Costco Wholesale Corp (NASDAQ:COST) Q2 2020 Earnings Conference Call
March 5, 2020 5:00 PM ET

Company Participants

Richard Galanti - EVP, CFO & Director

Conference Call Participants

Simeon Gutman - Morgan Stanley

Gregory Melich - Evercore ISI

Christopher Horvers - JPMorgan Chase & Co.

John Parke - Gordon Haskett

Karen Short - Barclays Bank

John Heinbockel - Guggenheim Securities

Michael Baker - Nomura Securities

Rupesh Parikh - Oppenheimer

Scot Ciccarelli - RBC Capital Markets

Judah Frommer - Crédit Suisse

Oliver Chen - Cowen and Company

Peter Benedict - Robert W. Baird & Co.

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Q2 earnings call and February sales conference call. [Operator Instructions]. I would now like to hand the conference over to your speaker today, Mr. Richard Galanti, CFO.

Thank you. Please go ahead.

Richard Galanti

Thank you, Rochelle, and good morning to everyone -- 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 operating results for the second quarter of fiscal 2020, the 12 weeks ended this past February 16, as well as February retail sales results for the 4 weeks ended this past Sunday, March 1.

Reported net income for the quarter came in at $931 million or $2.10 per share. This compared to last year's second quarter of $889 million or $2.01 per share. Net sales for the quarter came in at $38.26 billion, a 10.5% increase over the $34.63 billion realized last year in the quarter.

Comparable sales for the second quarter were as follows. In the U.S. for the 12 weeks on a reported basis, 9.1%; excluding gas inflation and the impacts of FX, 8.1%. Canada, on a reported basis, 8.9%; ex gas and FX, 6.8%. Other International, 7.9% reported; and 7.1% ex gas and FX. For total company, a reported 8.9% same-store sales increase and ex gas and FX of 7.9%. Both of those numbers were positively impacted as well by approximately 0.5% due to the Thanksgiving holidays occurring 1 week later this year than last year.

On e-commerce, we reported a 28.4% comp for the 12 weeks, ex -- and a 28% ex FX. And again, there was the bigger impact of this Thanksgiving holiday shift there given the importance of that to e-commerce. E-commerce sales in the quarter were positively impacted by an estimated 11 percentage points and, hence, the 28% comp result.

In terms of second quarter comp sales metrics, second quarter traffic or shopping frequency increased 5.9% worldwide and 6.1% in the U.S. Strengthening foreign currencies relative to the dollar -- U.S. dollar positively impacted sales by about 0.25% -- I'm sorry, by about 25 basis points. And gasoline price inflation positively impacted these numbers by about 80 basis points. Our average transaction size or ticket was up 2.9% during the quarter, which includes the positive impacts of gas inflation and FX. Later in the call, I will review our February sales results.

Moving down the income statement for the second quarter. Membership fee income came in at $816 million or 6.3% higher than the $768 million recorded in Q2 of last year for a $48 million increase. That percent increase is about the same as it was Q1 year-over-year. In Q1, we opened 3 -- we had 3 new openings. In Q2, we had no new openings.

In terms of renewal rates, at Q2 end, our U.S. and Canada renewal rates were -- came in at 90.9%, and worldwide renewal rate at 88.4%. These are the same levels of renewal that we've achieved at each of the last two fiscal quarters. In terms of number of members at second quarter end, in terms of member households and total cardholders, at the end of second quarter, we had 55.3 million member households, up about 600,000 from the 54.7 million 12 weeks earlier. And total cardholders totaled 100.9 million, up about 1 million from the 99.9 million we reported at the end of the first quarter. At Q2 end, paid executive memberships stood at 21.7 million members, an increase of 321,000 during the 12 weeks or about 27,000 per week increase since Q1 end.

Going down the -- to the gross margin line. Our reported gross margin in the second quarter was lower year-over-year by 31 basis points, coming in at 10.98% compared to 11.29% a year ago. That 31 basis point reduction, lower number year-over-year, excluding gas inflation, it would have been 22 basis points lower. If you'll please jot down the 5 -- 4 line items and 2 columns as we usually do. First column is reported for the second quarter, and the second would be without gas inflation. The core merchandise margin was down on a reported basis 30 basis points year-over-year in the quarter. Ex gas inflation, it was down 22. Ancillary businesses, a minus 5 and a minus 2 basis points. 2% Reward, plus 4 and plus 2. And in total, as I mentioned, 31 basis points lower year-over-year on a reported basis; and ex gas inflation, 22 basis points lower.

The majority of the lower year-over-year core margin was driven by higher sales penetration of -- to significant lower-margin segments of our operations, which are growing at a faster rate than the core, notably gasoline and e-com as well as the start-up losses at our new poultry complex, which I had mentioned in the first quarter as well. Looking at the core merchandise categories in relation to only their own -- to their sales, core on core, if you will, margins year-over-year were lower on a reported basis by 15 basis points, of which 6 basis points related to the losses from the new poultry complex. Within the core gross margin year-over-year in Q2, we showed a gross margin increase in softlines; food and sundries was about even year-over-year; and decreases in both hardlines and fresh foods. Hardlines was down in the quarter, primarily due to holiday timing, which shifted more promotional activity into Q2 this year. Fresh was negatively impacted by our -- a step-up in price investments versus last year in fresh and by the margin impact from the new poultry complex, as I just mentioned. And we're now halfway through our first year of operations of the poultry facility, which opened on September 10, and we would expect the gross margin headwinds to decline but -- continue but to decline a little bit as we get to full production capacity and improve operations.

Ancillary and other businesses gross margins on a reported basis, minus 5 basis points year-over-year and minus 2 ex gas inflation in the quarter. Basically, you had a few things that hurt you and a few things that helped you, but overall, minus 2 ex gas inflation.

2% Reward was better by 4 on a reported basis and by 2 basis points ex gas inflation. This relates primarily to a true-up of our breakage estimate of the Executive Member rewards.

Moving to SG&A. Our reported SG&A percentage year-over-year was lower or better by 22 basis points, coming in at 9.78% of sales, down from 10.0% a year earlier. Without gas inflation, SG&A was lower by 13 basis points. Again, if you jot down the following few numbers, 4 line items and the 2 columns. Core operations, year-over-year in Q2 on a reported basis, showed an improvement. It was lower, so I'll say a plus 17 basis points; and ex gas inflation, plus 10. Central, plus 1 and plus 0. Stock compensation was lower -- or plus 4 and plus 3 on -- ex gas inflation. And again, the total on a reported basis, SG&A was lower by 22 basis points, plus 22; and without gas inflation, plus 13, so lowered by 13.

The core operations component, again, 17 reported; 10, excluding impact from gas. This figure includes the impact of the wage increases that occurred last March of '19. This hit our year-over-year comparison by an estimated 3 to 4 basis points. We anniversaried that increase just this past week so the impact in Q3 will be minimal.

SG&A also benefited during Q2 year-over-year from the shift of sales penetration to lower SG&A -- if you will, lower SG&A segments of our operations, which are growing at a faster rate than the core, again, gas and e-com.

Central was lower -- within SG&A, central was lower on a reported basis by 1 basis point or flat year-over-year ex gas inflation. We continue to invest and spend in IT to the tune of about 5 basis points higher year-over-year. That was offset by improvement in other expense items and, of course, helped by strong sales. And stock comp, as I mentioned, an ex gas inflation improvement of 3 basis points. This varies quarter-to-quarter. Looking at the last couple of years, generally, it's a small hit in Q1 and flat to a small benefit in the other quarters. Nothing really unusual to report there.

Next on the income statement is preopening expense. Preopening expense was lower. It came in at $7 million compared to $2 million in Q2 a year ago. As I mentioned earlier, this year, we had no openings. Last year, we had 2 openings both in the U.S., 1 net new opening and 1 relo. This year's Q2 preopening expense in this quarter relates primarily to a warehouse that will open during the third and fourth fiscal quarters. Coming up very soon are our opening in Perth, Australia and also our first in the state of Mississippi, in Ridgeland, Mississippi, that will be our 45th state where we operate. Those will both open during the next couple of weeks. All told, reported operating income in the second quarter of 2020 increased by 5.2%, coming in at $1.266 billion this year compared to $1.203 billion a year ago.

Below the operating income line. Interest expense was the same year-over-year coming in both quarters at $34 million. And interest income and other for the quarter was lower by $1 million, so almost flat year-over-year. Overall pretax income was up 5.1%, coming in at $1.277 billion compared to last year's $1.215 billion.

In terms of income taxes, our rate was just slightly higher year-over-year. In the second quarter, it was -- it came in at 25.9% rate compared to 25.8% in Q2 last year. For all of fiscal 2020 based on our current estimates, which, of course, are subject to change, we anticipate that our effective normalized total company tax rate to be approximately 26% to 26.5%. In terms of openings, as I mentioned, we had no openings in Q2. We plan 2 net new openings in Q3. And I'll give you a range for Q4, which is our 16-week fiscal quarter of 11 to 13. Part of that, again, most of the openings concentrated in our fourth fiscal quarter. And of course, there's probably a few subject to slipping into early part of next year based on weather. As of Q2 end, total warehouse square footage stood at 114 million square feet.

In terms of capital expenditures, during the quarter, we spent approximately $545 million. And our estimated CapEx for all of fiscal '20 remains right around $3 billion. In terms of e-commerce, again, we reported a 28.4% comp sales increase and 28% without FX. Again, a lot of that had to do -- a lot of that increase had to do with the Thanksgiving shift. We estimate again that about 11 percentage points of that related to Thanksgiving falling a week later this year and helping this number.

Overall, a few of the stronger departments, majors, special order kiosk items, seasonal and toys and housewares, these departments generally benefited from the holiday shift. In terms of total online grocery, that continues to grow at a faster rate than the store e-com comp, both 2-day and Instacart. The latter of which isn't included in our e-commerce numbers since they come into the warehouse to buy. Although the sales penetration is still very small, the sales are quite large in the high double-digit range year-over-year. During the second quarter, we successfully launched both our Japan e-commerce site in December and our Australia e-commerce site this past month in February. And not to be outdone, we recently sold another high-value large carat diamond for a little over $600,000. If anyone's interested, please give me a call.

Turning to our February sales results, the four weeks ended this past Sunday, March 1, compared to the same period last year. As reported in our release, net sales for the month of February came in at $12.2 billion, a 13.8% increase from $10.72 billion a year ago. In terms of geography, U.S. reported comp for the 4 weeks, 12.4%; ex gas and FX, 11.6%. Canada reported a 10.2%; ex gas and FX, a 10.4%. Other International, a 12.5%; ex gas and FX, a 13.5%. So total company, a 12.1% reported; and a 11.7% ex gas and FX. E-com for the 4-week period, 22.6% for the reported and 22.7% ex FX.

Our February results benefited by last week's big uptick in sales, the fourth week of last month, mostly, we believe, related to concerns around the coronavirus. This positively impacted the month's total and comparable sales numbers by approximately 3 percentage points. U.S. regions with the strong sales results in February were the Northwest, Texas and the Midwest. Internationally in local currencies, we saw strong results in Taiwan, Japan, Spain and Mexico.

For the month, foreign currencies year-over-year relative to the dollar hurt Feb comp -- February comp sales in Canada by about 60 basis points. It impacted negatively Other International by about 110 basis points and total company by about 20 basis points. Cannibalization was about a 10 basis point impact to the U.S., a minus, 140 basis point minus impact to Other International and 30 basis points overall to the company.

Moving to merchandise highlights. The following comparable sales results by category. Food and sundries were positive in the low teens. Strongest departments included foods, frozen foods, sundries and candy. Hardlines were positive in the high singles. Better-performing departments were lawn and garden, health and beauty aids and tires. Softlines were up in the mid-single digits. Better-performing departments included housewares, domestics and jewelry. And finally, fresh foods were up in the low double digits. Better-performing departments included meat and produce. Within ancillary, pharmacy, gas and hearing aids had some of the better comp sales increases in February. And gas price inflation, I think I mentioned this, positively impacted total reported comp sales by about 60 basis points.

Lastly, our comp traffic or frequency for February was up 9.2% worldwide and 8.9% in the U.S. Now given the impact in week 4 where we really saw the big uptick, as I know many did out there, it was related to the concerns over coronavirus, the first 3 weeks -- within that 9.2% worldwide for four weeks, the first three weeks stood at 7.6%. And again, within the 8.9% U.S. frequency number for the four weeks, within that for the three weeks, it was 6.9%. So still a good showing prior to that. For February, the average transaction was up 2.7%.

Now turning to the coronavirus and all the issues and impact surrounding it. Like everyone, we are keeping a close eye on the developments around the coronavirus, including the impact on operations, the health and safety of our members and employees and, of course, our supply chain. As already discussed, we saw strength in our February traffic and comp sales related to the news and concerns about the virus, particularly in the last week of the month, and that's continuing in the first few days of this week.

Our warehouses have overall remained open with only a few total days of closures at a couple of locations in Korea. As well, our Shanghai location, there's been some limitations required on the number of people in the facility at any given time.

Members are turning to us for a variety of items associated with preparing for and dealing with the virus such as shelf-stable dry grocery items, cleaning supplies, Clorox and bleach, water, paper goods, hand sanitizers, sanitizing wipes, disinfectants, health and beauty aids and even items like water filtration and food storage items. And we're doing our best to stay in stock on these and other items. We're getting deliveries daily, but still not enough given the increased levels of demand on certain key items. It's been a little crazy this past week in terms of outside shopping frequency and sales levels and not only in the United States.

In terms of placing quantity limits on what a member can purchase. We are doing that in some instances. It tends to be at all locations but may differ regionally based on supply levels. I do want to give 3 big shout-outs. Our buying staffs, both here regionally and abroad, working, in some cases, around the clock to procure supplies for both existing suppliers and from other sources where possible. Second, a shout-out to our warehouse employees. These last 9 or so days has been beyond busy. Even with the traffic jams, in the parking lots and the long lines to check out, they've been absolutely awesome. And anecdotally, we're hearing that daily from members. We hear a few other things occasionally, too. And lastly, our suppliers, both domestically and abroad, we feel our strong long-term relationships have helped to this crisis. We've been there for them, and they are certainly there for us now.

Overall, in terms of what the coronavirus-related demand items, in terms of that, it's looking better, but not perfect, and we'll see what each day brings. At our warehouses, in terms of cleanliness and sanitizing, we have enhanced sanitizing protocols, and safety procedures have been implemented in all the locations. Some examples, wiping down cart handles with sanitizing wipes, placing of sanitizing wipes stands at entrances, also along the fresh line wall and food courts. Enhanced procedures at the food courts, patio tables, condiment tables, dispensers and phone booths, et cetera, the general things you might expect and that we see in all the recommendations.

In terms of supply chain, closures of many manufacturing facilities extended well beyond the typical 1 week Chinese New Year holiday, which was the last week in January. In many cases, factories over there were closed for 1 to 2 additional weeks. That's now improving each week. Initially, 2 to 3 weeks of factory -- so initially, there are 2 to 3 weeks of factory closures, not 1. Then about 3 weeks ago, and just pulling some of the buyers that -- a deal with the factories, they felt there was a rough number of 20% to 25% production levels, moving up to 40% and now as high as 60% to 80%. But again, it's improving, and this still has a little ways to go.

In terms of transportation issues, whether it's Chinese New Year and then a couple of additional closure weeks. There were not only product issues but also trucking and port issues. These are also abating with port capacity in China improving each day as well. And I say port capacity, it's also the shipping lines that come to the various ports.

Domestically, truck capacity is plentiful. However, exporting items, including KS items as well as other U.S.-manufactured items to our locations in Asia and Australia. It's been a little bit of a challenge because of some container shortages here. But overall okay, just taking a little more work. We're finding other ways to handle any potential out of stocks by shifting SKUs to alternative items and categories, particularly in the areas of domestic goods, food and sundries and fresh.

And as you might expect, our travel business is impacted due to reduced demand as well as higher-than-normal cancellations of previously booked trips, particularly as it relates to cruises and international travel. I don't know if there's any surprise with that.

At this point, it's hard to quantify what the financial impact will be for our future results -- to our future results. Again, the first 1.5 weeks of this fiscal quarter has been -- the last 1.5 weeks has been quite good with the sales, but we'll see what tomorrow brings. We'll continue to pass that information along, and of course, we do report monthly sales results.

Finally, in terms of upcoming releases, we will announce our March sales results for the five weeks ending Sunday, April 5, on Wednesday, April 8, after the market closes.

With that, I will open it up to Q&A and turn it back over to Rochelle. Thank you.

Question-and-Answer Session

Operator

[Operator Instructions]. Your first question comes from the line Simeon Gutman from Morgan Stanley.

Simeon Gutman

First question is on the gross margin. I think if we take the core on core, down 15%, and you get rid of the chicken production costs, you're down 9%. Did you say within that what the e-commerce mix shift is and how that compares to prior quarters up to the prior run rate?

Richard Galanti

No. We weren't that specific, but a lot of it has to do with the fact that, that -- particularly that 1 week where it's so important to e-commerce on promotional items for Black Friday, Cyber Monday, the weekend, the 3 days leading up to Thanksgiving, so you do have some lower-margin -- you have some lower-margin categories in there to start with as well as we do a lot more promotional stuff as most retailers do with that week of Thanksgiving.

Simeon Gutman

Okay. So this was a little bit unusual given the timing and given just the fourth quarter -- or the holiday period was in that number.

Richard Galanti

Well, I want to stand corrected. There's a couple of people here who just corrected me. The e-com numbers are not in the core on core. So that would be outside of that. But it's still the strength in majors.

Simeon Gutman

Right. Okay. Got it. And -- but broadly speaking, the greater mix of e-com, Richard, is going to depress -- well, you're saying it's not in that number, but it's unfavorable to gross margin broadly, though, is that fair? And is that because of the mix of products that are being bought or because of the discounts or the markup that you're putting on those items?

Richard Galanti

It's both. I mean as we try to build new categories over the last year or so, like apparel, we're giving some hot deals out there. If you buy 1 shirt, it's X, if you buy 2, it's a little less for delivery or whatever else. So we're driving that business. And again, we've talked about -- yes. But the big thing is electronics. Electronics tends to be a low-margin business, not only TVs, but all the computer and phone things.

Simeon Gutman

Got it. Okay. My follow-up is on just overall reinvestment, right? Your business is growing at a really high level, high single-digit comps. I'm not sure if you planned for that level. And the core on core, in general, is doing relatively well. It's not down 20 or 30. And I guess, the SG&A that you're spending seems somewhat in line. But I assume you're not flowing through all the leverage that's coming through this model. And so my question is where are you finding places to reinvest. Again, it doesn't seem like the core on core is getting -- is going down enough to suggest you're putting it back in price. Are you finding other places to spend in SG&A?

Richard Galanti

Well, I'd argue that we are putting a lot of it back in price. Keep in mind of all the buckets we talked about historically from the membership fee income to the tax reform to the change in credit card, those things keep growing, and it allows us to be competitive. And when we see strong sales, I think it encourages us to do more of that. And the other thing is I'm not going to go through 10 different things. But there's lots of things we're very busy. It's not just the 5 basis points I mentioned in IT. We got a lot going on with the e-com fulfillment with the chicken complex, which I mentioned, there's a lot -- with the CCPA. These are small things, but each of these are various numbers of basis points. CCPA is the privacy -- California Privacy Act. We don't point it out because I'm sure there's something that goes the other way sometimes. But at the end of the day, there's a lot of things going on, and we feel pretty good about where our expenses are, though we're always going to try to improve them.

Operator

Your next question comes from the line of Gregory Melich from Evercore ISI.

Gregory Melich

Richard, two things I wanted to follow up. One is on the membership fee income, could you give us what that is in constant currency. And also, if you're seeing any membership sign-ups inflect like the way sales and traffic have in the last couple of weeks.

Richard Galanti

It's $2 million, is it? $2 million? It's $2 million even with FX.

Gregory Melich

Got it. Once we adjust for that. Got it. And then on the sign-ups, have you seen any change there in the rate of sign-ups?

Richard Galanti

I honestly don't know. I know even a few people -- I mean the shopping frequency is off the charts for the last few days. And you see it on social media with people sending in pictures. So I've got to believe there's been a little bit of it, but not enough to move the needle.

Gregory Melich

Got it. And then secondly was just on gasoline. What -- did you have the average selling price this quarter? And if you have any sort of trends on the gallons would be great as well.

Richard Galanti

I don't have it in front of me. I know that there was -- gas was inflationary, correct?

Unidentified Company Representative

Yes.

Richard Galanti

I think -- hold on a minute. Gas price, in Q2, it was 7.9% inflationary.

Gregory Melich

Inflationary. And that's the average selling price per gallon versus a year ago?

Richard Galanti

Yes. 2.75 versus 2.55.

Gregory Melich

Got it. And then last, I'll sneak it in because I know it's common. The balance sheet, very strong, more volatile markets. How should we think about buyback capital structure in the current rate environment and environment of the world?

Richard Galanti

Well, every banker calls us every day to let us know that rates are even lower today, time to borrow. But no, look, we continue to look at it. We talked about it in every Board meeting, and all I can tell you is to stay tuned.

Operator

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

Christopher Horvers

So a few follow-ups. First on March. I mean you are limiting some of those high-volume items. It does look like you've got some pretty low in stocks out there. Do you see the potential for conference later this month?

Richard Galanti

Well, we don't know. People have asked us what happens when people have been bulking up on certain items. And yes, there's out of stocks every day, too. But overall, the numbers are incredible because there's so many people coming in. And they're buying other stuff as well. So I don't know what tomorrow brings. When asked the question, are the people then go through this additional purchasing of water and shelf-stable food items and everything, I guess, it depends. Some of them putting it in their basements for another day. Some of it related to the fact that people aren't eating out as much. I think it's a combination of those factors. All we know is that last week, starting Tuesday or Wednesday, which is when a lot of the news went even -- went -- in the U.S. went even further, we had a huge pickup in traffic, which continued over the weekend and increased the first few days of this -- even further in the first few days of this month -- this week. And so we'll see what tomorrow brings.

And again, on the supply side, there is clearly, not just at Costco but other places, you really can't go in and generally find sanitizing items and what have you. And while we're getting shipments daily somewhere in the U.S., whatever limited amounts we get or allocated is gone pretty quickly. And I would assume that over the next few weeks or several weeks that will abate. But it depends on what else happens with the virus itself.

Christopher Horvers

Yes. I was at a store on Saturday. I've never -- right after they open, I've never seen the line that long, all the way back to dairy. The -- my follow-up question is, this might be hard to parse out, but I think the big question on investors' minds is how the consumer is going to behave. Obviously, you have the pantry load, but you also sell a lot of general merchandise. You also sell a lot of big ticket. So were you able to sort of tease out if you're seeing any pullback relative to trend in the past week or so in some of the more discretionary and larger-ticket categories?

Richard Galanti

Yes. What's interesting, I'm just looking at some hand-written notes from our -- I spoke to our senior buyers yesterday. You would think things like patio furniture would be impacted because it's a big-ticket discretionary item. The comment was we're selling it extremely well. Now part of that is we've got a bunch more people coming in, so maybe per customer -- the purchase per customer is down a little, but there's a lot more customers. And so -- and what else, lawn and garden is doing well. The buyers grew, and that's more weather-related in certain markets. There has been some impact in -- excuse me?

Christopher Horvers

TV? Did you say TV? Were you going to say TV?

Richard Galanti

No, I said lawn and garden, weather-related. And then in some electronics items, while some are strong, there's others like some laptops and some phones where there's been some supply chain issues. But I would say, overall, the initial thought -- my initial thought is that big-ticket discretionary items might be negatively impacted right now. To the extent they are, it's been more than offset, at least in these last several days, by the influx of shopping frequency. I don't know what that means for tomorrow, we'll have to see.

Christopher Horvers

Understood. And super helpful. And I'm sure all the media outlets are picking this a lot. My other questions, two quick ones. One is have you expanded the number of SKUs in the MVM. It seems to have picked up over the past couple of months, but wanted to get your thoughts there. And then lastly, it looks like you have a new grocery delivery option in the app and on your website, sort of an extended delivery option, not the 2-day and not the same day. So sort of what's been the strategy there? And is that new or just a repackaging of something you already have?

Richard Galanti

Generally, there's been no change in MVM items. I mean, if it's up a little or down a little, I think that's random, not planned. And as it relates to shipping, at least the people in the room with me here are not aware of that. Was it?

Christopher Horvers

Okay. It must be just a repackaging of something that you already have.

Operator

Your next question comes from the line of Chuck Grom from Gordon Haskett.

John Parke

This is actually John Parke on for Chuck. Can you guys provide a little bit of an update on the performance of same-day and Costco 2-day and how that's impacting kind of total spend from these customers that are utilizing it?

Richard Galanti

It's still relatively new for us over the last year. Overall, and my knowledge of this is a couple of months old, it's a slight improvement. The concern, of course, is they buy more, having delivered in one day and two day, and then they come in less frequently. But how less frequently, and they are coming in a little less frequently, but the sum of the two still is fine. Again, it's too early to tell, in our view, just fine, continue, or does it change a little bit? We're still -- but keep in mind also, we continue to do a lot of things consciously even through e-mails to get you come back in the location with certain promotional things that are in-store only.

John Parke

Got it. And then I guess just going back to the coronavirus. I mean is there any way to kind of indicate whether the margin on these sales are materially different than your traditional shop?

Richard Galanti

Food and sundries overall is -- yes, it's about in line, I would say, on the company averages.

Operator

Your next question comes from the line of Karen Short from Barclays.

Karen Short

A couple of questions. You -- Richard, you commented on the fresh gross margin decline. And I'm wondering if you could just give a little bit of color on that, and that's obviously excluding the poultry. You kind of called that a step-up in price investments.

Richard Galanti

Yes. We're just -- I mean, at the end of the day, our heart is we're merchants, and we try to drive business. And fresh is an area that also is a frequency driver. So it's more -- my comment is more anecdotal than some new change in strategy.

Karen Short

But not necessarily -- also comment on the competitive landscape.

Richard Galanti

No, that is -- the increased level of competition that I've talked about, that goes back 1.5 years plus ago. And that hasn't changed.

Karen Short

Okay. And then can you just maybe clarify a little bit on the -- I guess, the true-up of the breakage estimates?

Richard Galanti

Well, I mean, at the end of the day, it's a small amount of basis points. When we issue a significant amount -- you can kind of back into the numbers yourself of what percentage of our sales are the 2% Reward. And we send out those certificates, and there's always going to be some slippage. Notwithstanding the fact that we send out reminders to our members that you haven't cashed this. At the end of the day, we tend to be -- we do our best guess to accrue for slippage. And I'd like to think that we tend to be a little conservative. And therefore, when there's a review, it picks up the other way. But at the end of the day, we -- accounting rules say you do your best guess of what it should be. And then when you re-review it, you adjust that.

Karen Short

Okay. And then I just want to switch gears to the Shanghai store, and I think you said you'll be opening a second one soon. But maybe any thoughts on what you think that the actual annual volumes could and will settle out at for that store? And then any update on the number of members at that store since the last call? And then, I mean, I ask it in the context that to the extent that China is an opportunity, it's not so much about the units. It's actually about the volume per unit.

Richard Galanti

Right. Well, it's hard to say because this one is so off the charts. I mean, again, the last few weeks -- the last several weeks with some limitations on number of members for some of that period of time, it's changed a little bit. But I mean that was either our top or second-largest location in our company for the several weeks leading up to that. And the number of members is, again, off the charts, nearly 5x the company.

Karen Short

Okay. And -- but would we take that same number and apply that to the total revenue for that box? Or how should we think about that?

Richard Galanti

No, no, no. Because given the population of Shanghai and the fact that this thing went throughout social media, and it was very popular over there, you have a somewhat higher renewal rate. We don't know yet because we opened it in August. But we know from other countries -- I'm sorry, lower renewal rate. And no, and you can't just simply multiply that out. But our -- but the unit overall is, again, either number one or two, up until the last few weeks with what's going on over there with coronavirus, was one of our Top 2 units.

Karen Short

Okay. And then just last question for me. I don't think I've asked this for a while, but do you have any -- are you willing to give an update on what you think or what the -- where the average ticket is in the U.S. of an Executive Member today versus just the basic membership and how that's trended in the last several years? Because it does seem like the momentum is really continuing to increase in terms of your share gains.

Richard Galanti

Yes. Look, we don't disclose that, but more Executive Members and more penetration of Executive Members is good. More members who have the -- in the case of the United States, the co-brand credit card is good. And if they have both, the Executive and that, it's even better. All those things, I think, are -- help our sales growth.

Operator

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

John Heinbockel

Richard, the price investments you mentioned in fresh food, was that actually proactive price investments or more delays in passing through vendor increases? And then where those investments occurred, was that more protein as opposed to other categories?

Richard Galanti

It's definitely proactive on our part. And I think it's all of the above. It's protein. It's fresh -- I mean it's produce.

John Heinbockel

Okay. And then if you -- I mean, if you look at the fresh food comp, right, so I think you said low double digit and that included the final week, right? So that was the best fresh food comp you've had in a while. I don't know if you can parse out, and maybe you can looking at the final week, how much -- was some of that coronavirus-related or was a lot of that step-up related to the price investments?

Richard Galanti

Who knows? Clearly, week 4 was different than weeks 1, 2 and 3 for everything, just the sheer number of people coming into the warehouse. I personally believe that given that restaurants probably have been impacted a little bit the last couple of weeks, they're buying more at supermarkets and more at Costco. So those things helped a little bit as well.

John Heinbockel

And then lastly, when you think about it, I know you said the margin on some of that stuff is sort of in line with the average. When you think about the sort of the cost associated with restocking and dealing with that volume and you think about, I don't know, an EBIT margin tied to that volume, normally the EBIT margin will be -- the incremental margin will be a lot higher. Is that less the case here because of the cost required to keep up with that volume?

Richard Galanti

Well, yes, I think there's a lot of additional things that cost you. I mean there's not a lot of it, but I'm sure there's a little air freight going on. And I'm sure there's -- when you've got a high-cube, high-weight, low-value item like water, 40 0.5 liter is for $2.99 or something, and you're going through it faster than you could put it on the floor, there's more labor and everything else. So -- but it's still a net positive. In the scheme of things, I don't know if it helps or hurts the bottom a little bit. Yes. And the other thing is they're not just coming and getting those 5 items and leaving. They're shopping a little bit. Again, I personally was surprised that patio furniture is strong. And maybe per person, it's a little weaker, but there's a lot more persons.

Operator

Your next question comes from the line of Mike Baker from Nomura.

Michael Baker

Okay. A couple of questions. One, can you tell us how gas profits were this year versus last year? And then remind us, if you could, how much that helped 2Q '19 versus 2Q '18.

Richard Galanti

Yes. I don't have it in front of me, but I believe last year, we said gas helped us relative to the prior year. It was pretty -- it wasn't worth talking about plus or minus either way, this year versus last.

Michael Baker

Okay. Got it. Okay. Shifting gears, a couple more, if I could. So February, even if you take out -- first of all, the 300 basis points, can we take that out pro rata across international and the U.S.? Or is it -- did it impact one region more than the other? And the real question is, when you strip that out, February was much stronger than you've been running even so. In other words, I presume the first 3 weeks were strong. So what do you think is behind that uptick even before you got to week 4?

Richard Galanti

It must be those investments in price. No, at the end of the day, it is generally around the world. I think Korea has been a little less of that -- probably a little less of that benefit. But there's been -- there was an outbreak there that had a lot of publicity, and I think there were more people perhaps staying home or not going out. The -- but when I look at the U.S., Canada and several other countries, all of them had big upticks in that last -- the past 9 or so days. And I'm sorry, what was the last part of the question?

Michael Baker

Just why do you think weeks one -- so weeks 1, 2 and 3 were obviously strong as well because when you take out that 300 basis points, it's still -- you're high single digits. So what do you think is behind that big uptick?

Richard Galanti

There's probably lots of little things I'd like -- my mother would say we're good merchants and great stuff at low prices. There's nothing that stands out completely. Certainly, there was not a lot of press out there of issues around coronavirus, even though it was in the news a little bit. So maybe on a macro basis, there's a little bit of that in there. I think there may have been some weather issues a year ago that may have impacted a little. But overall, we were -- in those 3 weeks, forgetting about week 4, which was off the charts, it was -- we're feeling pretty good about it that some of the stuff we're doing is working from a merchandising standpoint and a pricing standpoint.

Operator

Your next question comes from the line of Rupesh Parikh from Oppenheimer.

Rupesh Parikh

And thanks for all the comments on the coronavirus. So I guess, Richard, just going back to your commentary on the supply chain. So as you guys look forward, at this point, do you expect any impact on your supply chain related to coronavirus? Or is it too early to tell, earlier in the year?

Richard Galanti

Well, I think first of all, there has been an impact on it. It's now starting to get a little bit further than normal, back to normal on regular stuff. On some of the virus-related items that people are buying like water and sanitizing items and paper tiles and things like that, that's going to take a little bit while longer. When I ask the buyers, they're working day-to-day with suppliers. You've got suppliers that are literally working around the clock to produce and to ship. But again, people are coming in and buying stuff, if you will, for their basement.

Rupesh Parikh

And what about -- I guess I was asking more of some of the other categories like electronics and some of those categories that may come from Asia. Just curious if you expect an impact.

Richard Galanti

Well, I think I mentioned there have been -- we have seen some little impact on some laptops and some cell phones, and I think that's related to some of the things that we all read about in the paper about some shortage -- some delays because of some of the component parts. I think one thing that helps us a little is we're able to pivot a little bit. So if there was a shortage or something with one area, we're able to put something else in its place since we sell pretty much everything. But we just don't know what's going to happen tomorrow.

First order of business is to get the supply chains back open and running well. There are two kinds of supply chain issues. There's a supply chain issue related to all these very high demand items related to fighting and protecting yourself, the waters, the sanitizing and things like that. And then there's just stuff. I mean everything from furniture to apparel to electronics coming from China. And on the latter, it seems at least while the one week -- and keep in mind, given the planned Chinese New Year week, there were stuff brought in early, not only by us, but I'm sure others, but then there was two more weeks of closures. So those kind of things over the last three weeks in terms of talking to our buyers, the supply chain has -- and the manufacturers are now back open, they went from 0, if you will, to 25% to 40% to 50% to 60%, 80%, and now it's getting to the ports. And some of those things are also being abated, some of the issues there. So my guess is if everything got better tomorrow, from a concern standpoint, you still have a few weeks here where it takes time to fill those supply chains.

Rupesh Parikh

Great. And one follow-up question. Just on the holiday season. You guys had a really strong performance, even with fewer selling days. So just curious if there's any surprises or what do you think contributed to the really strong outperformance.

Richard Galanti

Well, I think we -- this is -- that's what we do. I mean I think we've done a great job. We've been helped by strong big-ticket categories, like electronics, like patio furniture and lawn and garden right now, and other hardlines and softlines areas. Fresh continues to drive our business. When we -- as you know, when we're asked, what are the 2 or 3 big factors that drive our business -- or categories, it's fresh, it's gas, it's Executive Membership. And again, utilizing those different bucket -- even when sales are good, we want to be aggressive in pricing. And when sales are bad, we want to be aggressive -- more aggressive in pricing. When the sales are good, we want to be more aggressive in pricing. It drives -- the top line improvements drive the bottom line.

Operator

Your next question comes from the line of Scot Ciccarelli from RBC Capital Markets.

Scot Ciccarelli

Richard, you talked about expecting margin pressure to moderate a bit from the poultry plant ramp. And I know there was an incubation period there. So is that plant actually turning out product at this point? And related to that, can you give us an idea of what the incremental benefit you guys are expecting once you're in full production mode.

Richard Galanti

Well, I think it was mid-September when we -- when the first chicken went through the plant, if you will. The plan was that 45 weeks later, there would be approximately 2.2 million birds a week being processed. And so -- call it, September to August. And so we're a little bit past the halfway mark on that. And I believe in terms of projection, we're a little bit past the halfway mark on that. Call it 1 million birds a week. I should be off a little bit on either side. And so a lot of this has to do with the fact that you've got this big facility that is running at well below capacity. The amount of impairment to margin related to that in Q2 was less than Q1. We would expect it to be less than in Q3 and further. So once we get the full capacity, I think -- and then I'm sure there's going to be some operational improvements over the first couple of years as well. At the end of the day, it's a combination of sourcing and just simple supply. And our view is we can improve, if you will, the ultimate cost per bird. But we don't know that yet. We spent a little more than we planned, but we also upgraded the facility to be air-chilled instead of water-chilled. It truly is a state-of-the-art facility for the U.S. and a very high-volume facility. And I would say, right now, things are going as planned in terms of that 45-week cycle. And I would like to think that a year from now -- 6 months from now or two more quarters from now, it's not going to be an issue that we really even talk about as it relates to how it impacted margin.

Scot Ciccarelli

Got you. I appreciate that.

Richard Galanti

We talk about it a little bit. I don't think I'll be that wrong.

Scot Ciccarelli

Got it. And then I know you obviously had the surge in that kind of fourth week, as you pointed out, because of the coronavirus. Warehouses were obviously jammed. Everyone kind of sees that. But I'm curious if you happen to see an even larger increase from e-com in terms of -- like, has there been some sort of shift in consumer behavior at all? Or is all the activity concentrated on warehouses?

Richard Galanti

No. I mean we saw an increase, but not really. I mean mind you that -- no, we saw -- yes, throughout February, we saw some increase in e-commerce. But again, if people are looking for those -- the sense of urgency, I'm going out right now and get it, things like water and everything. And some of those key items, like peanut butter and crackers and the like, we have online as well. And those, too, in some regions, might be in and out of stocks.

Operator

Our next question comes from the line Judah Frommer from Crédit Suisse.

Judah Frommer

I was hoping maybe you could help us with kind of how things trended in Korea over the last few weeks. You have exposure there potentially weeks ahead of where the U.S. could be, worst-case scenario for the virus. So in terms of demand and kind of stock up, and then potentially demand falling off as the virus spread there, any insights there?

Richard Galanti

Well, I think the only insight is -- from what I've read, it is not -- is the issue that more people are staying at home and not even going out. Whereas even near the -- with all the publicity the state of Washington and King County is getting, with a few of the deaths, there are people out and about. There's a little less traffic on the highways, but notwithstanding that it's on the highways coming to see us.

Judah Frommer

Got it. And then kind of changing gears. We've seen some stuff about potentially requiring membership in some food courts in the press. Anything behind the thought process there?

Richard Galanti

Well, first of all, it's gotten more press than it deserves. There are, I believe, 7 current locations on the West Coast, where we -- and I believe they are all outdoor locations. And one of the challenges we've had is particularly on very busy locations, where people that are nonmembers just come and eat there every day. You've got member complaints saying, why are you -- I have to pay to come to Costco. And so we took -- we're testing it in 7 locations that we are limiting it to members only. It's easy in locations where you have the food court inside. But on -- in many of the ones in areas where the weather is generally good, like California, Arizona and things like that, you have a lot of them that are outside. And so we'll see. But again, seven locations out of 540 we're testing it at and it's gotten a lot of press.

Judah Frommer

Okay. Got it. And if I could squeeze in one more. Anything on supply in pharmacy? And any people stocking up there and potentially running out of inventory?

Richard Galanti

This is just a quote from the FDA yesterday. It said while the FDA and other outlets are reporting disruptions and medical products are possible, at this time, manufacturers are reporting that no specific drugs experienced a shortage due to the impact of COVID-19. And talking to our head of pharmacy yesterday, he said the only thing that we've seen, there's been a little pickup there as well. Let's say somebody has a year-long prescription. So 4 9 -- a prescription plus 3 90-day refills for -- and they'll come in and they'll want all 4 of them filled now. And in some cases, even when their particular insurance plan doesn't cover it, they're paying cash. They're just hoarding -- they're hoarding up on their prescription to make sure we're not running out. But that's more, again, I think the same thing you're seeing with paper goods. But from a supply and availability standpoint, we haven't seen anything yet. Why don't we take 2 more questions?

Operator

Okay. The next question comes from the line of Oliver Chen from Cowen.

Oliver Chen

Richard, regarding the supply chain and what you're seeing, what are your thoughts regarding the price increases -- or potential price increases, whether that be from transportation costs or other and what your buyers think may happen there. And the second question is related to e-commerce. You made a lot of progress on your mobile app. Just what's ahead for changes to the mobile app? And also more broadly, capital investments related to e-com and supply chain.

Richard Galanti

As it relates to costs, the general view of the buyers is that we have -- I get back to the comment I made earlier about strong relations. To the extent that there's some raw materials cost increases because of shortages, that's going to rain on everybody. In our view, it rains on us a little less. But I think we -- given the limited number of items we buy and the amount of things we -- the amount of a given item that we buy, our buyers, we feel, know a lot more about the cost structure. And so I haven't seen any commentary on that internally other than there was one small comment -- I can't find it in my mess of papers here, that there may be, in some small cases, some raw material increases on some particular item -- some particular raw material for some manufacturing process. But overall, there's not been a big issue. Right now, the only increase in transportation is on some very limited items where there's been a little bit of airfreight. What we're finding is that the ports, again, are getting back to capacity, and there's plenty of space. And so that's not been as big an issue.

As it relates to an e-com investment. There's not a lot I have on my plate to tell you today. We're working on more things related to our app, to our membership digital app. And we certainly have some things going on, on the fulfillment side of e-commerce. And we've been focused on getting 2 more countries opened, as I mentioned in the last quarter. And we think -- there are a few other things that we've got going on that I'll be happy to chat with the next time around.

Oliver Chen

Okay. Is buy online, pick up in-store going as you like? And do you expect a lot of enhancements ahead to that as customers like it?

Richard Galanti

Well, customers like it, but we don't like it necessarily. We're doing buy online and pick up in-store for some small items -- small high-value items. But we're not at the point where we're looking for members to buy online and come and pick up their whole grocery baskets. So we're trying to figure out our way. And certainly -- again, the last 9 or so days notwithstanding, seems -- things seem to be working pretty well for us in that regard. We continue to work on the -- where we've had good sales and good strength over the last few years in e-commerce is taking certain big and bulky things out of the warehouse, like white goods and things that are delivered, in some cases, installed, and so we continue to work on those kind of things as well.

Oliver Chen

And lastly, Richard, with the surge in demand and the traffic trends that you've seen, how have you managed like this customer and guest satisfaction and also labor in your stores, those kinds of things that we're curious about?

Richard Galanti

How do we measure it?

Oliver Chen

How you managed it and just tried your best to make sure that customers are happy and also you have the appropriate labor levels relative to spikes and changes in demand.

Richard Galanti

Well, again, the last 1.5 weeks, notwithstanding because it's been nuts. No, first of all, member comments and basic member renewal rates. I mean we actually -- the operators and all the way up to Craig see weekly information on comments. You can't imagine how many people call and e-mail when they have something that they're concerned about. And we also measure the least expected but the positive letters to that effect.

On the operations side, the key is still -- well, aside from merchandising, the art of merchandising out there and giving the branch managers, the assistant managers and the merchandisers -- warehouse merchandisers, some leeway, not -- I mean, certainly, electronics is when you walk in and there's defensive promotional goods and fresh is in the back. But at the end of the day, there is a bit of merchandising that is pushed down to the regional and warehouse level. And that's what, I think, drives our business there. In terms of the front end -- managing the front end, I think we've got less count -- 120 of our 540-ish locations in the U.S. with self-checkout. And we plan another 100 in the next 3 months. And so always trying to figure out and measuring the number of member transactions through the front end per hour.

Operator

Next question, from the line of Peter Benedict from Baird.

Peter Benedict

Richard, just two quick ones here to close out. So it looks like the business is probably comping in the 20% range there in that last week, and certainly, the demand is probably even higher than that, just given that you guys are running out towards the end of the day. How do you think about the ability for the club to kind of keep up that take -- with that pace of demand? I mean if this were to go on for three, four more weeks, do you guys think you've got -- does the supply chain able to keep up with that level of demand? Or are you hitting a point where you're not -- you're just not going to get another delivery tomorrow of pick your category?

Richard Galanti

Yes. No. Well, I think it's all over the board. Yesterday, I think there was a couple of -- either Los Angeles or San Diego counties that announced a heightened level of concern. King County here in Seattle did that a couple of days ago. When that happens, that's another catalyst that puts people to go out and get more stuff. I would hope -- and look, we would all hope this thing peaks and starts to slow down. It depends what happens tomorrow. We'll be tired but still working hard. Given that half of our employees -- roughly -- a little over half of our -- of the 90% of employees in our warehouses that are hourly, about a little over half of those 90% are full-time and a little under half are part-time. Certainly, there are employees that want to work more than part-time, and so we've been able to accommodate some additional hours there. But everybody is a little tired but that's what you do.

Peter Benedict

Okay. And then my last question is just on lawn and garden, you mentioned that a couple of times, and you talked about seasonal. Maybe expand on that a little bit. Where in particular are you seeing the strong -- I guess, it's an early start to spring, but maybe talk a little bit about what you're seeing on that front.

Richard Galanti

Well, the only thing I mentioned there was that in -- and getting ready for today's call, I had spoken to several of the senior merchants in the different categories. And one thing without even looking at the numbers, I thought, is I assume some of the big-ticket discretionary items might be a little weaker because people are not running in to get those items. They're running in to get other concerned items. And the fact was, to my surprise, that they said that certain items like patio furniture and lawn and garden was strong. They felt -- and again, it was just their view, that patio -- lawn and garden was more related to some of the areas of the country where the weather has turned already. And -- but clearly, because you got X percent more people coming in every day than normal.

Okay. Well, thank you, everyone. Have a good afternoon, and we're around to answer any questions. Have a good day.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.