

## Costco Wholesale Corp:

### Warehouse Sales with Loyal Members Around the World

Costco Wholesale is one of our stellar investments. The first purchases were made in 2016 with prices in the range US\$142-\$151. The price is now approximately \$550. Importantly, EPS has grown from \$5.33 to \$12.70 over this time.

Charlie Munger has served as a director of the company since 1997. Recently he said: "I think Costco is going to be a big, powerful company as far ahead as you can see. And I think it deserves its success. I think it has a good culture and a good moral ethos. I wish everything else in America was working as well. Think what a blessing that would be for us all." He also said it "is going to be an absolute titan on the internet, because it's got curated products that everybody trusts and huge purchasing power on a limited number of stocking units."

**Strategy:** Costco provides low price quality household products sold through 815 mega-stores (referred to as warehouses) around the world: At August 29, 2021, Costco operated 815 warehouses worldwide: 564 in the U.S. located in 46 states, Washington, D.C., and Puerto Rico, 105 in Canada, 39 in Mexico, 30 in Japan, 29 in the U.K., 16 in Korea, 14 in Taiwan, 12 in Australia, three in Spain, and one each in Iceland, France and China. They typically open 20-30 new stores per year.

The key distinguishing feature of Costco is that they charge a membership fee of around \$60 per year. Basically all their profit each year comes from these fees. For example, in FY21 fees totalled US\$3.35b while net income was \$3.66b.

They have almost no mark-up on what they sell apart from minimal overheads so Members feel confident that whatever they buy at Costco will not be available elsewhere for less.

The other key distinguishing feature of Costco is the length they go to make sure their overheads are as low as possible.

Another cost-saving feature is that they have only approx. 4,000 SKUs per warehouse. Instead of 20 or 30 brands and sizes of, say tissues, Costco will only have a single brand in a single (generally large) size.

**Success Drivers:** Costco have a formula for starting and running warehouses. Starting with the US and Canada, this formula has been shown to work globally.

Costco generates more than US\$1,100 in sales psf. In comparison, Wal-Mart generates roughly US\$420 psf: Keep costs down, pass on the savings. Adam Baines, the Costco Warehouse Manager for North Lakes in Queensland, explained that it was a "top-line" company. This meant doing everything possible to make sure they have top products at best prices so that they would continue driving sales. He explained the philosophy of choosing staff that espouse the Costco approach: choose good people, give them good jobs, and pay them good money—then good things will happen.

**Economic Moats:** Costco's membership creates a unique "obligation" for people to keep coming back to justify their upfront costs. A second moat is that it is almost impossible for others to compete on price.

**Key Future Risks:** A key risk is that they fail to stock products that their members want and sales start to drop. A related risk is that they fail to sell inventory and must discount it. Another risk is they fail to maintain membership growth and loyalty.

Dividend Yield	ROE	5 Year Growth	
		SPS	EPS
0.7%	27.9%	9.7%	15.6%

• Market Cap: \$232b • 5-yr Total Return: 31.0% pa

**Conclusion:** Costco is run exceptionally well with strong moats. It has significant opportunities for steady growth around the world for years to come.

*This report is prepared for members of the Conscious Investor Fund. It does not take into account anyone's personal circumstances. Remember, what happened in the past is not always what will happen in the future. Questions? Contact us: Conscious Capital AFSL 427 216 Level 3 Suite 2 80 Mount Street North Sydney NSW 2060, ph 02 9416 1941*

Confidential: Do not photocopy or distribute © Conscious Capital October 2022