gas inflation and FX, it was worse by 8 basis points, coming in at 9.82 of sales this year; that would be the 15 basis points lower than the 9.97 on a reported basis. Again, for ease of explanation, we'll jot down two columns of numbers, Q4 '18 as reported and then Q4 '18, ex-gas inflation.

Core operations is the first one, lower by 16, and I will say plus 16 basis points and minus 4 basis points or worse by 4 basis points on ex-gas inflation basis; central minus 4 and minus 7; stock compensation zero and zero; and other was a benefit, plus 3 and plus 3. Again, you add up the columns, you get on a reported basis, we were lower or better by 15 basis points and ex gas inflation, higher or worse by 8 basis points.

Now, the core operation component, I'd say, the U.S. wage increase that went into effect in June 11th to our hourly employees in the U.S., that negatively impacted SG&A by 6 basis points. And as I mentioned probably last quarter, this will continue to impact the SG&A comparison over the next three quarters, so June 11 through June 10th of next year.

Central expense was higher year-over-year in Q4 by 4 basis points, 7 ex gas inflation, IT expenses were 2 basis points of that, and the balance coming from a lot of small changes in a variety of miscellaneous items frankly. But, net-net, it added up to minus 7 ex gas. And lastly, other was better by 3; that related to expenses incurred last year on the SG&A line as well from the Hurricane Harvey.

Next, on the income statement, preopening expense. About the same year-over-year. This year, it came in at $31 million; last year, it was $30 million, so $1 million higher. Last year in the quarter, in Q4 we opened 15 openings, 13 net, plus a couple of relos. This year, we had 12 openings, 8 in the U.S. and Canada, and 4 international. All told, reported operating income for the 16-week Q4 of '18 came in at $1,446 million; this compares to a $1,450 million in the 17 weeks results of last year in the fourth quarter.

Below the operating income line, reported interest expense was $5 million lower year-over-year, coming at $48 million this in Q4 compared to $53 million last year. Interest income and other for the quarter was higher year-over-year by $29 million. Interest income itself was higher by $11 million, despite one less week year-over-year, a combination of higher interest rates earned on the cash proceeds, cash we have, as well as higher invested cash balances. Also benefitting the year-over-year comparison were positive year-over-year FX items that in total amounted to $14 million.

Overall, pretax income was higher by 2% or $30 million in this year's 16-week quarter, coming in at $1,449 million this year versus last year's 17 weeks results of $1,419 million.

In terms of income taxes. Our tax rate in Q4 '18 came in at 27.4% and 28.4% for all of fiscal '18. This compared to 27.4% for Q4 compared to last year's Q4 of 34.3%. This quarter's tax rate benefitted of course from the income tax reform that was effective January 1st as well as the favorable discrete tax adjustments. For fiscal '19, based on our current estimates, which of course are subject to change, we anticipate our effective total Company tax rate to be approximately 28%.

A few other items of note. During -- in all fiscal '18, we opened a net of 21 new units, plus additional -- 4 additional relos. Of the 21 net, 13 were in the United States and 8 were international. For '19, we expect to open 20 plus, in the low-20s net new warehouses. About 3 quarters will be in United States and about a quarter international. As well, we plan to relocate 4 units to better located and larger facilities, same number as we did this year.

We're also under construction with our first Costco in China in Shanghai with the opening expected late next September. As of Q4 end, total warehouse square footage stood right at 110 million square feet.

And next subject, stock buybacks. In Q4, we repurchased $89 million worth of Costco stock or 419,000 shares at an average price of $211.35. For all of 2018, we repurchased $322 million at an average price of 183.13 per share.

Moving to e-commerce activities. Overall e-commerce sales increase has continued at strong levels for the quarter, coming in at 26.2% and for the year, 32.2%. First and foremost, we continue to deliver great values for our members as well we continue improving and slightly expanding our offerings, including some new brands and higher end brands. We continue to improve the member experience as well. This past fiscal year, our site traffic conversion rates and orders, all improved year-over-year.

Online grocery, both our dry grocery as well as our -- our dry grocery two-day delivery as well as our same-day fresh delivery, the latter through Instacart and others like Shipt are growing nicely, but still a very small part of our Company's sales. In terms of online two-day grocery, which is the right side, we're generating sales in all 50 states including the 6 states where no physical Costcos are present, still relatively small to our Company.

We continue to improve the online merchandise and sales offerings and services offerings with Hot Buys and Buyer Picks, and buy online and pickup in store. And we'll continue to do exciting merchandising activities. Overall, all these efforts we feel are positively impacting our business, both online and in warehouse and are helping our sales increasing member awareness of our digital presence, as well as increased traffic that we've enjoyed in our warehouses.

The next subject I'll touch on is tariffs and their impact on our business. As you know, there are many moving parts and it's extremely fluid, starting with the actions and reactions by both the U.S. and Chinese governments. What actions are we exploring and taking in some short term and some long term? Accelerating shipments before tariffs go into effect; recognizing there's a limited ability to do so, everybody's trying to. Working with suppliers to see what can be done to reduce and/or absorb some of the costs. In some cases, reducing our commitments on certain impacted items. Alternative country sourcing, sure, but again, it's where possible and feasible; it's limited ability that takes time. Five, taking advantage of lower pricing on some U.S. items because of the reverse, if you will, such as pork, nuts and soybeans.

In summary, we'll have to see how customers and competitors react to tariffs and what impacts it will have remain to be seen.

Last topic, as was noted in this afternoon's press release. We plan to report in our Form 10-K a material weakness in internal control related to general IT controls. These controls relate to internal user access and program change management over certain of our IT systems that relate to our financial reporting processes. I can tell you that there have been no misstatements identified in the financial statements as a result of the deficiencies, and we expect to timely file our Form 10-K.

In terms of remediation. Remediation efforts have begun. But material weakness will not be considered remediated until the applicable controls operate for a sufficient period of time and we conclude through testing that controls are operating effectively. We expect that the remediation of the material weakness will be completed prior to the end of fiscal 2019.

Lastly, in terms of upcoming releases. We will announce our September sales results for the 5 weeks adding the Sunday, October 7th, next week on October 10th.

With that, I'll turn the call back over to Britney for Q&A. Thank you, Britney.

**Question-and-Answer Session**

**Operator**

[Operator Instructions] And at this time, we have a question from Michael Lasser.

**Q - Michael Lasser**

Good evening, Richard. Thanks a lot for taking my question. With the core gross margin down 2 basis points, the expectation was that you'd be taking some of the tax reform and investing it in the value proposition, particularly price. So, have those investments been made? And if they have, has it just been [technical difficulty] in areas? And where do you think your pricing now currently stands with others in the marketplace that have been investing in price?

**Richard Galanti**

Well, keep in mind, we invest in price as it's in our DNA. Certainly, over the last few years, there's been several buckets, if you will, that we've talked about, starting with the credit card transition that afforded us some great savings, some of which we used to invest in price, if you will; next was the what's occurred generally every five or six years, a fee increase in June of '17; and then, of course, the tax reform. And all those things I think have afforded us the ability. So, I don't know -- it's not like this one thing, but these monies are fungible. And we are not only investing in price, we're investing in infrastructure that we would have done anyway, remind you, with the initial successes of two-day and one-day fresh. So, there is a lot going on.

And in terms of how we feel competitively, I can tell you, every four weeks when we meet for our daily budget meeting in each of -- the U.S. as an example, each of the -- all regions, including foreign regions, but in the U.S., the eight geographic regions, they do price shops compared to our direct competitors, and we feel very good about those where we stand competitively. As it relates to monies that traditional retailers, whether it's supermarkets or the other big boxes, look, it works and it helps. But we think it impacts other traditional retailers a lot more than it does to us. I think that we've seen as evidenced by our strong traffic numbers and frankly our strong comps in store, we feel pretty good about where we stand on that.

**Michael Lasser**

You've been accelerating your e-commerce growth and it's growing at a very nice clip. So, would you consider further doubling down on some of your e-commerce investments in light of the fact that you've been able to show growth through both channels?

**Richard Galanti**

Well, doubling down, I guess there's going be lots of definitions of doubling down. I think, we are; I mean, we certainly are putting a lot of focus on. And I can tell you, within IT, we've got a lot of efforts going into fulfillment and sourcing and you name it. But, I think part of our long-term natured DNA is that we're going to do what we feel comfortable doing and grow it nicely. We've got a lot of activities in that area. We've added brands; we've added some categories. But for us, doubling or tripling 3,000 or 4,000 SKUs to 8,000 or 9,000 is a lot for us. But, there are plenty of opportunities that we're seeing, not only on adding products but the way we do it. We feel that the one and two-day delivery options that we now offer at frankly better prices and our items were being offered by other third parties before, dramatically better pricing, should help us, should help that process. We're finding the ability to benefit not only with e-commerce but using online and emails to drive traffic into the warehouse, again with Hot Buys and perhaps in some cases some targeted buys, and online and e-commerce to be able to sell some items that were seasonally in nature that we might only have for 8, 10, 12 weeks, notably, patio furniture and lawn and garden or furniture during the summer. But patio lawn and garden, we generally were in and out of that stuff for 10, 12 weeks. Now, we're in 52 weeks online and there are some real sales to be had there. So, part of it's on us to keep that awareness going and improving that awareness. I think we're doing a better job of it, but we have more to do there.

**Operator**

And your next question comes from the line of Simeon Gutman.

**Josh Kamboj**

Hi. This is Josh Kamboj on for Simeon Gutman. Thanks for taking our question. Your comps have been very strong for the last few quarters. If you look at the basket that consumers are buying, would you attribute the strength more to capturing a broader set of categories, or are customers trading up within your core consumable categories? And if the former, which new categories are you seeing the most success in?

**Richard Galanti**

It’s really pretty balanced, I think not only for us but other non-food retailers like Walmart, and Target and certainly Best Buy. Electronics has been strong, and there are some higher price points there in general. Apparel has been helpful to us. So, we’ve had some continued strong results for several years now in apparel, both brand and Kirkland Signature. And we keep trying to put another can in that package. So, I think all those things help. But, it’s more -- I’d say, it’s more broad based than specific.

**Josh Kamboj**

And then, just as a quick follow-up, looking at consumer health through your lens now. Gas prices had leveled off for a while. They’re beginning to rise again. Are you seeing greater sensitivity greater sensitivity in any of those categories?

**Richard Galanti**

Well, we haven’t yet, but again, every day is a new day. One thing -- we found that when gas prices were going down, some retailers were taking them down as much as they could have, in our view, which is fine with us. We could have gone down a little more, but still were able to make a little. So, that’s helped us and enhanced that value proposition. Generally, when prices go up, same thing, we generally can find where people are more conscious. I know -- I remember, back in the first part of calendar ‘08, when the economy was on fire and gas prices were north of $4 and some were saying it’s going to go to north $5, we saw a big increase in comp gallons. Same thing we’re seeing in the last couple of years; we’ve seen -- we’ve enjoyed a big increase in comp gallons because of that value proposition. It’s hard to say how that impacts our numbers. Our numbers are fortunately pretty good.

**Operator**

And your next question comes from the line of Chuck Grom.

**Chuck Grom**

Richard, just first question is on the ancillary part of the gross profit margin composition that you provided. Just wondering why the ancillary line was up 14 basis points, so it's a big reversal from the third quarter.

**Richard Galanti**

Well, the big thing is gas. Gas is now low double digit percent of our total sales on a price point that's 20-plus-percent higher per gallon than a year ago. And while it's a low-margin business relative to us, the Company, its margins had improved year-over-year. So, on that penetration, that helped us. E-com helped us a little as well.

**Chuck Grom**

So, e-com has sort of captured in that line item, okay. And then, the second question is, I know you guys have talked about -- you talked about sort of store targets in the low 30s; now, you're talking low 20s. Just wondering why that deceleration in number of openings planned for 2019?

**Richard Galanti**

Well, we have a budget that's -- it's between 20 and 25. So, I come in at the low 20s, just to be conservative. We've got more on plate. If you look at this year, this coming year, it's like three quarters one quarter U.S. There's more in the pipeline now internationally, but that pipeline takes longer to get through; it's longer pipeline. And so, I think you'll see that change, best guess, in 2020 and 2021. If I was a betting person, over the next five years beyond '19, probably some number in the mid-20s is a likely number, but we'll have to see; that's subject to change.

**Chuck Grom**

Okay. And then, just a last question on e-commerce. What do you think about the impact from consumers buying online? Have you seen any change and how their shopping in store? In other words, are they coming less frequently to the store? And I don't think you are too concerned about, but if you could just kind of flush out maybe the entire basket for and trends for total household when you blend in the store trips along with the online buying habits.

**Richard Galanti**

Well, I mean, the fact that traffic is actually as strong as it's ever been, we enjoy like a 4.2 [ph] average compounded annual traffic increase for seven years from '09 to '15. And I know everybody was concerned -- you guys, everybody was concerned when it got down to the low 3s and we've enjoyed it back in the 4s now and 4.95 the last couple of months I believe. And so, it's hard to say, should have been higher than that if e-commerce. We think it's been a net additive, but it's hard to say at this point.

**Operator**

And next we have a question from John Heinbockel.

**John Heinbockel**

So, Rich, let me start with the difference between the minus 22 margin ex deflation, and the minus 2 in their own category. So, obviously adverse mix; I think that's maybe picked up a little bit the last six months. What's the primary driver of that? Is that mostly the strength in electronics or are there other factors that work?

**Richard Galanti**

It's not mix, no. Electronics margins are generally where they've been; there is not a big issue there. It's gas. You've got a business that's -- what percentage of gas is our business now, 12%, 13%? 12% of our total Company sales is gas on a much different margin structure.

**John Heinbockel**

Yes. But, I think, when you pull out the -- so, ex gas deflation, right, I think, margins were down 22, but there were down only 2, right, when looked at in their own categories, but the difference between the two is not mix driven?

**Richard Galanti**

Well, it may be mix driven somewhat but keep in mind, there is lots of other things that go into margin. There is ancillary businesses that have high margins -- if you think about pharmacy and optical, their gross margin, which is sales minus cost of sales is a higher gross margin than the 40 to 50 we talked about, because it includes special optometrists and pharmacists. So, it's kind of like what is the price that customer is buying it all in that. And you've got other categories that have -- ancillary categories or services that have higher margins. So, all those things go into the mix.

**John Heinbockel**

But you're seeing penetration of KS continue to rise, and is it rising same as it had been, faster or slower?

**Richard Galanti**

I think it's been consistently rising, not faster or slower. Keep in mind, there is still new items out there. But, you've got a lot of items that start out at 10 and 20, and 30 million. The big items, like toilet paper and water. Yet, we saw a big growth over the last couple of years in water as -- where we brought the price down from $3.49 to $2.99. And just looking down the list of late, the Kirkland Signature 40 cartridge razor blades with a handle, several -- the organic cheeseburger in the food court, fragrances, the KS fragrances, all kinds of beverages.

**John Heinbockel**

Okay. And then, just separate topic. You obviously were doing some stuff with BOPUS on a limited basis, and I think you wanted to keep it limited. Is it still just applying to those items, right, the notebooks and the bags or is an idea of expanding that?

**Richard Galanti**

Well, we've talked -- in the past we've talked -- we mentioned things like jewelry, some limited electronics items like tablets, small sized items as well as handbags, high-end handbags and things. We have expanded it to some additional electronics items. But, it's still -- we still want to do it our way. We think that these are areas where we've been surprised that many people are buying it, because it's convenient and then, they are going to come by to shop. Not to suggest these are all incremental [ph] member shops, by no means. But while they are in there, are over half of them are not just picking up the item they're going into the shop. They frankly shop at a higher -- much higher average than the average shop. So, so far so good, and we will see.

**Operator**

And your next question comes from the line of Karen Short.

**Karen Short**

Hi. Thanks. I just wanted to start with e-commerce for a second. Can you just give us an update on where e-commerce is as a percent of sales? And then, I wanted to see if you could give us a little color on how to think about the growth rate of e-commerce going forward?

**Richard Galanti**

I'm sorry. What's the last part of the question?

**Karen Short**

How to think about the growth rate of e-commerce going forward?

**Richard Galanti**

Well, I mean, the number is right around 5% of sales, I think a shade under -- I'm sorry, a little over 4%. And, look, we're going to drive it as much as we can. I think, a few months ago when we went from a string of monthly 30 pluses to 23 or something, people were disappointed a little bit out there. We feel very good about it. I think, we've shown the last couple of months, I can't say anything about September, that will be next week, but we've seen the numbers that we feel -- look, we have the benefit of having not focused on a lot for many years and now taking advantage of that in a big way. And I mean, the example of some big ticket seasonal items like home furnishings and furniture one part of the year and adding 40 extra weeks of offerings if you will, offering online now, as well as what we've done with white goods and the success there. In three years, we've grown from $50 million to $500 million in white good sales, which has been helped of course by the brands willing to sell us good high-end stuff and our ability to sell it.

**Karen Short**

Okay. That's helpful. And then, just in terms of the tariff commentary that you made. Any way to give some sense of what percent of product is imported from China today and where you can see that going in the next few years?

**Richard Galanti**

It's really hard to -- no, we don't want to give out specifics. There have been some of the analysts out there that have done some estimates that are -- seem to be within the range, but it's fluid. But, the real answer is things can't change overnight. And what can change is demand for an item, if the price is set to go up 15% or 25%. But, we've experienced not dissimilar things. I mean, in Mexico when you got bunch of U.S. sourced goods historically, when the peso to the dollar has changed dramatically from 3 to 8 to 10, and then from 10 to 14 and more recently, the last couple of years from 14 to 18 to 20 range that'll have a dampening effect on certain products until it has less of a dampening product -- impact. So, it's really too early to tell.

**Karen Short**

Okay. And just last question. I guess, can you just give us inflation in 4Q, both cost and at retail, and then expectations, translation, given all the narrative from vendors base, since calling out passing on cost increases?

**Richard Galanti**

I don't know. I don't have that off the top my of head on a cost basis. And this is purely like looking at LIFO indices and not on sales, because some categories have a higher penetration. It's very small -- it's slightly inflationary. But I'm talking about capital S in the word slightly.

**Karen Short**

And then, what are your thoughts generally, because there has been a lot of narrative from the vendors in terms of passing on price increases? Where do you guys kind of stand or what are you seeing on that front?

**Richard Galanti**

Well, I mean, our DNA is we want to be the last to raise the price and we want to work with any supplier to figure out how to not do that. But ultimately, you can't eat all these. But, we feel competitively, we'll keep doing what we do that we're usually the last to raise the price and the first to lower. And I think, we have, as a company one advantage is, is that we don't have to sell every brand alternative, every size alternative, and every SKU alternative on given item. And there are times when I think we -- our buying power is in effect -- the octane of that buying power is more than $138 billion of purchasing power. Because it's much number of limited items and not only brands competing, but also what we know about many of these items because of our private label nature. So, it affords us I think some opportunities that perhaps make it a little easier for us. But nothing…

**Karen Short**

Thanks.

**Richard Galanti**

Thank you.

**Operator**

And your next question comes from the line of Christopher Horvers.

**Christopher Horvers**

So, first question is, you mentioned in the release that there have been no misstatements found related to the internal control weakness? What's-- is that the highness? Is there any risk that there could be a misstatement of the financials in the future or is that more about sort of just fixing the systems and getting the testing done?

**Richard Galanti**

Well, keep in mind first of all that we feel comfortable and we feel that ultimately our auditors feel comfortable. We would have expressed a level of comfort we did in the press release about the time that there's no misstatements and there is the timeliness [ph] that will be filed on time including the K. The issues had to do with internal user access, so people within IT or contractors. And when somebody who may have had access to something they should have and sometimes that they -- once they should have had that access relieved, it took a little too long to do so.

So, the controls weren't in place. We should have done a better job. We went back as far as we could and looked back as far as we could in some systems, for the entire fiscal year, which is what you want to do and some of the newer systems, there was no look back ability for certain things. I can tell you with all the look backs that we have done and then our outside help has done, has found no issues whatsoever in terms of misstatements or breaches. So, that's what we can tell you. But, we can't be more positive that until we release the 10-K. And so, I don't want to belittle it. We should have -- it should have been fixed it, but it's -- it was internal to us, not external and we'll go from there.

**Christopher Horvers**

Can you also talk about sort of the -- like an organic MFI growth number, sort of ex-FX and the 53rd week? It looks like all-in that that number was running a little bit below 5% in the first half of the year, and then in the third quarter sort of picked up over 5%, and then in the fourth quarter nearly 6%. Is that sort of rough math that you're seeing sort of like a MFI comp accelerating…

**Richard Galanti**

Well, that is -- that's pretty good rough math. But keep in mind, one of the issues is the deferred accounting. The U.S. and Canada $5 and $10 fee increases that went into effect June 1st of '17, so in effect, I believe that in total, it was $245 million. Well, in the next 12 months, using that number as the example, that's how much more we have in our checking account. Based on deferred accounting, it takes 23 months to get that into the P&L. And so, part of the increase from Q3 relative -- year-over-year Q3 relative to year-over-year Q4 is you peak in 12-month sense, if you think about it. Somebody who got a $10 increase for the first time, their renewal happen to be in June, that $10 was effectively $0.80 a month for 12 months, right June to May. Somebody who got it 11 months later in May, they paid it for the first time, 11 months after the first person did, that will hit the $0.80 a month for months 12 through 23, rough numbers. So, if you will, in month 12 is when you peak in terms of that -- getting what I'll call, the full effect of 1/12 of the 270 million -- 245 million as an example.

So, I think a little of it probably has to do with that. I wouldn't suggest that what used to be a 4% increase became a 5% and there is no 6%, some of that increase is related to that. And some of it of course is related to how many openings we have and when the openings are where we open a very successful unit on these side of Seattle and Redmond a year-and-a-half ago with three other units on these sites including Kirkland and Issaquah, we're headquartered here and one another. We went from 195,000 members or 65 per building on average, maybe we added another 8,000 or 10,000 over the next year. We've reduced the average members, but we added net of cannibalization, 120 to $130 million of extra sales in year one and we'll grow from there. So, when you do that that changes that growth metric a little bit. Similarly, when we opened in Australia or Asia, we're afforded huge numbers of new signups in the first year with a lower renewal rate. But nonetheless there have been openings where we've had 40,000, 50,000 new members with the company average for all warehouses whose average age is probably in the high-teens, if not in low 20s, an average in the low 60s of warehouse -- of 60-plus-thousand members. So, international impacts it. A few of the LivingSocial things that we've done once every year, year or two, all those things have backed that number a little bit.

**Christopher Horvers**

So, I guess, fighting through all the noise, how would you describe sort of like MFI comp trend over the past 12 months, has it improved?

**Richard Galanti**

I would say, -- well, if you take out the benefit of the fee increase and you take out the difference of weeks, my guess has been about the same. I'm guessing we picked up a little from some of the Sam's closings, the 63 Sam's closings, we opened up a couple of units less than we did a year ago, and I think proportionately a few less international units. I don't have that in front of me. So, all those things were tweaking a little bit one way or another. I think overall, the fact that our renewal rates have improved and continue to improve, finally after the impact of the transitions of credit cards in the U.S. and Canada makes us feel pretty good about it.

**Christopher Horvers**

And then, last question, could you give us how many Visa cardholders you have in the U.S. currently and how does that compare to when you entered in with from an AmEx cardholder perspective?

**Richard Galanti**

I don't have that number in front of me. It continues to grow. I believe that in the U.S., our Visa tenders -- total Visa, not just co-branded card, is just -- is approaching 50%, in the high 40s. And it's probably 55-45 the Costco co-branded Visa. That could be 60-40. I don't have that number in front of me. But, it continues to grow. We continue to get signups. And I think when somebody sees some of the things we've done with some of those monies, talked earlier about investing in price, when you can buy something like a high-end television, that's already at great value at Costco and then when it's on MVM or coupon, it's another 200 bucks off. And then, on top that if you use your Citi Visa card, not only you get a cash card -- and it's not on every item, but in terms of promotional things that we've done over some of the holidays, it's really worth. And so, those are kinds of things that we've used that for.

**Operator**

And your next question comes from the line of Edward Kelly.

**Edward Kelly**

Rich, I wanted to ask you about complements. I mean, if you could just maybe reflect a little bit on the impressive run that you had. It wasn't long ago in U.S. the comps had kind of slowed to the low single digits which now seems like a one-off. But, comps now are above historical -- what you think I guess historical norms. Can you just talk about what you think is driving that incremental strength? And then, how should we be thinking about, I don't know, I guess, what I would call mean reversion and the timing around that and what is the real mean? And is 2016 even relevant to think about?

**Richard Galanti**

Look, I don’t know, I never went to -- 2016, one, we did a little bit to hurt ourselves when we changed up in the MVMs and greatly reduced the number of promotional days or shopping if you will, and we changed that over a quarter -- over a few months and we got back to where we were. There’s also add-on that the conversion of credit cards where you had a lot of people that were auto renewal on credit card that lost our auto renewal. Any member under the old AmEx program was using it -- a different AmEx card at Costco, whether it was the Delta card or a hotel card, Starwood card, all those things -- some of those became auto renewal. Members opted in to just have auto renewal. Well, when we switched from one card -- one network to another, all those non-cards were bought by the acquirer, all those auto renewals went off. So, I think some of that is tied up into that ‘16 year.

I also think that some of the things we’ve done with Buyers’ Picks and Hot Buys and collecting email addresses, again we’re proud of the fact that we’ve greatly increased the number of email addresses we have. Some who look at it, say, why didn’t you do this all along? We did, and we’re not benefiting from that. So, all those things I think have helped us. And hopefully, the norm will continue for a while. But every day is a new day.

**Edward Kelly**

And then, just circling back on e-commerce growth. Obviously, you started the year strong. You’d actually mentioned something, Richard, about people being little bit disappointed when it slowed. Did that surprise at all that it slowed the way that it did? And can you talk about how grocery is ramping relative to your expectations, two-day, same-day, and are there any metrics that you can share relative to the basket size, margins et cetera?

**Richard Galanti**

Well, in terms of when renewal rates or comp slowed a little bit, remember when our shopping frequency had slowed a little bit after this incredible run from ‘09 to ‘15. I remember, at the end of ‘09, when we achieved I think 3.8

or 4.0 frequency up from historical average like 1.7, I was the first to say and remind people, if it's a lot lower in '10, it's still a good two-year stack because this is not sustainable. And then, for four years, we enjoyed it. But, I think you look at the things that we've done merchandising wise, the added brands we have, the better communications tools that we can communicate with our members, and really that low-hanging fruit that we are benefiting from on top of, as one of my colleagues just said, great merchandise at low prices. I mean, there is a lot of new things that we've had going on for ourselves. I think that should continue. We still have a lot of buckets here.

**Edward Kelly**

I meant on the e-commerce comp, e-commerce growth, and what we've seen recently there relatively how we started the year, has that that small slowdown surprised you at all, and how has like two-day…

**Richard Galanti**

The e-commerce slowed -- well, we say slowdown, went from a low 30s number to a low to mid 20s number. I'll through the two-year stack back at you. We feel very good about it. We feel very good about what we're doing. We think we've got a lot of new things to come on and to expand it. And we still have a lot of, if you will, funds in the bucket to drive business in that direction as well. And there are brands that are willing to sell us that historically haven't. So, all those things help. But, I think the biggest thing is we're focusing on it. But, we're focusing in our way. We don't need to go buy a company and we're finding out that there is a lot of opportunity for us doing some of the things that we want to do.

**Operator**

And your next question comes from the line of Scott Mushkin.

**Paul Kearney**

This is Paul Kearney on for Scott. Just a question on growth going forward and also business today. Where do you think you are in terms of wallet share of your current customers? And what's the biggest opportunity to grow wallet share with customers? And also, if you had to divide going forward where most of your growth is coming from, is it coming from wallet share, is it coming from acquiring new members or continued unit growth in new markets? Thanks.

**Richard Galanti**

Look, frequency is up; average sale is up. We know, there is an example when we did fill that we don't add a lot of new members, we have a lot of loyal members that are shopping a lot more frequently. We know there our success with both -- when we are asked question what are the big two or three things that impact that help our sales, I think generally speaking, we all generally feel it's our strength in fresh foods, which continues to grow and improve; it's our gas stations, which gets you in the parking lot; and the executive membership. And we're doing a better job of now emailing you. And so, I think all those things have helped. But, as our head of our merchandising would say, it's great merchandise at low prices, and some of these Buyers' Picks and Hot Buys have helped as well.

**Paul Kearney**

Great. Thanks. And one quick follow-up, and maybe it's too early to tell. But, are you seeing any changes in membership trends for your clubs that are more like heavily using Instacart. So, is Instacart delivery for non-members leading to any uptick in memberships for those clubs? Thanks.

**Richard Galanti**

Instacart and others, third parties like Shipt and others -- and Instacart is the big one. We have good relationships with them. And it's growing nicely. But, it's still a pretty small part of our -- we have not discerned any big difference there. When we looked -- and this is anecdotal, not statistically valid, but when we looked at it, you take a group of loyal Costco members and then a group within that group who had like characteristics of average basket to shopping frequency and they're loyal. And then, you have them -- some of them will start using Instacart, some of them are using to fill in, some of it. They may reduce their annual shops by a few and increase this way several. The key for us though is making sure they still get into Costco occasionally. And so far, we've seen a net increase in that but it's a very strong population and it's very small size in its entirety at this point.

**Operator**

Your next question comes from line of Scot Ciccarelli.

**Jonathan Livers**

Hi, Richard. Thanks for taking my question. This is Jonathan Livers on for Scot Ciccarelli. Just a question on e-commerce as well as it continues to be a focus and you've made sizable investments there and still putting up pretty impressive growth. Could you tell us what percentage of e-commerce is shipped I guess stores versus shipped by vendors?

**Richard Galanti**

Very little if -- I mean, 50% is us, but not to the warehouses, just us shipping directly from our e-commerce fulfillment centers. Very little is done at the warehouse.

**Jonathan Livers**

Okay…

**Richard Galanti**

And by the way, it's only the business center with our two-day dry.

**Operator**

And your next question comes from the line of Oliver Chen.

**Oliver Chen**

Hi, Richard. Regarding e-commerce, as it becomes a bigger percentage of your total business, what are the main dynamics in terms of the margin impact there? And you have been speaking about this, but what are your main -- how would you prioritize the main drivers to drive the awareness growth of e-com and the kinds of initiatives that you're pursuing as that seems like a big opportunity?

**Richard Galanti**

Again, we said before, first and foremost, we wanted to get into the facility. And there is certainly in some categories, like white goods and big ticket -- fiscal [ph] ticket items as well, e-commerce is the way to go in a big way, and we certainly benefitted from that. We don't see e-commerce taking over our brick and mortar. We've also tried to figure out how to do some of the e-commerce or delivery related activities that some members want and then we could provide savings too, but doing it our way. So, I think there is still plenty of low-hanging fruit. And, we don't want to get comfortable at just shopping at Costco online, unless there is not a Costco within 100 miles.

**Oliver Chen**

Okay. And Richard from a modeling perspective for CapEx for next year, what are some of the major buckets and how should we think about how that will unfold?

**Richard Galanti**

Well, first and foremost, it's warehouses. And to the extent there is few -- more international, couple of more, IT is few-hundred extra. I mean, it's not extra from the year before but general. We've got a chicken plant, which is north of $300 million, a big chunk of that is expended in fiscal '19 and we really started spending money. The cheapest money was the acreage; the expensive money is the facility and all the equipment and everything. And the whole fulfillment -- I guess, what's new would be some things like the chicken plant would be some of the fulfillment activities we have on two-day delivery, and e-commerce, small package e-com where that'll be a savings frankly to us. But we're just -- we are doing a lot of those things a lot more manual than we need to do.

**Oliver Chen**

Thank you. That's helpful.

**Richard Galanti**

[Multiple speakers] So, there's a few extra things. I think, the number would still be in the very high-2s ish, low 3…

**Oliver Chen**

Okay. And lastly, the multi-vendor-mailer. Are you pretty pleased with the state of it now? Is it in the right place? I know, it's an important document, and you've been thinking about making sure that it's sufficient with respect to breadth and depth?

**Richard Galanti**

Well, I think, we're pleased. Other than a year and a half ago, -- nine months when we changed the number of MVM days in the warehouse which hurt frequency in the warehouse, once we changed that back, the fact that we've reduced the number of offerings in an MVM by 20-plus-percent and increased the total value by more than that and by net positive, and it's definitely working in terms of what we want to get out of it. Remind you also, we've taken some of those items -- not every item is that works the same way. Sometimes some items that have been regular to get stale; sometimes we've got to shake it up a little bit or change the value proposition; sometimes we take it out of the MVM and do it in the different way with these Hot Buys and Buyers' Picks. So, I think we've in a way added to the arsenal a little bit, and it's working, but it's still -- it'll still evolve some more.

**Oliver Chen**

And do you believe that tariffs will contribute to risk factors with consumer confidence? Like, what are your thoughts on how that may interplay, because we have such -- we're in such a great backdrop currently?

**Richard Galanti**

Look, on an item given basis, when you have an expensive discretionary item, take like a patio set, I'm just using that as an using example. You're going to have a less demand probably. Is it going to change? I remind you, there's a few items on the food side that are going the other way, because this -- examples of pork where something like a third of the U.S. pork goes -- is exported to China; that's changed. Therefore, pork prices are way down, there's great savings. That's creating some opportunities. Same thing with nuts; same thing with soybeans, I believe. I'm just giving you some anecdotal examples. So, you're going to lose some and win some. How it impacts -- I think everybody feels that tariffs -- people smarter than me don't like them. And so, it's probably a small bit negative. Certainly, whatever negative it is, we can weather it better than others.

**Operator**

Your next question comes from the line of Greg Melich.

**Greg Melich**

Hi. Thanks, Richard. I had a couple of questions. One was on gasoline, obviously, grown a lot. But what was the gallon growth from the quarter, and did penny profit actually improve? It sounds like it did. But I just want to see if that's the case?

**Richard Galanti**

The gallon increases were in the low-double-digits, 11% or 12%.

**Greg Melich**

Got it.

**Richard Galanti**

Which is huge compared to the U.S. economy. That's also new gas stations as well. But I think the comp, it's got to be in the high singles.

**Greg Melich**

And how many new -- I mean, stations are at most of the clubs that you can have them, right, is there a penetration number you have?

**Richard Galanti**

Well, new openings are getting up more so than not. And internationally, we're still adding we can. I think, in the Australia with 10 locations we've got 4, maybe 5 with gas; Mexico, we are adding some; Japan, we have a few. U.S. and Canada certainly is more saturated with gas stations. And we would say we're not going to have one in 117th Street East Drive. But where we can -- generally speaking, where we relocate, we do. A good example in your neck of the woods is where we took the old land, occupied or constrained Hackensack at Costco and moved it to Teterbor, and then turned the Hackensack into business center. Teterbor is I'm guessing here 20,000 square feet larger with all the bells and whistles with the gas station and with a lot better parking, and so, a few here and a few there that way.

**Greg Melich**

And then, a follow-up on the cobranded card, if I did my math right, sort of upper 20% of the tender now would be on your card in the club. If I remember correctly, the part of the benefit of this is getting people top of wallet and getting them to use it everywhere. Do you have any sort of update on the usage of how much more it's being used outside of Costco, and therefore, how much more loyal that member is in terms of using the card and then, coming back to the club?

**Richard Galanti**

I'll just say, yes, we do. We do have that information. But we're not…

**Greg Melich**

Okay. Is it the same -- is it back to where it was with AmEx, I guess is what I would say, or above?

**Richard Galanti**

I think it's quite a bit above.

**Greg Melich**

Quite a bit above. That's very…

**Richard Galanti**

It continued to grow. And actually, keep in mind, part of that is the fact that it can be use at more places. So, if we get -- whichever of those cards was your top of wallet, you have more potential to use it today than you did before.

**Operator**

And your next question comes from the line of Matt Fassler.

**Matt Fassler**

My first question relates to SG&A, kind of couple of moving pieces. First of all, it looks like the wage increase that you discussed probably drove the SG&A higher by a bit less than the percentage points, so not an overwhelming increase. Just trying to benchmark the year-on-year increase when you exclude the factor of the extra week a year ago. I went back and you weren't terribly granular I think on last year's call about the expense profile of that extra week. So, as we think about the apples-to-apples increase because clearly the SG&A seems like it's going to -- might increase at a slightly accelerated rate with the wage increases. How -- was that an average week that you would have had for the extra week a year ago, are there expenses that don't get carried in for the extra week?

**Richard Galanti**

There is little, if any, expenses, similar to kind of what people said, virtually nothing. So, the weeks are fully allocated. It's not like if we took an annual expense and divide it by an extra week or had a free week at the end of the year, we don't. We do it by the number of days and the year, and so nothing there. What was the other part of the question? There was a response for it.

**Matt Fassler**

No. I think you got that one.

**Richard Galanti**

In terms of the wage increases related to the tax reform. At the time we did that, we announced it was going to be somewhere between $110 million to $120 million a year.

**Matt Fassler**

And so, I guess, partial impact here in Q4 given the June implementation…

**Richard Galanti**

Right. June 11 -- was about three quarters -- it was 12 -- even though Q4 is normally a 16-week quarter, not a 12-week, it was about 12 of the 16 weeks was this.

**Matt Fassler**

Secondly. Your inventory increase was a bit higher and it did speak to frontloading some receipts in anticipation of tariffs. Was that a factor, or anything else moving the inventory in that direction?

**Richard Galanti**

When I look at the list category-wise, electronics year-over-year is higher, by choice. A little of it -- some of it's volume but a little of it is what you just mentioned. And I think, the last thing is that we currently have increased our inventory levels, particularly in e-commerce and delivery-related items.

**Matt Fassler**

And then, finally, on renewal rates, you seem to have shaken off some of the cobwebs that emerged I guess in the period after the credit card transition, your U.S. and Canada renewal rate is back to where it was in the third quarter of 2016, so I guess the best in nine quarters or so and even more so for the worldwide rate. Have we sort of shaken the cobwebs off now? And are we -- do you think there's more room to move higher here or do you think we're kind of back at that level where we're likely to plateau?

**Richard Galanti**

Who knows? I think we feel good about the royalty and what we're doing to brand royalty, there's some things that impacted either little up or little down. It depends on rounding next tenth [ph] or not. When we do one of those -- I think we've done four of them now in the last four or five years, like the LivingSocial or anything like that; you'll get an extra 250,000 members in a 10-day period or 12-day period and would by definition have a lower renewal rate in your hands. So, that hurts you a little bit. And that anniversaries a year later and it helps you a little bit. So, there's lots of little things like that. But, when we look at the underlying, the rates and I look at -- even taking a country like Australia, which is really 10 locations, its renewal rate, it's still in the 70s, but it's relatively new. The average age of those locations is, what, four years-ish, maybe. And I look at the last four years, I only know this because I am going there next week, and its renewal rate has consistently improved for the company in each of the last four years, which is consistent with what we've seen in other countries. So, I think the bellwethers are of course U.S. and Canada where we're mature, the average age of these locations are in the 20s, and so far so good.

**Operator**

And your next question comes from the line of Peter Benedict.

**Peter Benedict**

Hey, Richard, a clarification just on the CapEx. I just want to make sure I heard you right. So, CapEx this year, high-2s, maybe low-3s with the incremental increase driven I guess part of it by the chicken plant. Is that the way we should think about it?

**Richard Galanti**

Yes. Typically, our own internal budgets are $200 million to $300 million above where we come out. I believe this year, we maybe were $100 million above, right at 3 or 3.1, and that includes the beginnings of the chicken plant, so additional things we're doing with fulfillment. So, I think overall, something in the high 2s or -- I think we've graduated from 2.5 to 2.8 range, to 2.8 to 3.1 range.

**Peter Benedict**

Do you have the fourth quarter CapEx number?

**Richard Galanti**

Not yet. It will be in the K in a couple of weeks.

**Peter Benedict**

Okay. On the international openings, you said 75% of the clubs this year are going to be in the U.S. But you said you got a bigger pipeline internationally, they take longer. Is there a timeframe where we should be thinking about when non-U.S. club openings will account for more than half of your openings, is that a couple years down the road?

**Richard Galanti**

If you had asked me couple of years ago, I would say it’s three years around the road. If you asked me today, it’s probably two to three-year around the road, and I could be wrong by a year further. We do definitely have more in the pipeline. And we have also been surprised by more opportunities in the U.S. that we -- if you go back to 10 plus years ago, some of the cities we’re in today, we would’ve said that we’re not going to go there. There is always -- there is somebody else there already and it’s not that big of a town. But we’re finding success in those examples. So, I think we -- ultimately international -- I don’t know what it is, whether it’s three years or four years from now or two years from now.

**Peter Benedict**

Okay. Last question just around brands, both yours and others’, which categories beyond white goods are you seeing kind of an incremental step up in your ability to get premium brands? And then what was the private label penetration for 4Q and for the year?

**Richard Galanti**

It can’t give you the latter number. But in terms of ability to get new brands, apparel continues, cosmetics, some specialty food items but those are fewer and further between, sporting goods to some extent.

**Operator**

And your next question comes from the line of Kelly Bania.

**Kelly Bania**

Hi. Thanks for taking my questions, Richard. Wanted to just ask about -- with e-commerce now about 4% of sales, just curious what percent of your members are really engaging online? And I guess in connection with kind of the renewal rates question. As you look at those members that are engaging online, are they renewing at a similar rate or higher rate, just curious how that could influence the renewal rates over time.

**Richard Galanti**

We don't disclose how many of our members. It's increasing dramatically but from a smaller base, because we have tried in the past. As it relates to -- I'm guessing, I know the Executive member is more frequent, more loyal than a Gold Star member. An Executive member with a Citi Visa card comes more often and spends more and is more loyal than that. I would guess that somebody who is using it online, if they come from the warehouse and they are using online in addition to that that's more loyal than their respective groups of those other things. But, beyond that, when you got somebody that's just using online, I don't know off the top of my head.

**Kelly Bania**

Okay. And just clarification on the CapEx, I think you mentioned some spend there going towards the two-day delivery program. I guess, what exactly is that for?

**Richard Galanti**

Well, the two-day delivery is with about seven -- most of that's e-com fulfillment. There is some additional expenditures in some of the business centers including building a couple of business centers in geographies that will greatly reduce the -- what I will call the outsized UPS fees relative to the current mileage that has to be traveled to give those packages to their customers.

**Kelly Bania**

Okay, got it. And maybe just one last one on wages. You've obviously been making investments. But with the announcement this week from Amazon going to $15, just curious if you see more pressure from that, or broadly speaking, and how you plan to go over the next couple of years?

**Richard Galanti**

Well, first of all, we've raised our entry level wages to $14 and $14.50 in United States in the past year related to tax reform. We give increases at top of the scale every year. Even though our starting wage is 14 to 14.50, an employee who's been here over number of years can get up into the equivalent of the low -- the mid-40s to the mid-50s on an hourly basis over time, on top of the great health benefits. So, at the end of the day, we feel very good about where we are. Employees starting today on a full time basis, it takes about five years to get the top of scale. And I think our average U.S. hourly wage is in the mid-22s, 22.5 roughly, which we believe dwarfs any other retail or retail type entity out there on a base scale. And I believe that you'll see more pressure on it. And by the way, there are some geographies around the country, even before we raised to it 14.50, we were already above that. We started at about a tranche or two above that because of necessities. Parts of the Bay Area would be an example.

**Kelly Bania**

Thank you.

**Richard Galanti**

One more question.

**Operator**

And your last question comes from the line of Budd Bugatch.

**Budd Bugatch**

Hi, Richard. Thank you for taking the question and thank you for lasting this long on the call. Most of my questions have been answered, but just on e-commerce. Can you give us the e-commerce impact on comps? Do we have that number?

**Richard Galanti**

I'm sorry, the comps?

**Budd Bugatch**

Yes, e-commerce impact on comps? How many basis points does it impact the comp?

**Richard Galanti**

It's somewhere in the 70 or 80 basis-point range.

**Budd Bugatch**

Okay. Thank you. And…

**Richard Galanti**

It's north of 50 and it's not 1.

**Budd Bugatch**

Say again.

**Richard Galanti**

It's not of 50 basis points and it's below 100. So, I think it's mid to high.

**Budd Bugatch**

And can you talk a little bit about the demographics of the membership signups by age? What does it look like? Is your average age of members reducing, getting younger, and what about the signup, distribution?

**Richard Galanti**

Well, we feel very good about the signups. But, by the way whether they are called Gen Xers or Gen Zs or whatever they were called before that, that's what you generally sign these people up. I think, we're in the very high-30s or low-40s in terms of younger people signing up, which is consistent with what we've seen. What was the other part of the question?

**Budd Bugatch**

That was just the impact on the pace?

**Richard Galanti**

I need to find that out myself. I haven't seen that since we told people that our average member in the U.S. went from 54 to 52. That was a number years ago.

**Budd Bugatch**

Okay. And the last on e-commerce. Is there e-commerce activity outside of the U.S., and can you talk about the strength that you might see there?

**Richard Galanti**

Well, we're in U.S., Canada, Mexico, UK, Taiwan and Korea. And over the next year and half, I think we have two other countries planned. And it's growing nicely in other markets. I frankly -- the U.S. e-com business dwarfs the others. And it's probably had the biggest benefit other than starting off of a very small base, because of where we had taken and combined in line and online buying together two years ago. And I think that we've seen a big benefit from that. We'll do that elsewhere. But, it works.

**Budd Bugatch**

Okay. Thank you very much. Good luck on that on the next period.

**Richard Galanti**

Thank you very much.

**Operator**

And this concludes today's conference call. You may now disconnect.