Costco Wholesale Corporation (NASDAQ:COST) Q3 2017 Earnings Conference Call May 25, 2017 5:00 PM ET

Executives

Richard Galanti - Chief Financial Officer

Analysts

John Heinbockel - Guggenheim Securities LLC

Simeon Gutman - Morgan Stanley

Michael Lasser - UBS

Karen Short - Barclays

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Matthew Fassler - Goldman Sachs

Paul Trussell - Deutsche Bank Research

Scott Mushkin - Wolfe Research

Brian Nagel - Oppenheimer

Scot Ciccarelli - RBC Capital Markets

Oliver Chen - Cowen & Company

Kelly Bania - BMO Capital Markets

Peter Benedict - Robert W. Baird

Greg Melich - Evercore ISI

Edward Kelly - Credit Suisse

Operator

Good afternoon. My name is Samantha and I will be your conference operator today. At this time, I would like to welcome everyone to the Q3 Earnings Conference 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] Thank you.

I would now like to turn the call over to Richard Galanti, Chief Financial Officer. Please go ahead.

Richard Galanti

Thank you, Samantha and good afternoon to everyone. I'll start by saying 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 we do not undertake to update these statements except as required by law.

In today's press release, we reported our third quarter and year-to-date fiscal year 2017 operating results for the 12-week and 36-week periods ended May 7th. For the 12-week fiscal third quarter, our reported earnings of $1.59 a share or $0.35 a share above last year's third quarter reported earnings of $1.24.

As noted, in this afternoons release, the $1.59 reported EPS figure included an $82 million or $0.19 per share income tax benefit in connection with the $7 a share special cash dividend that the company declared on April 25th and which is payable tomorrow May 26th.

The realized tax benefit related to the special dividend payable to company's 401k plan participants as it is considered compensation to employees under U.S. tax law. There is about a little over 30 million Costco shares held by employees among our other investments in the 401k plan.

In addition to this one time earnings benefit, here are few other items I would note, when comparing year-over-year results. Number one first, our co-branded credit card as well as the case in both the first and second fiscal quarters in this past year, the Citi Visa co-branded credit card program, positively impacted year-over-year margins by 16 basis points, and SG&A expenses by 20 basis points.

And our overall bottom line in Q3, benefitted earnings by $0.14 a share. By comparison and I believe in Q1 and Q2 the numbers were up $0.01 or $0.02 less than that per share, but still significant as we are still in the first year of the program change.

Number two, gas profitability, our profits from gas during the quarter as compared to last year's third quarter were higher by $37 million pre-tax or better year-over-year by $0.05 a share. Gross margin, last year's third quarter earnings included a $19 million pre-tax benefit from a non-recurring legal settlement and this represented an improvement of gross margin of 7 basis points year-over-year or $0.03 a share, which was in last year and not this year.

SG&A, this year's third quarter earnings included a $14 million or $0.02 a hit to SG&A this year related to two non-recurring legal items, so whereas last year had a benefit, this year had a detriment. IT expenses, as a percent of sales was actually flat year-over-year as percent of sales and in-line with sales growth during the quarter.

Number six, FX, the two FX items, as compared to year ago during the third quarter, foreign currencies where we operate were mixed relative to the U.S. dollar and our aggregate weakened versus the U.S. dollar most notably in Canada, the UK and Mexico and this resulted in our foreign earnings in Q3 where we convert back into U.S. dollars for reporting purposes being slightly lower by about $5 million or about $0.01 a share, then if the exchanges rates have been flat.

Conversely we had a gain reflected in our interest income and other line related to forward FX contracts and U.S. dollar holdings by our international subsidiaries, we do that when they use to pay for U.S. dollar denominated merchandize payables. In Q3 that benefited P&L by $9 million or a little over a $0.01 a share year-over-year.

LIFO, there was no LIFO charge or credit in this year's third quarter results whereas last year in the quarter we had LIFO credit of $13 million reflecting deflation in our LIFO indices. That represented about a $0.02 a share benefit credit last year and versus nothing this year but we do have deflation. There is no LIFO reserve to draw from and essentially you can't go below zero.

Income tax rate, as previously discussed, our third quarter tax rate was very favorable due to the treatment of the special dividend, as a result the reported tax rate in Q3 was 26.8%. Excluding the impact from the special dividend our normalized tax rate would have been 35.3% for the quarter.

Turning to our third quarter sales, reported sales were up 8% and our 12 week total company reported comparable sales figure was up 5%. For the quarter, the plus five comp sales figure was helped by gasoline price inflation to the tune of about 140 basis points and offset or hurt from FX by about minus 60 basis points.

By segment the company increases were as follows; U.S. six, Canada two, international four excluding the impacts from gas and FX, the six in the U.S. would have been at five, the reported Canada of two would have been three and the international reported at four would have been a six, still totaling up to five overall.

In terms of new openings, our opening activities and plans, we opened 12 net new locations during the first two fiscal quarters, the first half of the year; in Q3 we opened a net of two new units, three total and one [indiscernible], so including our 37th location in Mexico and our first business center in Canada in Ontario.

For all of fiscal 2017 we have current plans to open a total of 12 more locations, so 26 net locations for the year; of the 26 for the entire fiscal year 13 were in the U.S., six in Canada, on a base of 91, one each in Japan, Korea, Taiwan, Mexico and Australia as well as our first openings both in Iceland, which occurred two days ago, on Wednesday and France coming towards the end of next month in June. This afternoon I'll also review membership trends and renewal rates, the upcoming membership fee increases plan for the U.S. and Canada, those become effective next week on June 1st.

An update on the CV's Anywhere card program, additional discussion about our margins and expenses in the quarter. E-commerce results and the recent special dividend and related $3.8 billion debt offering that we completed recently.

So starting with improve results. As I mentioned, sales were up at $28.22 billion, up 8% over last year's $26.15 billion in the quarter. Again, on a reported basis and on ex-gas and FX basis, comps were up 5%. For the quarter, our 5% reported comp figure was a combination of an average transaction increased of 2% and an average shopping frequency increased a little over 3% and as little over 3% is something wide and was the 4% just in the U.S.

In terms of sales comparison by geography, Texas and Midwest regions were strongest, with Northwest, Southeast and California not far behind. Internationally, in local currencies, better performing countries the UK, Korea and Mexico. In terms of merchandise category sales for the quarter, for the third quarter within food and sundries and was up in the low-single-digits spirits, deli and candy were the leaders.

Tobacco continues to be a negative, and as we have mentioned in the last two to three quarters anniversary itself by the end of June the tobacco component. For hard lines, overall in the mid-single-digits, strongest department sales were in tires, hardware, and health and beauty aids. Our consumer electronics overall were down low singles. Soft lines also were up in the mid-single-digit range, with apparel, house wares and domestic showing these best results. And in fresh foods comps were up in the low-single-digits.

Within ancillary, gas had great comps in the quarter aided by of course the higher sell price per year to $2.42 per share versus $2.08 a year ago, as well as strong comp gallon growth. In addition, hearing aids were up in the mid-teens in terms of comps followed by optical in the high-singles and pharmacy in the low to mid-singles. In the third quarter, the U.S. front-end basket. U.S. units were just under percentage point. Well average basket value was slightly positive. These results now standing they were still seeing a little deflation in the core business.

Lastly, in Q3, the number of MVM promotional days, if they were to stay year-over-year in Q3 plan change from Q2 and year-over-year during the 12 weeks in the second quarter, they were 17 fewer in the MVM promotional days and as we have mentioned in the last call need to make changes. So the lack of promotional days wouldn't impact company as much as it had impact since the quarter.

Moving to the line items in the income statement, membership fees reported came in at $644 million, up 4% in dollars or $26 million and down eight basis points as a percent of sales. FX had a low to do with the dollar increased and also the number of new openings year-over-year in the quarter. In terms of membership, we continue enjoy strong renewal rates 90.2% in U.S., Canada 87.5% worldwide on a fully capture basis and we continue to see increasing penetration of the executive membership and those companies where we offer that.

At the end of the quarter, we had $37.8 million Gold Start members, up from 37.5 million 12 weeks earlier at the end of the second quarter. This is primary $7.4 million, the same quarter-over-quarter for 12 weeks. Business add-on $3.4 million and $3.4 million. Household we had $48.6 million member households that for $48.3 million 12-weeks earlier. Notwithstanding the effect where we just had a few openings in the quarter.

Total card holders, came in at the end of the quarter 88.9 million, up from 88.1 million at the end of the second quarter. Also at the end of the third quarter, paid Executive Memberships stood at 18.3 million, and increased during the 12-weeks of 345,000 new Executive Membership or about 29,000 a week increase in the quarter. Executive Members now represents about 38% of our member base, and about two-thirds of our sales closer to 70% of sales in those countries based on the countries where it operates.

In terms of renewal rates, business members renewed and these members would be in U.S. and Canada which is about over 80% of our business. Business came in at 94.1% at the end of the quarter, down from 94.3% at the end of the prior quarter consistent with what we have seen in the U.S. as we are still in the process in first year of year-over-year from moving the card over to the new Visa Citi card.

Gold Star, remains both at second quarter end and third quarter end at 89.5 and its total was 90.2 both in the quarter end, so again we rounding, causing some of that, but those are the numbers 90.2 both at second quarter end and at the third quarter end. Worldwide, which includes the outside of U.S. and Canada actually and at the end of the quarter it was 87.5, we rounded up to 87.7 at the end of the second quarter, which had been up from 87.5 at the end of the first quarter.

Regarding the increases in annual membership fees in the U.S. and Canada these go into effect again next week on June 1st, recall that we had taken fee increases in several of other countries this past September for us is the beginning of our current fiscal year. Our primary membership will increase

$5 to $60 and Executive Memberships will increase to $120 up $10. And with regard to Executive Membership the 2% reward caps associated with the Executive Membership is being increased from the current $750 per year level to a $1,000 per year level based on eligible purchases by these Executive Members.

In all, the fee increase impacts about 35 million member households will be impacted by it about half of whom are Executive Members and half of who are Primary Members, so $10 to $5. Note that the Membership fees are accounted for differed basis, so in terms of when it will benefits the membership fee income line of the P&L. The full P&L impact would be over 23 months timeline based on the fact that it's over the next 12 months that renewers will get their first increase and then it's differed over a year period from which from the time that they originally pay it.

Before continuing down the income statement a quick update and few updated stats on the Citi Visa card offering which began last June early in our fiscal fourth quarter of fiscal 2016. Recall we would began last June with approximately 11.4 million co-branded cards which represented 7.4 million accounts that were transferred to city at the conversion.

As of Q3 end we now have about 1.5 million new approve member accounts, which represents about 2 million new cards since the last June 20th and that 1.5 million that represents about 290,000 additional accounts over the past 12 weeks since Q2.

And overall we are seeing the Citi Visa co-branded portfolio total spend higher year-over-year that both organically from cards converted to Citi last June and from these new accounts. In terms of the conversion the usage in this signs-offs the card I think as I said a quarter ago and a quarter before that so far so good.

Turning down to the gross margin-line, gross margins reported were up eight basis points, I'll ask you to do a little metrics here, four columns, well there will be two columns for Q2 2017 and two for Q3 2017, column one will be reported to 2017 year-over-year, column two will be without gas inflation and then columns three and four again will be reported for Q3 2017 and then Q3 without gas inflation. Those would be the year-over-year basis points change.

The first line item is core merchandizing, in Q2 year-over-year was plus one basis points and ex-gas it was plus nine , and Q3 reported plus seven and ex-gas plus 20. Ancillary businesses, minus 20 and minus 18 in Q2 and the two columns of Q3 will be plus 15 and plus 19. 2% reward, zero and minus one, and then minus two and minus four, LIFO minus fives across the board, again having some deflation this year but comparing to credit deflation last year in the credit but nothing to credit since we are below zero there.

Other zero and zero in the two Q2 columns, and minus seven and minus seven in two Q3 columns, so all to all the year-over-year in Q2 we reported gross margins in Q2 down 24 basis points and ex-gas they were down 15, this year in the quarter there was plus eight reported and plus 23 ex-gas.

Now if you take the numbers that I talked to you about on the benefit from the change to Citi Visa as compared to what it would have been had we had the old program. We benefitted as I mentioned by 16 basis points year-over-year in Q3, and I believe in Q2 we also benefited year-over-year by 16. So again if you just simply look at the total of just two Q3 here, the reported plus eight would have been minus eight ex that single benefit of the Citi Visa and the plus 23 would have been plus seven ex that, and that's how it shook out.

Overall Q3 reported gross margin again as I mentioned was started by eight or reported basis 0.3% excluding, as I usually do I'll go through the core merchandize component which is about 80% of our sales, food and sundries, hardlines, soft lines and fresh foods, the core merchandize component gross margin was actually higher by seven basis points year-over-year and up 20 basis points excluding gas price inflation.

Excluding the benefits of Citi Visa, minus nine and plus four, so again the plus four excluding gas inflation will be the number if you look at here. I'm sorry, it's essentially wrong. The plus side it was what I really told about the whole company.

In terms of the subcategories at the core, food and sundries, hardlines, soft lines and fresh foods, as a percent of their own sales they were actually positive year-over-year in the quarter by 12 basis points, with food and sundries, and hardlines both higher year-over-year, our soft lines and fresh foods little bit year-over-year but net of all four under our sales was up 12.

Second, ancillary and other businesses gross margins were up about 15 basis points, about 19 ex-gas deflation, about two of theirs that year-over-year increase was due to higher gas profits as I mentioned earlier in the call, but even ex that the other ancillary businesses, that year-over-year were up a little bit.

2% rewards, minus two basis points and minus four ex-gas, that basically means more usage by numbers you get the 2% Executive Member reward into spend or more. LIFO I talked about twice already. And lastly the other that minus seven if you will is the fact that last year, that was an $19 million non-recurring legal settlement, which of course zero this year so it’s a minus seven year-over-year comparisons.

Overall, margins we felt were good, with solid results in the quarter to plus 12 basis points on core sales and gas margins again also positively contributing not only in terms of higher gross margin within the gas sales as well. Offset by negative year-over-year comparisons from LIFO in the one-time settlement from last year.

Moving onto SG&A, our SG&A percentage in Q3 year-over-year was low or better by 14 basis points, and that plus 14 will be flat or zero without gas inflation, coming but plus 14 was basically 10.44 versus 10.30 last year. Again as I mentioned earlier, the benefit effectively lower fees related to taking new card versus our own program. Year-over-year would have been better by 20 basis points in those numbers are in here. So again, I will ask you to do a little metrics with the same four columns, Q2 2017 reported and Q2 2017 ex-gas and then Q3 2017 reported and Q3 2017 ex-gas.

In terms of core operations, reported into 2017, we were up 8 basis points, I'm sorry better or lower by 8 basis points year-over-year, without gas better or lower by 1 basis point. And then Q3 reported lower or better by 21 and ex-gas lower better by nine. Central minus two and minus three, so that was higher by that amount year-over-year and minus one and minus three.

Stock compensation pretty much in-line with the sales, but it's always a big impact in the Q4, in Q1 what we do our big brand each year. Stock compensation was minus one and minus two or higher year-over-year in Q2, to two Q2 columns and minus one and minus one again a little higher in the Q3 columns. Other is zero to zero in Q2 in this two Q3 columns minus five and minus five and again that relates to the $14 million in the two legal items that we are non-recurring that impacted this year Q3.

Also told, last year in Q2, SG&A reported was lower or better by plus five basis points and in natural gas inflation higher or slightly higher by four basis points. This year reported better by 14 ex-gas zero basically flat and again I'll just use the two Q3 columns. If you take out the benefit from the Citi Visa conversion and that was 20 of the 14 if you will so ex that it would have been higher or over minus six and again the zero would have been higher or minus 20.

Now excluding the Citi Visa Central year-over-year was higher by basis point reported in three without gas. Nothing unusual to quarter, depreciation expense was slightly higher year-over-year again stock compensation expense was a basis point higher and that other was minus five.

Next on the income statement line. Pre-opening expense $3 million lower this year coming in the 15 million versus 18 million. Quite a few less openings, eight last year in the quarter and three this year and but that has to do timing of locations to all the pre-opening doesn't actually happen in the quarter, which the actual opening occurs.

And certainly this year's figure also include some of the pre-opening expense rate turn entry into two new countries Iceland and France. All told operating income in Q3 came in at 968 million or better by 110 million, which is 13% higher year-over-year. Below the operating income line reported interest expense came in at 21 million.

Interest expense in Q3 this year is quite a bit of a lower improvement from last year's Q3 came in at 21 million as 9 million lower than last year reported $30 million for a year. Virtually all of it is due to the payments back in March of the our 1.1 billion, 5.5% fixed rate note that we as a [indiscernible] year note that we paid it off on March 15th, so that is about 60 million a year annualized interest savings since that end March 15th date.

As we reported last week, we successfully completed a new debt issuances totaling 3.8 million and that was done in fourth tranches, there was an $800 million five year tranche and then three $1 billion tranches at five, seven and 10 years. The details of that can be found in the press release dated May 9th. [indiscernible] the new debt have the un-mounted rate of little over 2.6%. As well on May 15th we gave notice of early pay-off of our December 2017 $1.1 billion 108% notes and the expected pay-off date will June 15, 2017.

Next line item on the income statement, interest income and other, it was higher year-over-year by $11 million coming in at 18 million in Q3 as compared to 7 million a year earlier. Now actual interest income for the quarter was better, but better year-over-year by 2 million. In addition we have benefitted by about 9 million I mentioned that earlier in credits mostly relating to the various FX items discussions and that I have discussed in the beginning of the call.

So adding these two line items, from operating income overall pre-tax income was higher by a 130 million or 16%, coming in at 965 million this year during 12 weeks as compared to 835 million a year-ago.

Again in terms of income taxes our reported tax rate this quarter of 26.8% normalized that would be 35.3 and that compares to last year 34.2, and we would expect it to be in that 35.3-ish range for the year. Overall, reported net income came in right at $700 million and that's compared to our reported $545 million a year-ago.

A quick rundown of the other usual topics. The balance sheet as included in this afternoons release, a couple of quick items that I always go through that one of them that’s not on their is depreciation and amortization for the quarter total $320 million and year-to-date $929 million.

One of the metrics we always look at is accounts payable as a percent of inventories as through the balance sheet came in at 97% it was 99% a year-ago in the quarter. We also take on all the non-merchandize payables and we calculate it so it's merchandize payables as a percent of inventories and that to came down two percentage points from 89 a year-ago to 87 so there is still a vast majority of inventories being trade balance.

Average inventory per warehouse that was up $693,000, coming in at $13.4 million compared to $12.70 million a year ago, about almost that quite 40% of it was majors electronic, we are seeing a big shift and finally a big increase and particularly in TVs kind of the next generation of bigger more K and you name it as well as some other electronics areas.

Small increases in various other departments as well some buildup in inventories related specifically to our e-commerce as just in the last year we have gone from seven to 19 e-commerce fulfillment centers in the U.S. year-over-year, but many of those and mostly those are connected to our depot operations we not their building along the new warehouses just for that.

In terms of CapEx, In Q1 , we spent $670 million. In the Q2 515 and Q3 538, so year-to-date we are at 1.723 billion. And overall for the year we'd probably be in the 2.5 to 2.7 range, probably it's maybe 100 less than we had estimated the quarter or so ago, just a couple as you saw in the number we are expecting 26 for the year, just a few delays nothing terribly different.

In terms of e-commerce we continue in the locations where we were 12 weeks ago, U.S., Canada, UK, Mexico, Korea, Taiwan, and we expect to do additional countries over the next one and a half or so years. For Q3 sales and profits were up, online sales were up 11% a quarter as well as comps at the same locations. Within the 12 weeks, we look at four week periods ourselves, that came net 11, represented 13 or 14 in the seventh, and the seven was weak in part due to the shift in both Easter, Mother's Day, but overall the number for the quarter was 11.

We continue to improve our offerings, and enhance our member experience, we continue to add new areas of merchandize, improved in-stocks on high velocity items as evidenced by conditional inventories in those areas and more locations. In April, we launched something new GE Appliances along with their self services delivery schedule, it's starting off well, but again it's just started off, and we will continue to add additional names.

In terms of online Kirkland Signature items, we recently launched Kirkland Signature maternity apparel, they have all so expanded from our KS groceries and consumable items on dot-com, and if you are in the mood for A4 Wagyu Center Cut New York Strip Steaks, we apparently have a great deal on four or 12 ounce steaks for $499.99. In terms of improving the experience functionality we have improved search, streamlined the checkout process both mobile and desktop, improved the members ability to track orders and Nevada made in much of the merchandize returns process.

Now, many people have that, we are newer to it, but we have done a good job I think in the last six to nine months of getting that member experience and functionality a lot better on the site.

Overall good things are happening online and both in terms of member experience and expanded products and certainly the great value is to our members. We still want you to come into the warehouse of course.

Next discussion expansion, as mentioned for the third quarter we opened three locations clearly one reload so net of two, quite of a lot openings in Q4, 12 total including Iceland just a couple of days ago. In fiscal 2016 if you recall we opened 29 units, so about 4.5% square footage growth, this year it was at 26 if it wasn't been delayed into the fall, 26 for the year that will be about 4% square footage growth, of the 26, half 13 are in the U.S., a quarter six are in Canada, and then one each in those countries that I mentioned earlier. And again of course this is our first locations opened to fans which is scheduled for I believe June 22nd and again Iceland just opened.

Total square footage some of you asked about Q3 ended sort of 105.4 million square feet. In terms of buybacks in Q1 we brought back $122 million worth, Q2, $66 million, Q3, $45 million, total of $233 million of stock or 1.486 million shares at an average of about $156.5. Regarding dividends in addition to special dividend, we increased our quarterly dividend, that was announced also on April 25th.

The new amount is $0.50 per share per quarter, so $2 a year, that's up 11% from the prior $0.45 a share and again that will be also be paid tomorrow on May 26th or 56 quarterly amount. The $2 a share annualized dividend represents a total annual cost of company of about just under $900 million. And as I mentioned earlier, the $7 share driven that will be paid on to shareholders tomorrow as well.

Lastly, our fiscal 2017 fourth quarter scheduled earnings release date and this is for the 17-week this international week in the year. For the 17-week fourth quarter that Amazon that is September 3rd, we will do the earnings release after the market closes on Thursday October 5th, with the earnings calls that afternoon it to get to be a pacific time.

With that, happy to open it up for a questions-and-answers. And I'll turn it back over to Samantha.

Question-and-Answer Session

Operator

[Operator Instructions]. Your first question comes from the line of John Heinbockel.

John Heinbockel

So Richard, first topic expansion and business centers. So you have added some more there is couple of coming here in the next month or so. How do you think about business centers versus regular clubs number one? And when you think about is there a big potential business center expansion here. And then lastly on expansion when you think about, is it too early to think about 2018 and we sort of get back to 30 openings worldwide next year?

Richard Galanti

Well, first of all with regard to the business centers, I think we started the year with 14 and signed up four this year so 18, that should be up by 1, and are first in Canada, we call that we had business centers for, I think we are going from four or five to seven or eight over about 10 plus years. And so we continue to be hit and news say we have found something that seems to work now and then there is a little method to that madness.

And but it's corollary to what our primary businesses is opening full Costco membership warehouses. And we were continue to open more, but I think again this is guess at this point. But on assuming the base at end of the year is 18 that should be up one using that two to seven or two to six or three to five, I mean, that will be in that range for the next couple of years. We are not looking to go from 14 to 18 to 28 in a year.

And so far so good, I think a couple of years ago, we said to ourselves one day that this would be since there would be 13 or 14 weeks who knows. I remember when we said years ago one day could we have 100 Costco's in the U.S. and we are approaching 500. So it’s by no means, the same as it regular royal spot in terms of capacity a lot lower than that but I just look at more of general to the last couple of years and extrapolate that for the time being.

John Heinbockel

Okay, and then and is it too early for next year? Can we think about...

Richard Galanti

Surely, it's too early I mean it is I mean our goals will be to get towards that but it seems to be challenging this year and but we can work in towards that end.

John Heinbockel

And then lastly on gross margin so if I look at ancillary ex-gas ancillaries that maybe six or seven basis points so was that anyone department to rise that and sort of how is pharmacy doing within that. And then the major categories within their own sales, so that was improved about five basis points versus last quarter. Is there anything to that or that was fairly broad based?

Richard Galanti

I think it's more broad based than anything. I think pharmacy is fine. That was sustaining all the challenges with that industry has and we have continued to [indiscernible] putting all there. Now I don’t see if there is anything specific I think it gets more back to the call a quarter ago where we said things are okay and it's not like we have it's changed a lot but these are going to fluctuate some basis points up and down periodically.

John Heinbockel

Okay, thank you.

Operator

Your next question comes from the line of Simeon Gutman.

Simeon Gutman

Hey Richard and thanks for the color on the bigger more K TVs. My serious question is first to get the lien gross profit dynamics for Q4. Can you just give us a sense relative compare. And then I'm going to have one follow-up?

Richard Galanti

Right, as everyone knows when oil prices go up we make a little less, our margins come down we make a less and when they go down we make a little more year-over-year Q3 that's where the period gas prices generally were going down that was good. But I think the direction when asked on the second quarter call which Q2 haven't been a great comparison with the other way.

We didn’t think it was going to be this good but we would also did know the cash prices have been key down they have gone up lately, so we will see as we had very good profits last year in Q4 some of that has to do there is a trends down towards the end of summer prices in general ex what is going into the market but it's that's why we show every corner and because there is going to be fluctuations that are dictated by what oil prices are doing.

Simeon Gutman

Got it, okay. And then my follow-up is on the credit card. Can you share with us were about I guess it's almost the year away from cycling the initial I guess the initial change over can you share with us - I know there is a few buckets of margin that we are helping some of its new sign-ups some it's the spend outside of Costco. Can you give us a sense and we lap the initial been effort from last year, what accretes - what the additive and year-over-year versus what it goes away I'm guessing that the bounty's on the new signups will probably fade, but can you just share with us how we should think about it?

Richard Galanti

Well, I mean generically the biggest bang is in the first year is there a little extra - on the one hand there is little extra because things maybe there were some transition challenges right around there for few weeks okay that's good news going forward for little bit longer. But there was also more incentive and a bigger bank for your bucks and the first time you offer it you get more sign-ups in the first week and the second week than the third week as no more sign-ups being more bounty. So generally speaking, we still think it will be a net accretive if you will or additives to the company in the second year but the big bang is in the first year.

Simeon Gutman

Okay, thanks.

Richard Galanti

And if you look at Q4, Q4 there is five or six weeks of the big bang if you will before June 20th and 10 or 11 weeks afterwards so and there is a little bit above the two-thirds of its after that anniversary.

Simeon Gutman

Okay, thanks.

Operator

Your next question comes from the line of Michael Lasser.

Michael Lasser

My first question is on e-commerce growth which was in the low double-digits in the quarter. Richard are you mindful of maintaining your relevant online especially at a time when other traditional retailers are aggressively growing their e-com presence yet one of your big box competitors talk about 69% e-com growth in the most recent quarter and I believe you are 11% came on an easier comparison it sounds like it flowed throughout the period, so are you mindful of that at all?

Richard Galanti

I guess I'll use my phrase that I used several times on the last call, not to be arrogant or cavalier about it but we feel good about what we are doing, we have got great brick-and-mortar comps, we are doing things offensively in our view, not defensively on mind and we have got a lot of things going on the online side but we are not really worried about what others are doing and there is lot of good things about online and there is challenges and we are trying to do more of the good things but again we will look into the way we do it, don't expect us to increase by 69% partly through acquisition and we are going to keep doing organically, we think we have got, we made a lot of changes in the last year probably more than we had in the last several years online, and that will show some good results.

Michael Lasser

My follow-up question is on the group core gross margin being up 20 basis points, that's on the heels of you making some investment in everyday low price in the prior quarter, so did you get the intended effect of those price investments, and is there now an opportunity to do more especially as your gross margin continues to float up?

Richard Galanti

Well I think the 12 year is 12 on the core, I have already turned that sheet to the side, but look we are going to always do more investing in price, just when you think it's safe to go outside you guys we are going to drive sales top-line and certainly the fact that our margins are strong that we have got upcoming fee increases just starting that we have got additional monies from the credit card, all of those things allow us to do things in an offensive way and drive our business and so we kind of think we can do both, have decent margins and drive our business and lower prices.

Michael Lasser

I just follow-up on that, because you mentioned the upcoming fee increase in your response to the answering about price investments, should we expect that a good portion more than half would be - that if you get enough fee increase you are going back on the price?

Richard Galanti

Well I can't really tell you that, but we are known for giving a lots of things back to the consumer, to remember and it's not completely formulated but we are going to constantly try to excite our members and drive our competitors crazy.

Michael Lasser

Thank you very much and good luck.

Operator

Your next question comes from the line of [indiscernible].

Unidentified Analyst

Good afternoon Richard. A couple of questions here, first curious that penetration on the new Visa card as you use the tender here in the third quarter and relative to the first half of the year and also curious to where it was relative to when you had the agreement with AmEx?

Richard Galanti

Well I think we are talking in U.S. dollars because it's a U.S. program, I believe we are in 46 range currently and that's trended up since its inception a year ago, I think the highest we were on AmEx that was with AmEx co-brand, it was -- by the way but that number I'm giving you is all Visa not just Citi Visa because we accept all Visa's and we excepted all AmEx cards, not just the Costco co-brand one, I believe we have got up to the 43, 44 range, and so we have exceeded that but we wouldn't expect it to given the improved value proposition to the member, and the fact that there is just more market share out there and more places probably rewards garden to be used and again more incentive for that part to be used everywhere which helps us as well.

Unidentified Analyst

And has the basket changed at all?

Richard Galanti

I don’t know, and I know there was some anecdotal items in the very beginning at the transition on big ticket items like hearing aids or big screen TVs or furniture but I think the answer is yes it has a probably has a plus sign in front of it is so the minus but not huge and again as more anecdotal stories I have heard I didn’t heard anything big. The biggest thing in terms of the whole part is the fact the inside and outside spend, we are very successful under our own program over 14 or 16 years getting the outside spend on that card up to, to get to 2.5 plus for every dollar spend inside.

And that where this issuers all of the issuers wherever the co-brand card is they want more spend on that card because that creates APR that creates carry balances and late fees and everything else, and it's just a big in portfolio. And as we would expect, given the greater market share presence that a Visa has in the market there is going to be more usage if we can get that member to have that as top of wallet there is going to be more usage on it and that's exactly what is happened. Anything that get the expectations have been little better than planning on that.

Unidentified Analyst

Okay, and just switching gears a little bit Michael's question on e-commerce I think you said 11% growth. Can you just remind us where the penetration is today and also the numbers SKUs that you guys are offering online so we realize you don’t want to have the 350 million that Amazon has, but how big do you think you can grow that and then also on the margin profile the e-commerce business have you believe it's better than your brick-and-mortar margins just wondering if you could clarify that directionally?

Richard Galanti

Yes, well the sales are about little under 3.5% of sales again is the year that we are going to end up doing just extrapolating the first three quarters something in the mid-120s we had an extra weekend there to this year. And so again it's over a well over 4 billion now. And that's we don’t that's pure e-commerce online we do have delivery online, and we don’t include that we have travel online we don’t include that it's just been normal online that we started with.

And I'm sorry, in terms of profitability nothing has really changed their generally speaking the gross margin of dot-com compared to the gross margin of warehouse as gas the four walls of the warehouse, the warehouse is a little higher. The SG&A on dot-com is a lot lower, so the pre-tax earnings of dot-com it is higher and nothing has really changed there.

Unidentified Analyst

Okay, and just number of SKUs and if you have at the percentage overlap of those SKUs relative to what is in store?

Richard Galanti

As we had somebody had I think there the SKU challenge ex-office supplies because that's not through a third party and there is 8,000 or 10,000 [Indiscernible] I believe, but I think we have got about 8,000 to 10,000 items and that's exclusive of like - about 2,000 of the roughly 4,000 in the warehouse are online.

Unidentified Analyst

Okay, perfect. Thanks very much.

Richard Galanti

And I need to say fresh foods is not online other than through third-parties like Google or like Instacart or like that in Google.

Operator

Your next question comes from the line of Karen Short.

Karen Short

Hi thanks for taking my question. I just actually trying to get a sense on the gross margin in terms of the MVM. How much was a change in the MVM from Q2 to 3Q or how much of this does year-over-year change in margin-at-margin in 2Q versus 3Q would have been a function of the end game changes and then just wondering what is the number of days on the MVM we can expect in 4Q 2017 versus 4Q 2016? And then I just got another follow-up?

Richard Galanti

Okay. Well, first of all in terms of the number of days, I think it's like four or less this coming year versus a year ago. Three or four? It's a few days, so not totally meaningful, I mean the big meaningful was in Q2 when it was 17 less on 84 days. And I'm sorry the other question, Karen, the first one you had asked.

Karen Short

Well when we just look at how the merchandize margin in 2Q versus merchandize margin change in 3Q, I guess how much of the difference I mean sequentially was due to the MVM changes, like the pressure that you had in 2Q versus what we are looking out on 3Q?

Richard Galanti

I think the biggest change from Q2 year-on-year and Q3 year-on-year was the number of MVM days. we are still being pretty aggressive on the MVM being fewer items with better savings and it's plus a little more if you will that have a seat at the table there from a vendor merchandizing standpoint. But we are also [indiscernible] if we need to - we are not here just to drive margins down, we have got lot of buckets of stuff and when you have increasing kind of inflation and some higher margins areas like fresh foods or some high margins area like pharmacy, those things help as well. But there is something in little pieces that can effect it. Overall we felt pretty good about the Q3 comparison versus the Q2. But there is no material change.

Karen Short

Okay. And then I guess just as obviously we are kind of getting out of a deflationary period and into flat or maybe slightly inflationary there has just been a lot of questioning as to how deflation impacted your P&L versus how inflation will impact your P&L and I guess I just want to talk through that a little because it would seems to me that deflation, because you had some much tonnage, it actually is a double set, because you have so much more labor involved in meeting the demand. So I don't know if there is any way you try to talk through a little bit on how much more easing I guess you'd have on the P&L as we are no longer in a deflationary period [indiscernible].

Richard Galanti

Well I think for low margin retailers and certainly we are at the low end and the lowest end of margins, but super market is well on the food side, a little inflation is good, a little deflation hurts you a little bit it still has the D in front of it, not the IN and so it’s still impacting some. it hurts you most in items like I think the example I gave last quarter was of fresh meats where year-over-year, second quarter or first quarter year-over-year per pound beef was down by 10% and we were selling more than 10% more tonnage and certainly we are having lower gross margin dollars because of that and so as that changes that will help us a little bit.

Karen Short

Well I guess presumably higher growth SG&A dollars to you because of the labor content, that's kind of where I'm getting at it, there seems like you didn’t have a lot…

Richard Galanti

Actually on the fresh foods we have higher labor, inflation would help all those things.

Karen Short

Okay. Thanks.

Operator

Your next question comes from the line of Zach Fadem.

Zachary Fadem

Hi good evening. So, Kirkland Signature continues to perform pretty well, just to what extent is this growth coming at the expense of branded items if any and when you think about positioning the brand going forward are there any areas where you think Kirkland is underpenetrated and work pursuing expansion?

Richard Galanti

Well, I'm sure of it in term of the expensive branded some of that though in some cases it's the branded manufacturers they are supplying as not always by no means not all the time and but it's another competitor and again we are pretty transparent about it we want brands and private label and so we will continue to see both of those. it really is an item business and some of the success on the - all of the big items I mean paper trails, water, giant items that are 100s of millions as dollar - we have a several items that are billion dollars in unit sales several KS items.

In some cases we have a billion plus dollars on the branded side of the same time, whether it's assortment or bounty and Kirkland Signature one those two items whether it's various regional brand names of order of its Kirkland Signature order. And it works for us and we will continue to do that.

Our new category, while I think in the last in the last year or two I think the thing that has done very well for us is the wine and spirits and that continues to have some legs and substantial legs and the good news like other KS items when the brands loose the market share they get sharper on their own prices which with us not only with everybody hopefully which makes it a season more competitive more on the brands. So all of that stuff works in our view will sure benefit and having the brand loyalty certainly helps with membership and wanting them to come back to Costco.

Other areas our voice apparel still has legs if you will and arms I guess. You have got cosmetics organic items and there has been several organic items probably every month of the budget meeting we see new organic items whether its chicken broth or beef broth or some candy caramel chocolate things or nuts clusters and these are $10 million to $25 million whole margin items for us without competitor. In terms of it's not replacing a branded item necessarily.

We have done really well in some of the other snack items and energy bar items. We have items where - if a bar I don’t need names here, but if a retail bar, retails for $2 meaning we would sell it for $1.49 we are out there sell the buck on a great item and a full margin for us and providing to some real volume and so I think apparel, cosmetics, health and beauty aids, organic food items not fresh, but packaged food items all those are areas where we continue to I think have some room to grow.

Zachary Fadem

Okay, thanks for the color. So Richard could you - I know and nothing to beat on e-commerce so again but could you provide some early color on the Instacart and ship partnerships and is there anything notable you could call out regarding customers response or basket sizes versus an in store shop and then just going forward how should we think about potential expansion of these partnerships?

Richard Galanti

Well it's still a very small piece of our business, but it seems to be working in a sense, since that it's growing for them. We have Google Express which is operates on a five cities with several markets but they are in the process out there of offering as several items in one to three day delivery and we are participating in that with them, so that should be a positive for the program. Instacart has continued to grow dramatically, they currently operate in 40 of our cities up from 26 a year ago utilizing 240 of our warehouses from a 132 a year ago so that's growing, and then there is a few others that I mentioned [indiscernible] was one or something else.

Boxed, I don't know if we are doing that, that’s [indiscernible] and look two big ones are Google Instacart and there is not a whole lot of other color, they are working; we want sell merchandizing and they help us do that, but again don't expect us to be doing anything giant and big in one [indiscernible].

Zachary Fadem

Got it. Thanks Richard. I appreciate the Time.

Operator

Your next question comes from the line of Matt Fassler.

Matthew Fassler

Thanks a lot Richard, good afternoon. First question is a follow-up on inflation, we are seeing overall CPI start to recover, but we have seen the producer price index for PPI come back a little bit faster, are you concerned at all about any kind of gross margin squeeze s or is what you are seeing on the cost front resembling some of those macro indicators or should we just think about the fact that pricing is moving higher and general is being in that positive [indiscernible].

Richard Galanti

Pricing move general is net positive, if anything though I think we create some of our own deflationary pressures because we are good at - look at the MVM example, greater value to the member means greater lower prices which means us and our vendor lowering the price some and most of that is driving prices down from our suppliers with the anticipation of significantly more unit volume. The good is, most of time that happens and so that's what we do, but that does drive - those things work, don't always work in concert with the immediate bottom line improvement.

Matthew Fassler

Understood and then second question, just relates to competition. As Amazon takes 10s and billions of dollars of retail share annually and clearly the biggest share gain or by far the biggest one we have seen in a while. Are you seeing any - obviously your comps overall are increasing at a faster rate than most of the states, is there anything you are seeing in the mix that we might not catch through some of the commentary, that would suggest a change in complexion of how the consumer is really using your store, is it more consumable focused than it had been or is it kind of business as usual with no sign of change in the backdrop?

Richard Galanti

Look so far, and there is no guarantee in the future, but so far it's been business as usual. There is a number I read few months ago about how Amazon - if the entire U.S. sale, increase in sales or whatever, it was 50 billion they were half of it, well they were, 25 divided by 50 is half, but we were also up, the fact is there is others in the industry that were down 50 billion and so they were a quarter of a 100, minus 50 to plus 50.

That 25 billion is still credible and formidable, but in our view we are fortunate that a lot of the impact is it's impacting some food items or even packaged food items, it's traditional food retail that is getting hit more than us. We have to keep driving our member into our warehouse and we do that with off course great prices and great items certainly fresh foods, certainly gas station and traffic, which brings them into parking lot if you will and certainly the loyalty program which they have on to, all those have been helped us and then the treasure hunt.

We love it when we hear from someone that they heard that we had something, they went the next day and it wasn't there. well we are still pretty good at all that stuff and I think again the Kirkland Signature help that as well. now so far so good. When we look at the specifics even in markets where whether those Amazon or somebody else is taking share, a lot of were there taking on fracture something, fracture is hard and even they would acknowledge and others.

There will be more competition in the future, but who is going to get - we are asked a lot about legal coming into the east coast, they are going to take share, but they are going to take share from everybody else a lot more than they can take share from us. So we haven't really seen a big change like people are buying less something at Costco because of other formats out there.

Matthew Fassler

Thank you so much.

Operator

Your next question comes from the line of Paul Trussell.

Paul Trussell

Hey Richard. On SG&A we have recently cycled some labor investments made a year-ago. Could you just outline for us some other puts and takes we should keep in mind that's is going to impact the P&L in 4Q and beyond?

Richard Galanti

I'm sorry could you repeat that.

Paul Trussell

So on SG&A on the expense front, really just want you to help us think about some puts and takes on the expense side of things in 4Q and beyond especially since we just cycled some of the labor investments you made a year-ago?

Richard Galanti

Right, well look the biggest put and take is sales. If we can get another percentage point or two in sales that's always good and that solves a lot of things. When you look at some of the line items payroll is the next one, yes we just anniversaried some of that at the end of March that helps a little bit. Healthcare is still a challenge in the U.S. increasing penetration outside of the U.S. helps that number just by a higher a penetration within the total cost of the company and lot less everywhere else. But again that's going to happen slowly overtime in a positive way, and in some quarters the inflation the U.S. is does more than any small offset to that.

IT expenditures, somebody internally said we probably get the question asked upon it is the zero year-over-year basis point or inflection point, probably not we got to be lucky. Sales were a little higher, we had lot of expenses last year leading up to the end of the fiscal year or day one of the new fiscal year when we installed the new [indiscernible] counting platform on which other things will be built and so we had a lot of third-party contracts, lot of training which you write off, you don't capitalize and so that will get a little help there. But in fact, it will come down overtime but it's not going to be zero.

I think we e-commerce helps a little bit to the extent even at 11% last quarter or 13% or 14% in the first two-thirds of the quarter before the Mothers Day and what have you that's a higher growth rate than the rest of the company. So that a much lower SG&A, so that helps you a little bit. But I think we do pretty well at trying to drive the things in a right direction, but not touching certain things, we are not going to tweak wages a little bit less or does have an increase that’s a little bit less.

We don't do big things like some of those incremental things that anniversary at March like done on scale. We ended that I think in six years, but every three years we look at everything formal way. And so we are still couple of years away from looking again in terms of the big way. I still vote for a sales increase, if you get some extra sales everything else falls in place.

Paul Trussell

And then just could you speak to Gold Star and overall household membership growth; the growth has slowed a little bit. Just how you are thinking about membership count in the U.S. and also what you are seeing on the international front?

Richard Galanti

Part of it has to do where we are spending, several of our units in the past couple of years in the U.S. for example that it's do small markets, where you don't give the biggest bang. I think we had one big bang, I gave you example of Tulsa in new market, but that's not as small as some of the markets we want to do. When we open in another Seattle unit which we have two in last couple of -- two and a half years, or in the Greater LA market, it's a great success net of cannibalization. But you don't get a few 1,000 extra members, because everybody is member couple of more frequently because 20 minutes for driving the roadmap 40.

We also -- part of the growth depends on how many units we are opening overseas. When we open a new unit in Asia, as of opening date signups paid signups over the eight or 10 or 12 weeks prior and through opening day, you could have 25,000 to 40,000 new members. Iceland although there is only one location in Iceland, as of opening day we had I think over 35,000 members, over 35,000 and it's national news. And so I don't worry looking into the numbers, it's much based on where we have opened, it's not like a life opening compared to two years ago is getting fewer signups.

Operator

And your next question comes from Scott Mushkin.

Scott Mushkin

I just want to follow-up on the last question, just a dated question jumped into my head. Are comp memberships actually rising in U.S.?

Richard Galanti

Comp memberships…you mean comp buildings?

Scott Mushkin

The memberships going up and….

Richard Galanti

I think they are but it's probably a very small number, I mean closer to zero than the number of others. And part of that is when you are opening in a, let's say when we opened in Redmond where Microsoft's headquartered, that cannibalized knowingly three locations, two of them doing in the low to mid 300s a year, and doing in the mid 200s or low 200s a year. We signed up several 1,000 new members, but not 20,000 new members. If we average roughly 62 -- if we are just adding to our membership number of households divided by number of locations, it's about 61,000 or 62,000. And next year of that opening the comp of those three locations is down because some of those members now are allocated to the new rounds.

Scott Mushkin

So the one I want to just ask about just popping in my head. So how do you think about that as your business matures in the U.S., I mean does that make you want to slow down your center growth I mean how should we frame that, it's maybe the number eventually goes negative?

Richard Galanti

Maybe it does, I don't think we are there yet. For 25 years people have asked what is your next, whatever -- what is your next fresh foods, what is your next gas station, what is your next pharmacy, what is your next geographic market. Five years ago, I don’t think any of us thought about and I am not assuming us about going into New Orleans, in Baton Rouge, in Mobile and Rochester and Toledo and Tulsa and the like. And we know by the way on average that you are going to be a little slower to take few extra years, but they still have good metrics to them.

We have slowed I think using the two examples in Greater Seattle area in last 2.5 to 3 years we have opened Woodville and Redmond we waited on Redmond for 10 years to do knowing that we actually owned land in Redmond 15-20 years ago. But as we opened [indiscernible] there can be in the first one of these sides of CNE and then several years later opened Woodville, which is north of that north of Redmond, we have kept -- we actually sold the land and years ago. And finally -- so we are we try to be pragmatic about what we do. But overtime you are right we haven’t found the bottom, that's the good news.

In terms of, again anecdotally, I remember years ago when we have included we needed a minimum of 0.5 million population to serve the warehouse. And then it was 450, now it is 400 and we have the very successful warehouses that you divide the number of households in the community in the population, it's in the very low 200s and if you were in the high 100s. So hopefully we will keep pacing that goal in that direction and that will give us little more life hopefully the business center create some life, and hopefully that term fee is to improve. And hopefully we find couple of more countries. So we think we have got plenty to go and so that changes we'll let you know.

Scott Mushkin

So then my follow-up question and my real question was I noticed BJs competitor of you has offerings and pretty significant discounts on their memberships. I think you get the first three months free if I am remembering the commercial correctly and $40 for the first year. How do you -- is that matter to you guys I mean you are putting a fee increase through. But a competitor in the northeast and Mid-Atlantic southeast is offering significant discounts. I just wanted to get your comments on that and then all yield? Thanks.

Richard Galanti

Sure. And I think first if the advertise is good, we don’t advertise we don’t spend on that and we would love seeing add TV and the print adds still from both other competitors. And we are not concerned about it. We think that the value of the Costco is still as significantly higher price or without the free three months is a much better value. And we think that's evidence by our success of what we have done overtime and the fact that even what we have done in the past renewal rates have not really been impacted by it.

Operator

And your next question is from Brian Nagel.

Brian Nagel

On the gross margin Richard it was definitely a better performance here than the prior quarter, s going back to the discussion we had on the conference call last quarter. How much of the better performance reflected I guess more stable gas price environment, was that a significant contributing factor to the gross margins this quarter?

Richard Galanti

Well, the guest helps the margins as did other ancillary business as well. But again to put me in terms the chase, the roughly 80% of our sales which is food, sundries, fresh -- food, sundries, hardlines, soft lines and fresh foods, year-over-year on their own sales they were up 12 basis points. So, it was a lot of different things.

Operator

And your next question comes from Scot Ciccarelli.

Scot Ciccarelli

Two questions, number one, in terms of the e-commerce business as you guys reach a certain scale. Do you need to change your processes or do you continue to go with the drop ship philosophy?

Richard Galanti

What relates to what, I didn't hear the first question?

Scot Ciccarelli

Your e-commerce…

Richard Galanti

Well, as I mentioned earlier, part of the inventory increase in the Company because we are just rejuvenated by number of warehouses, you give me a number and we'll maybe change that over time. But we had an increase in inventory for e-commerce related stuff, not at the warehouses but we went from seven to 19 distribution points in the last year. So we are getting closer to the customer, we are also working with third parties. I mentioned in the call the GE scheduling system there is other scheduling thing that we are doing. And I mentioned the thing we are testing right now in our Bedford Illinois Business Center. I mentioned last quarter where in addition to 50 or 70 mile radius where we deliver with Costco truck through third party, there is one or three day delivery to 17 states all the way to the Pennsylvania New Jersey. And so if anything I think we are getting it's getting quicker and cheaper to do these things for us. And maybe we started off high and begin with how we baked and how we did it, but we are improving.

Scot Ciccarelli

And then second question is hopefully this is an easy calculation here. We look at the debt redemption the issuance, looks like you guys would be incurring about 25 million more a year in interest cost call it 6 million a quarter. Should that just be a pretty straight calculation or is there something else we should keep in mind as we kind of work on our model?

Richard Galanti

I did a back of the envelop this morning and I came in with a number that's few million higher that still has two in front of it. Now it's pretty straightforward I mean you've got 3.8 billion tons somewhere between 260 and 270, call it 265 it’s a rounded number, you've to pay down of the March debt that we did, which was 60 million a year savings, you've got the call, shortly of the 1.1 billion, 108% that's on the interest expense line, a little bit of an offset will be the cash. As you know we borrowed 38, roughly 31 is the dividend, the others 700 is cash earning less than net interest rate, and even less than the one that’s coming up. But it all moves up to something like you said, if you go back to the March where we had in place the March 2017 5.5%.

Operator

Your next question is from Oliver Chen.

Oliver Chen

Our question is on multi vendor mailer, how are you feeling about what you've been doing in terms of testing and learning; and that the MVM product versus the product that you are offering at every day values? It's been -- I know you are thinking about how to optimize that appropriately; so just curious about the status of that? And the second question is about the mobile app, and Amazon has a really good mobile app. So what features do you want to have in your mobile app over time that you don't have now? Thank you.

Richard Galanti

I want to get back to you on the latter question. Just because I don't have something here you can help me on that one. The first one, I forgot now, what was it?

Oliver Chen

The monthly vendor mailer….

Richard Galanti

I think we feel good about it. I think as I have said on the last call, something as we enhanced the value and kept in the multi vendor mailer and items some of the things we took out and did everyday little pricing on; sometimes it's still better value based on and the vendor working towards that end and to have it more prominent, so there is lots of different things. It was 12 weeks ago that I said to you and many of you on the phone things are fine, there is a few things that impacted us a little more or something that didn’t work. I think we have improved on all of those things but we will continue to do that it's been only as we haven’t solve family answered everything but we feel good about what is happened in the last 12 weeks as it relate to that question.

Oliver Chen

Richard, lastly on traffic and store traffic you've been able to do a great job on the multiyear basis with physical store traffic. What are some of the opportunities ahead or what are some of the plans you have just aim to sustain that in a sustainable healthily growing manner? And how do we or should we be more cautious because it's been still good on a multiyear basis. Just it's something we monitor and it's been impressive for you to achieve such good store traffic in a tough environment.

Richard Galanti

Well, this is where we go all shocks. And I think we are going to keep focusing on driving value of items and identify the item that makes sense. And I mean it as many of you known us for years as we have said many times, it's the good news it's a lot of little things. Even gasoline is a lot of little things today, because it had a big help for several years in the U.S. -- in Canada for few years. We now have about a dozen plus unit at the gas stations and countries like Japan and Australia, and soon a couple of other countries. And not everywhere, but it's now a lot of its little extra thing in some of those countries.

I think the wine and spirit thing has caught us off guard in a positive way that what started as a few line items a number of years ago we are actually receiving rewards on price points that are nobody can match and the trust to the brand. On the spirit side, we never thought we would be successful, and it's a double positive because it's not only selling us the full margin private label item but it's creditors the brands don't like losing market share to us and they want to get look better on pricing at Costco, so all those things had helped us.

I think the apparel area as I have mentioned has been something we hadn't thought about it. But over the last two or three years, it's a $5 plus billion business that's been growing at 9% compound it's 3.5 years. And that has more lives even though retail apparel was weak. And so we will keep coming up with stuff. I think the first trend that our traffic went from a boring 4.2

compound for seven calendar years '09 through '15 and then it hit 38, 35, 33, 28 and everybody is saying Bob and I others were the first to say, this could very well be the durable not just punch on it but 4.2 is pretty hard to do. With that being said we feel really -- where we got some things for traffic drivers and fresh food still has legs, JS still has legs, gasoline still has legs executive membership so the credit card extra value. So we feel pretty good about -- that's in a way or not quantitative answer but all things are relatively sorted.

Oliver Chen

Richard, you have very talented merchant. Did Amazon is trying to hire them is that something that comes up in terms of that capability being such a competitive advantage?

Richard Galanti

I would hope not. To my knowledge, we lost one or two merchants but not in the last few years. We lose a few IT engineers several of whom 18 months of the date call us back after they hit their [indiscernible]. But that's everywhere I mean look Amazon is in our town and they hire a lot of people from every company in town and out of town. We have been fortunate, people have chosen to stick around but the answer is no, we haven't. But we cross our fingers to you in the future.

Operator

And the next question is from Kelly Bania.

Kelly Bania

Just another one with e-commerce, I think you mentioned that you've expanded some KS items online. Just wondering if you could elaborate what categories those are. And really just what is the pricing strategy with online versus in-store for those items that I think you said 2,000 items that crossover. I mean should we expect prices are the same or is there a difference in pricing strategy online versus in the club? Thanks.

Richard Galanti

Sometimes online they don't hire for delivery, sometimes as we tried some, what call them velocity apparel items, stocks and shirts and things. We need to some of that ourselves in terms of shipping as we want to get people comfortable ordering velocity items, whether its apparel or health and beauty aids or sundries like Jacobs. And unfortunately, I don't have the list in front of me and some of the new items with several KS items, but other brands as well. And again give me a call after the holiday -- I just don't have that information with me.

Kelly Bania

And then can I just ask one more just clarification on gross margin. I think when you talked about the core gross margin the up 7 up 20 with and without gas that includes the 16 basis points from the Citi Visa but the up 12 the 80 basis or the 80% of the core business, up 12, that excludes the Citi Visa. Is that correct?

Richard Galanti

That’s correct, yes.

Operator

And your next question is from Peter Benedict.

Peter Benedict

Richard, just a couple of quick ones, MFI trends, some underlying slowing there I mean is that just a friction from the new card changeovers or are you seeing anything in terms of signups that's concerning you?

Richard Galanti

The biggest issue is re-openings in the quarter, actually two net openings. One was there so no, nothing that's terribly -- that's concerning. Nothing that is dis-concerning, I shouldn't have used the word terribly.

Peter Benedict

Second question, the lift in comp that you've seen over the last several months recovering comp trends; has there been anything in terms of business members versus Gold Star, anything like that that has kind of disproportionately driven that?

Richard Galanti

No, not really.

Peter Benedict

And then my last question is just around the e-commerce fulfillment centers, just get 19 of those. Where do you see that number going in the next few years? And then could the clubs actually be used for that whether you said 2,000 items that are in the clubs that are also offered online, can the clubs to be used to sell that delivery of those?

Richard Galanti

First of all, going from 7 to 19 has a lot. And again, we are more than saving on that because we are getting the stuff to you quicker. We are spending less on freight we did it somewhat inefficiently to start with. There’ll be more -- I don’t that's I don’t know if -- I just know what those few data points for 7 and 19. The other question was where we ever use the warehouses fulfillment centers, yes sure. And I'm saying that not suggesting it's going to happen tomorrow. And one of the things we are doing with the Bedford, Illinois Business Center in a way is e-commerce related, you order online and it will be deliver in one to three days via third party carrier; certain items, I mean I think the items have certain weight and size limitations we are not to be delivering sofas to New Jersey from there.

But probably we will be delivering that but using the business centers like using a warehouse and different set of items, but it was easy to do because it will set up at some ways to accommodate it fat. And we’ll see, but it's logical to think that would you have some of allocations around the country that could do some things at night when they closed or a low volume unit that could help out. But we haven’t -- don’t expect anything on that front for at least the next year, and I would always suggesting to next year that this we haven’t really talked about and a lot of other than could we.

Operator

And your next question is from Greg Melich.

Greg Melich

Richard, could you fill us in on what gas was the percentage of sales. And I think you said the gallons comp positive and if you have the number that would be great. And I have follow-up?

Richard Galanti

It was okay we are almost there.

Greg Melich

Should I go with the next question?

Richard Galanti

Yes.

Greg Melich

Okay, so the other question I just want to make sure I get the timing of Visa fitting and how that came in last year. So it is the 36 bps of help to the EBIT margin, if I get this right. And in the fourth quarter, we should probably get another four or five weeks of that benefit. Am I thinking about that right or is there some other thing at work, if I remember correctly, as you are running out the Amex program you were not signing up people and not getting the payments for signing up people for the card? Or is it just the straight forward think about that got a few more weeks of the benefit cycles?

Richard Galanti

I think it's like six weeks, not just three or four but then you get -- there was 220 that we have some disruption around it. We are also conservative on some of the assumptions. I mean look it’s not going to be nearly as it was in the last three quarters, but it's not going to be a quarter is the only of quarters base. In terms of the gallon comps, it's a very strong number. It has two digits but not -- is very low two digits, so I can't tell you anything.

Greg Melich

Low single digits, and gas a percentage of total company sales?

Richard Galanti

Yes, hold on a second…

Greg Melich

And maybe why you are digging that out, since I got -- the membership fee growth in local currencies, how much effect that line?

Richard Galanti

First of all gas is a little under 10% and the other one was membership fees, that was in my -- membership fees reported was up 4% in dollars, or $26 million and 5% without FX. FX was a $3.6 million hit to the number. FX should have been flatter -- the number would have been $3.6 million higher.

Operator

And your next question is from Edward Kelly.

Edward Kelly

Richard, just a couple of quick one for you entail on here, on the gross margin in Q4. Is there any extra leverage from the extra week in Q4 that we should expect, that's meaningful at all?

Richard Galanti

Nothing. The margin very little on the expense side almost nothing.

Edward Kelly

And then on just a follow-up on fresh food, just provide maybe more color on what is tied up here in terms of things you've been talking about, particularly in organics. And is there any kind of step change or just continuation of what you've been doing?

Richard Galanti

Global store sales -- being the largest purveyor of USDA prime beef in the universe and we are now -- in the U.S. we are something like a third of all U.S. prime beef sales. Before ’08, vast majority of all prime beef sales went to restaurants and hotels.

Edward Kelly

And how are you doing on capacity and some items in produce from an organic standpoint that maybe you struck a little bit in the past?

Richard Galanti

I think, overall, and not just us but everybody has benefitted in fact there is more supply out there. I think we feel competitively from a standpoint that we are well positioned because I think we have used the number on produce. We source produce from 44 countries, nobody does that and that gives us some additional advantage in that area. But it's gotten less hard but it's still organic as -- there is more demand than there is supply. But if I look at the price points of organic versus conventional, on most items, the premium is still a premium but not as big a premium that it was two years ago because of the fact that there is less of a supply demand imbalance.

Operator

And there're no further questions.

Richard Galanti

Well, thank you everyone. Have a good afternoon, and holiday.

Operator

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