Costco Wholesale (COST) Earnings Report: Q3, 2015 Conference Call Transcript

The following Costco Wholesale conference call took place on September 30, 2015, 11:00 AM ET. This is a transcript of that earnings call:

Company Participants

- Richard Galanti; Costco Wholesale Corporation; EVP and CFO

Other Participants

- Charles Grom; Sterne Agee CRT; Analyst
- Simeon Gutman; Morgan Stanley; Analyst
- Paul Trussell; Deutsche Bank; Analyst
- Oliver Chen; Cowen and Company; Analyst
- Dan Binder; Jefferies LLC; Analyst
- John Heinbockel; Guggenheim Securities LLC; Analyst
- Bob Drbul; Nomura Securities Intl; Analyst
- Meredith Adler; Barclays Capital; Analyst
- Michael Lasser; UBS; Analyst
- Peter Benedict; Robert W. Baird & Company Inc.; Analyst
- Scott Mushkin; Wolfe Research; Analyst
- Greg Melich; Evercore ISI; Analyst
- Matthew Fassler; Goldman Sachs; Analyst

MANAGEMENT DISCUSSION SECTION

Operator:

Good morning. My name is Kayla, and I will be your conference operator today. At this time, I would like to welcome everyone to the Q4 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)

I will now hand today's call over to Richard Galanti. Please go ahead, sir.

Richard Galanti (EVP and CFO):

Thank you, Kayla. Good morning to everyone. Last night, we reported operating results for the 16-week fourth quarter and 52-week fiscal year that ended August 30. These results are compared to the similar 16- and 52-week periods of FY14, which ended last year on August 31.

Please note that these discussions will include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements address risks and uncertainties, and may cause actual events, results and/or performance to differ materially from those indicated by such statements. These 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.

To begin with, our fourth-quarter FY15 operating results. Net sales for the fourth quarter came in at $35 billion, up 1% overall a year ago. Comp sales were down 1% on a reported basis, but were up 6% including the negative gas and FX impacts. Gas prices for the quarter were down 21% year over year, negatively impacted US comp figures by a little more than 3 percentage points, so a plus[6%] US comp excluding gas price deflation.

Foreign currencies overall were weaker relative to the dollar, year over year, in the fourth quarter, such that our reported international comps, on a reported basis, of minus 10% in Canada and a minus 7% in other international, assuming flat year-over-year FX rates and excluding gas price deflation, would have been plus 7% in Canada and plus 6% elsewhere internationally. For the quarter, earnings per share came in at $1.73, up $0.15 or 10% from last year's $1.58 figure. In terms of a year-over-year comparison -- EPS comparison, a few items of note. And the biggest item of note, FX. In Q4 year over year, the foreign currencies where we operate were weaker versus the US dollar, resulting in our reported foreign earnings this year in Q4 being lower by about $53 million after tax, or $0.12 a share, than these earnings would have been had FX exchange rates been flat year over year.

Number two, income taxes. Our income taxes this year in Q4 included several discrete items that, in the aggregate, decreased our income tax line by $23 million, or about $0.05 a share. The largest component of the $23 million figure was a $17 million, or almost $0.04 a share, income tax benefit that resulted from our decision to repatriate, in the near future, from Canada back to the US, CAD750 million, or about $560 million, of cash balances. Third item of note, IT modernization. As discussed in the past several quarters, our major IT modernization efforts are ongoing, and will continue to negatively impact our SG&A expense percentages through the next fiscal year, and possibly beyond, especially as new major systems are placed into service and depreciation begins. In the fourth quarter, on an incremental year-over-year basis, these costs impacted SG&A by an estimated $22 million, or 6 basis points, 4 basis points without deflation and FX, or about $0.03 a share. And lastly, LIFO. Last year in the fourth quarter, we recorded a pretax LIFO charge of $11 million pretax, or $0.02 a share. This year, we actually had a LIFO credit, or a bring-back of $14 million pretax, or $0.02 a share. A lot of that had to do with gas deflation.

In terms of new openings for all of FY15, we opened 25 new locations, which included two relos, so a net of 23. 12 new in the US, 3 each in Mexico and Japan, and 1 each in Canada, UK, Taiwan, Korea and Australia. Which therefore ended FY15, a few weeks back, with 23 net new warehouses, and a total of 686 locations operating worldwide. For the current FY16, our plans are to add up to 32 net new warehouses, including a few business centers in the US. 18 to 20 of the planned new locations will be in the United States, with the remaining in international markets, including our second opening in Spain and our first opening planned for France. During the first four months of 2016 through calendar year end, we plan to open 13 of those up to 32 warehouses, including two relos, so net of 11. 9 in the US, 1 each in Canada, Australia, Japan and Spain, and then the 2 US relos are in that 11 figure -- in the 9 figure, sorry.

Also this morning, I'll review with you our membership trends and related activities, our e-commerce activities. Plenty of discussion on margins and SG&A, and recent stock repurchase activities. Okay. So for our fourth-quarter results, sales, again, for the fourth quarter, the 16 weeks ended August 30, were $35 billion, up 1% from last year's $34.8 billion. On a reported basis, again, comps were down minus 1%. For the quarter, this minus 1% reported comp figure was a combination of an average transaction decrease of about 4.5% for the quarter. And again, this included a detriment from FX of a little over 4%, and gasoline price deflation of a little over 2.5% impact. So as you can see, excluding these negative factors, comps overall were up 6%, and the transaction actually, on an ex-gas and FX, would have been slightly positive. And an average frequency increase of just under 4%, at about 3 3/4%.

In terms of sales by geographic region, most US regions registered low single-digit comp increases. Again, these numbers include the impact of gas deflation of a little over 3% in the US, with the Midwest, Texas and California being the strongest. Internationally, in local currencies, the strongest results were Australia, Mexico, Taiwan and Spain, recognizing Spain only has one new unit -- one unit. In terms of comp sales by merchandise categories for the quarter, for food and sundries, comps were mostly flat for the quarter. Again, all these figures include about a 4% detriment from FX. The better-performing departments were deli, sundries and candy. Within hard lines, in the low single-digit range, better-performing departments were sporting goods, hardware and automotive. Consumer electronics were negative low single-digit year over year, positive low single-digit ex-FX. For soft lines, comps were in the low single digit range. Better-performing departments included home furnishing and domestics. And within fresh foods, comps were in the low single-digit range, as well, with the best results in deli, produce and meat.

Moving on down the income statement to membership fees. On a reported basis, membership fees came in at $785 million, or 2.24% of sales. That's up $17 million, or 2% in dollars, and up 3 basis points. Again, FX has a big impact on these dollar figures. Assuming flat year-over-year FX, the 2% dollar increase would have been up 6%. In terms of membership, we continue to enjoy strong renewal rates, 91% in the US and Canada and 88% worldwide. And a strong -- also, we're enjoying strong sign-ups, both new and existing warehouses, and continued strength in our executive member program. In terms of members at fiscal year end, we had 34 million gold star members, up from the most recent quarter of 33.2 million. Primary business, 7.1 million, up from 7 million. We continue to have business add-on members of 3.5 million.

So all told, member households, 44.6 million at fiscal year end, which is up from 43.7 million 16 weeks earlier. Including additional cards, total card holders out there stood at 81.3 million at fiscal year end, up from 79.6 million a fiscal quarter ago. At fiscal year end, executive memberships were 16.1 million, which was an increase of about 400,000 members since Q3 end, so about 25,000 a week increase in the quarter. In terms of membership renewal rates, as I mentioned, they continue strong. Total came in it at -- rounds up to a 91%, and -- for US and Canada, And total worldwide rounds up to an 88%.

Getting back to the income statement. Our gross margin in the fourth quarter, on a reported basis, was higher year over year by 44 basis points, coming in at 11.14% this year, versus a year ago fourth quarter at 10.7%. And without the impact of gas price deflation, that increase would be up 15 basis points. Now I ask you to jot down just two columns of numbers, looking just at the fourth quarter here. The column one would be reported basis, and column two would be without gas deflation. First line item would be core merchandise. On a reported basis, year over year, up 17 basis points, ex gas deflation, down 8 basis points. Ancillary businesses reported plus 25, without gas, plus 18. The 2% reward increasing sales penetration related to executive member sales and the 2% reward, minus 5 reported, and minus 2 ex gas. LIFO, plus 7 and a plus 7. And total reported basis, as I mentioned, plus 44 basis points, and ex-gas plus 15.

Now reviewing these figures, again, the core merchandise component was up 17, but minus 8 without gas. Primarily a function of improved year-over-year gross margins within our gasoline and several other ancillary and warehouse businesses. The core merchandise gross margin, which I define as the main four departments -- merchandise departments: food and sundries, hard lines, soft lines and fresh foods -- as a percentage of their own sales, were actually up 13 basis points year over year. Food and sundries, hard lines and soft lines were up year over year, while fresh foods was a little lower.

Ancillary and other business gross margins were up, as I mentioned in the chart there, up 25 basis points, plus 18 without gas. We enjoyed broad-based strength across most of our ancillary businesses, with year-over-year gross margin improvements in gas, optical, hearing aids, as well as solid operating results in e-commerce, business centers, travel and executive member services. And LIFO in the fourth quarter, as I mentioned, was about -- year over year, was a 4 basis point benefit, or $14 million, compared to a 3 basis point detriment a year ago, of $11 million. Our year-end inventory shrink results were in line with our all -

time best results, and our inventory positions are in great shape. All in all, gross margins of inventory is in good shape.

Moving on to the SG&A. Our SG&A percentages, year over year in the fourth quarter, were higher or worse by 27 basis points, coming in at -- right at 10% of sales this year, compared to 9.73% last year. Again, taking out gas deflation, essentially flat year over year, higher or worse by 1 basis point. Again, I'll ask you to jot down the two columns, Q4 reported and Q4 ex-gas deflation. In terms of operations, reported minus 15, or higher by 15 basis points, without gas deflation, plus 8 basis points, or lower or better by 8. Central, a minus 7 and a minus 5. Stock compensation, a minus 5 and a minus 4. All told, we came in, on a reported basis, higher by 27 basis points of SG&A. And again, ex-gas deflation, minus 1 basis point. And looking at these figures, the operations component of SG&A was higher, again, or worse by 15. And again, excluding gas, lower or better by 8.

Within operations, ex-gas deflation, core warehouse payroll and other operating expenses were better by 10 basis points, half of which was improvement in payroll percent. Central expense was higher or worse by 7 basis points year over year, 5 without gas, with nearly all that variance coming from our IT modernization efforts, 6 and 5 basis points, respectively, with and without gas deflation. Lastly, stock compensation expenses represented, again, a minus 5, minus 4 without gas, just we have over 4,000 people on our plan, and that's done well as a compensation tool.

Next on the income statement is pre-opening, higher by $12 million, coming in at $27 million this year versus $15 million a year ago. Last year in the quarter -- in the fourth quarter, we had 10 openings; this year we had 13. Of the $12 million year-over-year incremental expense, which is about $0.02, a share, a little under half of it is due to incremental units, 13 versus 10. The rest, about $7 million of variance, is simply an increase in pre-opening expense associated with upcoming openings they the first several months of our new fiscal year, versus the similar period of a year earlier. All told, reported operating income in the quarter increased $65 million, or 6% year over year, to $1.156 billion this year.

Below the operating income line, reported interest expense was higher year-over-year, coming in at $40 million this year, up from $35 million a year ago. This is mostly due to the interest expense on the $1 billion debt offering that was completed earlier this calendar year, to fund a portion of the special dividend. Interest income and other was higher or better year over year by $10 million, coming in at $40 million this year in the fourth quarter, versus $30 million a year ago. Actual interest income for the quarter came in at $12 million, compared to $17 million a year ago, so actually lower by $5 million. The other component of interest income and other was higher or better by $15 million, primarily related to various FX related items, a lot with the foreign countries, when they're locking in some of their FX needs.

Overall, pretax income was up 6%, or $70 million, this year versus last year. In terms of our tax rate, our Company tax rate for the quarter came in lower than last year, 32.7% this year versus 35.1% last year in the quarter. Again, we benefited from several discrete items in Q4, as I explained -- discussed earlier in the call. Such that overall net income was up 10% or $70 million, coming in at $767 million this year in the fourth quarter versus last year's fourth quarter, net earnings of $697 million. For a quick rundown of other items. While the balance sheet is included in this morning's press release, a couple of quick balance sheet info items. Depreciation and amortization for the fourth quarter came in at $351 million, and for the year, $1.127 billion. Our accounts payable, as a percent of inventories, on a reported basis was essentially 100%, 101%, both last year and in this year, fiscal year end. Ex non-merchandise payables, mostly construction-related would be that, both last year in fourth quarter and in this year fourth quarter, it came in at 89%.

In terms of inventory per warehouse, average inventory per warehouse was up $200,000, or 2%, to $13 million at Q4 end this year, up from $12.8 million. That's -- the actual number, again, excluding -- assuming FX was flat year over year, would have been $535,000, or up about 4.2%. The increase pretty much spread across many departments. No real surprises there. Overall, our inventories are in good shape, as I mentioned earlier. In terms of CapEx, in the fourth quarter, we spent $805 million. And for all of 2015, capital expenditures totaled $2.4 billion. Our estimate for FY16 CapEx is an increase from that $2.4 billion level, somewhere in the high [$2 billions], somewhere between $2.8 billion and $3 billion range.

This year-over-year increase in CapEx represents our plans for more openings this year versus last year. Increased spending for remodeling, expanding ancillary business operations, planned expansion of our cross-dock and distribution operations, and expenditures related to our ongoing IT spending for our modernization efforts. In terms of Costco online, we're still operating Costco online in four countries: US, Canada, UK and Mexico. For the fiscal year, total e-commerce sales came in just under $3.5 billion, up a little over 20% for the year. Comp sales in e-commerce again - were also up 20%, for both the fourth quarter and the fiscal year.

In terms of expansion, I talked earlier about up to 32 units. Net of relos, we would expect 11 in Q1, 3 in Q2, 7 in Q3 and 11 in Q4, Q4 being a little longer fiscal period, of 16 weeks versus 12 weeks, than the others. In FY15, I mentioned, on a net basis, we added 23 units on a basis of 653, so about 3.5% square footage growth. This year, assuming the 32 units on a base of 686, that would be just under 5% square footage growth. In terms of new locations by country, assuming that 30, 32 figure, about 18 in the US, Canada up 3, 2 each in Japan and Australia, and 1 each in UK, Taiwan, Korea, Mexico, Spain and France. As of fourth quarter end, total square footage stood at 98.7 million square feet.

In terms of common stock repurchases, buybacks, for the fourth quarter, we spent $260 million on 1.836 million shares, at an average price of just under $142. On an annualized basis, that would be about $850 million, as an annualized run rate during the quarter. For the year, we spent $494 million, at an average price of $142.87. In terms of dividends, our current quarterly dividend stands at $0.40 a share, or $1.60 a share annualized. It was up 12.5% from the prior quarterly rate, and paid in the first two quarters of FY15. This year's $1.60 per share dividend represents an annual cost to the Company of about $700 million. And as you know, back in February, we did a special dividend of $5 per share, which was a total of a $2.2 billion special dividend paid out to shareholders.

Lastly, and before I turn it over to Kayla for Q&A, our FY16 first-quarter scheduled earnings release date, for the 12-week first quarter ending on November 22, will be after market close on Tuesday, December 8, with the earnings call the following morning on the 9 of December. With that, I'll open it up for questions, and turn it back to Kayla.

QUESTIONS & ANSWERS

Operator: (Operator Instructions)

And our first question comes from Charles Grom from Sterne Agee CRT.

Charles Grom (Analyst - Sterne Agee CRT):

Good morning, Richard.

Richard Galanti (EVP and CFO):

Hi.

Charles Grom (Analyst - Sterne Agee CRT):

Just on the core margin performance in the quarter, I think you said it was up 13 basis points. Could you delve into the performance by the four sub-categories? I know you said that food, hard lines and soft lines were all up. Just curious, the -- (multiple speakers) why the pressure on the fresh food side?

Richard Galanti (EVP and CFO):

I think the pressure on the fresh food side is us. We -- when you've got some inflation on some of the commodity items, like eggs, you -- or nuts, you've got a -- we're not changing the price of a 16 pack of muffins, or a slice of pizza, or hot dogs. So it has more to do with that. Nothing really surprising there. If you look at each of those four categories, again, overall, the gross margin as a percent of sales, their own sales, year over year in the quarter, was up 13 [basis points]. I think the range was in the low [20%s], on the high side, and the mid-teens on that negative downside. So not -- pretty much similar or slightly above last year. No real big changes there.

Charles Grom (Analyst - Sterne Agee CRT):

Okay. Good. And then when you look to next year, just switching gears a little bit, when you switched to Visa from AmEx, can you shape out for us how the switch is going to work and be handled? And what you're planning to do with the interchange savings that you're going to generate? And also, just looking back, how you handled it in Canada, and any surprises on that front?

Richard Galanti (EVP and CFO):

No. Things in Canada, first of all, went -- have gone fine, a little different in Canada because of certain Canadian issues. The portfolio was not purchased by the new issuer, so we had -- essentially, you have people apply for it. That being said, they shop at Costco , they want that co-branded card, and it's done just fine. You see a little bit of change in renewal rate when that happens, because of auto renewals. You've got to re-sign people up and everything. But from an improvement in terms of additional monies, be it for us, in terms of lower merchant fees, or our members, in terms of better rewards on the co-brand, that's all been as planned.

In the US, we're working through everything right now. The plan is for, again, the current contract ends on March -- the end of March next year. That could be in and around a month or two from there. The two parties, AmEx and Citi, continue to work towards that end, and we would expect to tell you more when we can. In terms of how it's going to be split between merchant fees and rewards, I think our -- I think I've stated in the past, our philosophy is to, when we save money on product purchases, we want to give most of it back to the consumer, to the customer. And we're looking at all kinds of opportunities to do that. So stay tuned.

Charles Grom (Analyst - Sterne Agee CRT):

Okay. Fair enough. And just last question, August comps were obviously pretty good. Just wondering, with September almost closed here, any surprises on September sales for you guys?

Richard Galanti (EVP and CFO):

If I could tell you, I would. We'll wait until next week.

Charles Grom (Analyst - Sterne Agee CRT):

All right. Fair enough. Thanks.

Operator: Our next question comes from Simeon Gutman from Morgan Stanley .

Simeon Gutman (Analyst - Morgan Stanley):

Good morning, Richard. Quick question. I think you telegraphed this on the sales side, Labor Day, realizing it was in September both years. But this year, the quarter may not have caught the -- I guess the lead-up to it. I don't know if that's a big deal, from a sales or earnings perspective. Just quickly on that.

Richard Galanti (EVP and CFO):

More of just a sales perspective, given you're talking mid single, low single-digit numbers, reported -- normalized and reported. We basically, in August, it was a -- we feel, a negative impact of about 1 percentage point, and there will be a corresponding improvement in September reported for the same reason. Because of the -- but it's four weeks versus five, so it's a little less of a positive, maybe 0.7% or 0.8%, if our crystal ball is correct. So yes, the August numbers were impacted negatively a little, the September number will show a little positive [to that], and we'll point that out in the release.

Charles Grom (Analyst - Sterne Agee CRT):

Okay. And then the second question, on membership fees and potential increases. Just a question on the thought process, and I think in the past, largely, you've done them to cover inflation. I'm sure there's been inflation over the past five years in many areas. So can you talk about considerations, and how you think about it? Are you surveying? Are you probing customers ahead of time, to understand what's tolerable? And then taking into account that the landscape is evolving a little, you have some nontraditional online model, membership model. So how do you think about the right range to raise that?

Richard Galanti (EVP and CFO):

I think we've done six $5 increases over roughly 30 years, generally about every 5 or so years. We don't do a lot of polling. We look at it internally of, have we improved the value of that membership to our member? In terms of the tolerability of it to the member, I know our historical $5, and in the case of the executive member last time, five years ago, a $10 increase, is a heck of a lot less than we see in other types of fees out there, be it fees for your television or your phones or other services out there. So I personally don't think it's going to ever be an issue. When is -- we really haven't talked about it a lot. It's something that we'll probably do at some point, but stay tuned.

Simeon Gutman (Analyst - Morgan Stanley):

Okay. Thanks.

Operator: Our next question comes from Paul Trussell from Deutsche Bank.

Paul Trussell (Analyst - Deutsche Bank):

Good morning, Richard. Wanted to just discuss assortment and fulfillment online. Certainly, across the industry, there's been a lot of competition and investments being made in fulfillment, whether it's Amazon , or Jet.com, or some of the newer initiatives from Sam's Club. Could you just discuss some of your recent -- your recent online sales trends? And any updates that you could provide for us on upcoming enhancements around assortment or fulfillment online?

Richard Galanti (EVP and CFO):

I don't think there's -- in terms of -- there are a few things I mentioned over the last few quarters, on a topical basis. We certainly expanded, to some extent, the SKU selection, and added what I'd call more frequently purchased items, be it food and sundries or a few office needs. Everything from, again, sundry items to health and beauty aids, K-cups, a few apparel items. And so we've expanded that. We took certain key departments and brought them in line. So we're not competing with each other, and providing, I think, a little more excitement to that.

We ship out of more than one depot. When we first started this, for the first several years, in the US, everything was shipped out of one depot in Southern California, which meant that it might take a little longer to get to you, and it cost us a little more, in terms of delivery or the member. And as we've expanded, we've improved that quite a bit, as well -- quite a bit for us. And we're pleased with the fact that sales for the last -- gosh, the last two or three years at least -- have been, on a year-over-year comp basis, around 20%. So we're doing it methodically. We're not going to go crazy out there.

I think our mobile apps have improved, and will continue to improve. And we like the value proposition we have. We're recognizing that we can't be everything to everybody. That's not what we do for a living. And -- but we have great value. We also like the fact that some of these other services are buying from us. Some of our top customers are some of those guys. So if we can't deliver that single unit of milk or cereal to your doorstep, someone that is may want to buy from us.

Paul Trussell (Analyst - Deutsche Bank):

Got it. That's helpful. And you spoke about the impact to margins, from an IT modernization standpoint. Could you just give us a little bit more detail about what some of the latest focus points have been, in terms of system upgrades? And what we should be looking forward to you all tackling over the FY16 period?

Richard Galanti (EVP and CFO):

Going back, again, three-ish years ago, we embarked on a pretty significant effort to really upgrade and modernize all our systems. Our systems were, for the most part, legacy system, many of them written in-house, many of them, what I'll say, were Band-Aided over the years. And worked fine, but were arguably strained. Some of the systems that were included in that, that were not legacy were from outside suppliers that were not going to be supported going forward, or had not been supported. And so we probably started a little later than we should have a few years ago, and we've got a lot going on.

As I've indicated over the last -- each quarter, frankly, what we try to do is just show you really what the expense associated with those incremental efforts are. We've installed a new membership system a little under a year ago, I think. We installed a new point of sale system, which is another deliverable, if you will. There's a lot of small deliverables that I won't go into. We've got several more over -- that are heavy into the expense side, and should be forthcoming over the next year to two years.

The other thing I mentioned, in terms of -- I talk where it's hitting SG&A. On an incremental basis, over the last few years, I think we're now up to something in the low teens, 12, 13 basis points. Those [2s, 3s and 5s] that have added each year. And recognizing your denominator, your sales, [ex piece expense] over sales, sales keep increasing. We're seeing all the costs associated with it. I think we'll start to see benefits when we look out beyond 2016. Doesn't mean that this SG&A line will not go up a few more basis points. We'll see.

But we're -- there's a light at the end of the tunnel. It's -- sometimes it's long. Some days it's a longer tunnel than others. But we're starting to see some deliverables from it. So there's not a lot I can tell you about where the benefits are. There are clearly some benefits that we're going to see, on the transportation side, and some of the ancillary businesses like travel and other things. But the big switch-over will be when buyers are buying on the new system a year or so down the road, and as well as the benefits in transportation and other. But we don't want to put any dollars or basis points on those improvements. We had to do this, if we want to double our size over a 10 or so year period, starting a couple years ago with these expenses. Because we had a lot of systems that were really strained, and this is going to set us up for the years to come.

Paul Trussell (Analyst - Deutsche Bank):

Much appreciated. Good luck.

Operator: Our next question comes from Oliver Chen from Cowen and Company.

Oliver Chen (Analyst - Cowen and Company):

Hi. Thanks a lot. Good morning, Richard. Regarding a bigger picture question, and I was curious about your thoughts on what really set you apart from other Internet pure plays, in terms of your supply chain and vertical integration? And then this buying scale and scale you have [out] there? And then also, international is a nice piece of the business. Just as we look at our models, and talk to this part of the story, which countries do you have the most opportunity to increase your store base versus maximum potential? Thank you.

Richard Galanti (EVP and CFO):

Sure. In terms of e-commerce, first, we're different because -- for us, we have a lot more items. We have 8,000 or 10,000 or so, instead of 3,700 in-store. That's a nit, compared to everybody else out there, that has hundreds of thousands if not millions of items. I think what separates us is, we've got -- certainly, we and others will have great quality merchandise. We've got the best pricing overall. We work on margins that are at or slightly below our reported total Company margins, but up there in the high singles, very low double digits. We'll compare that to anybody out there.

Again, we recognize we're not going to be selling single items delivered within an hour, or four hours, or overnight necessarily. The -- but in a methodical way, we think we're doing just fine, and we think we'll have additional opportunities. And as I mentioned earlier, we're selling to a lot of these other guys that are wanting to deliver in certain unique ways. There's room for all of us. We've got to keep -- there's a -- it's a big pie out there, in terms of market share, and we think that we'll be able to take our share of that. Some little sub-departments, you lose a little. Others, you make a little. Certainly, we want people to still come into our warehouses.

In terms of opportunities outside of -- in terms of warehouse club growth opportunities, I think the first comment, and for those of you on the call who have known us for a long time, the market potential keeps improving. I don't think we ever would have thought, when we had 60 or so locations in Canada, we'd ever thought we'd have more than 80. We now have more than that, and we'll certainly be over 100 at some point in the next several years. In the US, we're expanding. If you had asked me five years ago, when we were 80 US, 20 international, I'd say five years hence, or now, it's probably 50/50, and going further south, in terms of the percentage of openings in the US. We keep finding more opportunities here. So that's good news.

In terms of other countries, we think we've certainly got a lot of potential in the three countries in Asia we're currently at. Bigger market, of course, is Japan, much bigger than Korea and Taiwan. But we think we can go from the low teens in each of Taiwan and Korea, double over the next 10 years, but we'll see. It's one at a time. Australia, we only have seven units in a -- seven? Yes, in a country that's, what, two-thirds, or a little more of that, than the population of Canada, which has 80 or 90. And I'm not suggesting we're going to have two-thirds of that any time soon, but we certainly can add a few there. Western Europe, we'll see. It's been tough getting in, with all the rules, regulations and permitting process. But we're pretty interested in continuing that process.

Again, we'll open our second unit in Spain next month, in Madrid, in Getafe. A third unit, second in the Madrid area, next calendar year. And hopefully, our first in France towards the end of the next fiscal year. So we think there's plenty of opportunities. I think we feel comfortable that, over the next five years, we'll continue to open 30-ish-plus units a year. We thought we would do that this year that just ended, up certainly in the high 20s. A few of those got delayed, and that's life, but we've got a pipeline that's full. The international generally takes a lot longer, for a variety of reasons, by country. And -- but so we think that we'll continue to grow, and do just fine, in terms of that.

Oliver Chen (Analyst - Cowen and Company):

Okay. And Richard, just a quick follow-up. There has been talk, in terms of competitors, in relation to how competitors are dealing with vendors. Could you just update us on your thoughts, on your vendor relationships? And any catalysts there? Given your buying scale and your leverage and your heritage, I was just curious on your thoughts. Thanks.

Richard Galanti (EVP and CFO):

I'd like to think that the comment that we shared internally, and that we talked to you guys about, is that we're tough but fair. We are tough. We fight for our member every day, and we -- I'd like to think that we do that as much, if not more, than anybody else. The good news about us, in terms of our view of our competitiveness is, is we give the vast majority of any improvement back to the member. And that, in our view, creates that moat that hopefully continues to get bigger. We -- one of the challenges and opportunities we have is just the sheer size of our needs of various commodities -- organics, nuts, long staple cotton, you name it. And so we've got a lot of efforts in that area that I think many of our competitors don't necessarily go to that level, because they're dealing with vendors, and lots of more items.

And so I think we have some opportunities and challenges that -- but opportunities and challenges that I think create something special about us. I don't think anything has changed. We -- as we get bigger, we can be tougher, but still fair. And we work with our vendors. We think we have good relationships with them. Would assume that most of them would agree, probably a few don't. But we'll continue to be very transparent in how we deal with our vendors, and we have very good relationships with many, many of them.

Oliver Chen (Analyst - Cowen and Company):

Best regards. Thank you.

Operator: Our next question comes from Dan Binder from Jefferies.

Dan Binder: Hi, good morning, it's Dan Binder. My question had to do with ancillary margins. The last five quarters, you've had three quarters where ancillary margins were up about 15 basis points, ex-gas deflation, and then two quarters where they were up substantially more than that. It happens to coincide with the decline in gas prices. And what I'm trying to understand is, how much of that gross margin improvement in ancillary is sustainable? Versus just being a function of the way gas was fluctuating during the quarter?

Richard Galanti (EVP and CFO):

Gas, for I think most if -- I think most of the last five fiscal quarters, on a year-over-year basis, has helped a lot. But other -- the other ancillary business continue to grow. And whether it's optical or hearing aid, or some of the other warehouse club businesses, all those things add up. Travel, you name it. So I think -- I hope it's sustainable. Other -- clearly gas, we have no illusion that at some point in life, gas prices go up and margins -- our margin will be more normal relative to our history. Right now, it's good for our member, in terms of low gas prices, and good for us, in terms of, albeit a lower top line sales, it's been more profitable on a year-over-year basis.

Dan Binder: Okay. And then the other item I wanted to talk about was other income, which I realize is a function of these FX contracts you talked about earlier in the call. Always a challenge to model. I'm just curious, if FX rates were to stay roughly where they are today, how do you think that line item would look in Q1?

Richard Galanti (EVP and CFO):

All I -- I don't know. All I can tell you is, is that we look at it that way, too. We manage it, in the sense that if you've got a foreign country, where some of their inventory purchases are paid for in dollars or euros sometimes, but use dollars as the bigger example, they will -- once they're comfortable with a price point, that they're going to be able to convert at that level, and sell goods in their local currency in their local country, they're going to choose to figure out how much of that they want to lock in. Recognizing locking in just makes it that they're comfortable at that price. If the local currency continues to weaken, that was good. If local currency then strengthens relative to the US dollar, shouldn't have done as much.

But we don't try to be completely right either way. And so I think over the years, in the last four or five years, that's a number that has probably ranged from plus or minus $15 million pretax, usually a little less than the number that we had this period, where it was up about [15] or so. But -- and I'd say it's -- we just want to point it out, because it's the component of the income statement. It's very hard to predict. I think by doing it -- I think by doing it the way we do it, we're not going to ever have any giant surprise either way, because of some drastic change in FX prices.

Dan Binder: And then the last item, the share repurchase picked up a bit this quarter. How are you thinking about it for next -- for this coming year?

Richard Galanti (EVP and CFO):

Well, we'll tell you each quarter end. It's part of our -- what we do with our cash. We -- as long as we feel good about our future, we're not going to ever be -- we're going to buy on a regular basis, not try to pick the market. I think the fact that we bought a little more this quarter, as the stock has come down a little bit, because as I've said in the past, we buy a little more when it goes down. And -- but we certainly -- I certainly feel comfortable about our future prospects as a Company. So don't expect giant changes in how we've done it in the past. Certainly, we've trended, each quarter this year, on an annualized basis, upward. And we're certainly comfortable at the current level.

Dan Binder: Great. Thanks.

Operator: Our next question comes from John Heinbockel from Guggenheim Securities.

John Heinbockel: So Richard, if you look at the three categories, or the three broad departments where we saw some margin improvement, so two things. Was there any common themes there, in terms of maybe COGS doing a better job on your cost or KS mix? So any commonality there? And then have we reached a point here, because I assume the KS mix will continue to get better, and how you buy that will continue to get better, where there should be an upward drift in growth, just secularly. Because there would be -- the elasticity of what you would choose to invest in doesn't merit, right, putting all of that back into the market, price-wise?

Richard Galanti (EVP and CFO):

I'd like to think that we were that smart. Overall, we try to improve margins a little, while lowering prices. I mean that sincerely. And we're going to give most of it back to the customer, and to our member. As you know, we're pretty stubborn and intent on maintaining, in a rising commodity standpoint, prices on certain fresh foods. So we've seen some impact there to the negative. I think you're right, though, as we continue to improve, increase penetration of KS, that helps a little.

Certainly, as we've had relative strength in departments over the last couple of years, like soft lines and domestics and housewares, and some of those items, we can improve that a little bit. And that's, of course, outside of the ancillary and other businesses, which, in some cases, work on higher margins as a starting point, be it pharmacy or hearing aid center, or optometry or whatever else. So but -- organics helps, in a small way.

I mentioned in the past, not only are organics, relative to their substitute, the non-organic same products, organics sell at a higher price point. But our view is, is that others, while it may be competitive, we actually can be -- we show a more competitive framework, and a little bit higher margin, than on the underlying non-organic items. So it's really, in our you view, a win-win for us, the challenge being getting more organic. And that's not just a challenge for us, of course, it's a challenge for everybody out there. So all those things help. I don't think we started the fiscal quarter and said, let's see how we can get an extra 10 or 15 or 20 basis points higher than year over year. But we're always trying to improve a little, as we know we have challenges elsewhere.

John Heinbockel: And do you think -- at least I've noticed this particularly, I think more in the soft lines. But do you think the quality of KS -- it seems to continue to get better, maybe at a faster pace even than it has in the recent past. Do you think that's fair? The quality's getting better, that's the investment, not price point so much?

Richard Galanti (EVP and CFO):

I think two things. Like on the soft lines side, like apparel and everything, we've -- over the last few years, we've made a bigger effort in that area. We took what sometimes would be a retail branded item, at $200 to $300 for a pair of slacks, that were $49.99. But when you go out and buy the same fabric, and make, hopefully, a very good quality item, and commit to 0.5 million or 1 million units of something, that helps. So we're always pushing the quality and the quantity and buying power of that. And that quality/value relationship continues to, I think, improve.

John Heinbockel: Okay. And then just lastly, I don't think you guys have done a whole lot of data mining, right, with your membership base. Do you see that -- does IT modernization allow you to do that? And then I'm wondering, when you think about sales -- comp sales by comparable member, I'm just curious. When you look, going forward, do you guys see a bigger opportunity to get -- and I'm not saying the most loyal members, maybe somebody a little bit below the top, to come in more frequently? And that's a fresh food driver? Or more of an opportunity to get product in -- more items in the basket per trip? When you think about sustainability of comps by somebody who's been a member for whatever, three, five, six years, where do you see the bigger opportunity?

Richard Galanti (EVP and CFO):

First and foremost, we've gone from doing virtually nothing to being a little more open minded about it. I think there's a lot of low hanging fruit that we haven't done. Certainly, there's more efforts in these areas, in our membership marketing team, on dot-com a little bit. But -- we don't do a lot with it, but we're doing a little more than we used to. We must get a call -- I must get a call a week from some analytics company that wants to film stuff, to do AB testing. Left or -- is the ketchup left or right of the mustard. We've done, I think, a better job on our multi-vendor mailer, in terms of that. But we have -- I think we have more opportunities than we've even touched the surface on. But I'm not suggesting that's going to be tomorrow afternoon.

Marketing has definitely been told to try some new things, and we have, and they generally work. I view that more as something, if things start to slow a little bit, we have some opportunities there. But we're first and foremost focused on just constantly driving quality and value on the products and services we sell. And that's -- we seem to have not figured out where the bottom of that is.

John Heinbockel: Okay. Thank you.

Operator: Our next question comes from Bob Drbul from Nomura Securities.

Bob Drbul: Hi, Richard. Good morning. I guess I just have a couple questions. I think last quarter, you had quantified the impact on the gas profit. I think you said it benefited by $0.01. I was wondering if you could give us that same metric this quarter? And the second question that I have is, I think, with some of the remodels that's are going on, could you just talk a little bit about category focus in the remodels? And your expectation on what the returns and the comp uplifts we might see?

Richard Galanti (EVP and CFO):

Yes. What was the first question? I lost it.

Bob Drbul: Gas profit impact on EPS.

Richard Galanti (EVP and CFO):

Yes, I think that's where there was not a big impact. It was a wash, year over year. It's more than a few cents, but not a heck of a lot. We really don't talk about it, other than directionally, which way it helped us. Certainly, I think four -- at least four of the last five fiscal quarters, on a year-over-year basis, it's been up -- yes, more outsize than normal up. And the second question?

Bob Drbul: Remodel. So like trends in remodels, what would be the expectation that you see? Category focuses, and how that might impact comp store sales, as we go through this?

Richard Galanti (EVP and CFO):

Sure. And keep in mind remodels, I think of traditional retail stores remodel, they're doing a whole new front, new flooring and new lighting fixtures. A lot of -- our remodels are everything. And we spend a lot of money on increasing refrigeration and frozen in the fresh foods area. That continues -- as somebody mentioned earlier, that continues to be a driver of our business. It's certainly something we're pretty good at. We constantly try to figure out what locations that we don't have, where we can put gas stations, although we're saturating that. There's certainly existing locations that are never going to have a gas station, but we still have a few left there. And we, of course, have added some gas stations in a few other countries beyond just the US and Canada. So there's little things like that.

There's typically half a dozen or so units a year where we're breaking out a wall, buying some extra land, perhaps adding 10,000 or 20,000 feet. Where it makes sense, and many times it makes sense economically, when there's some government incentives on solar. That's small dollar-wise, but I'm just throwing out some examples. So remodeling, for us, is just constantly -- sometimes improving and updating something, but a lot of times just adding some more stuff, more lineal feet of refrigeration is something that comes to mind, in a bigger way, over the last few years.

Bob Drbul: And then just one question on the ancillary businesses. Can you just talk a little about what's happening in the photo business, and trends in the quarter? And what the expectations are there?

Richard Galanti (EVP and CFO):

You probably have -- are processing less photos than you used to. It's actually about -- the business itself, profitability-wise, is about flat year over year. Actual photos processed is down. We enhanced the business on a few other things, with everything from canvas pictures to photo books to ink refill cartridges, toner cartridges. And -- but it's -- that's not a business that's going to come back tomorrow, either. It's -- of all the ancillary businesses, that's the one that's, it's big, it's profitable, it's not as profitable as it used to be. But it's -- and we'll continue to look at that space, and see what we want to do. But we still have it, and it's still -- we still try to figure out how to improve it.

Bob Drbul: Thank you, Richard.

Operator: Our next question comes from Meredith Adler from Barclays.

Meredith Adler: This is Meredith Adler. I was wondering if you could just talk a little bit about what happened with the store openings this year, which I think missed your expectations? I know some slipped into next year but were there any common themes in that? And when you look out, because you've got a nice number of openings for next year, do you think that there's any risk, based on what happened in FY15?

Richard Galanti (EVP and CFO):

Sure. There's going to always be risk. I think prior to the FY15, for the few years leading up to that, we actually got better on track of getting closer to what we think is going to actually open. We put -- this is our original budget. Everything that -- if everything generally goes right, and we've -- it's been green inked, if you will. It's been approved internally, based on whatever permits and zoning issues and whatever -- all the issues are out there, we think we have a decent chance of opening it. We're going to put it in there.

Recognizing, inevitably, there's always 5 or 8 of those units that are budgeted for months 11 and 12, if not a few more, of that fiscal year, maybe 10 units a year, in that last month or two. And inevitably, a few of those fall out. I think that we'll get closer than we did this year, relative to our budget. Generally speaking, it's not because we decided not to do a unit that we were going to do it. The only time that happens, or virtually every time that happens, it's something because something was -- became a big surprise. Doing additional drilling, we found something on the site that was a bigger issue. And that, by the way, is generally not our risk. Because when we do a site, it's for virtually all of them, nearly all of them, we have to feel comfortable we can be able to do it before we commit to it.

Meredith Adler: Okay. So there wasn't any -- (multiple speakers)

Richard Galanti (EVP and CFO):

I think we'll get closer.

Meredith Adler: And there wasn't any common theme to the ones that didn't open this year, or got delayed?

Richard Galanti (EVP and CFO):

No. It's -- every one's a unique story. But it's just typical delays: weather, zoning, other surprises that are unrelated to competition or anything else out there.

Meredith Adler: Okay. Great. Thank you.

Operator: Our next question comes from Michael Lasser from UBS.

Michael Lasser: Good morning, thanks a lot for taking my question. Can you give you us a little more detail on the traffic trends? Not only this quarter, but over the last maybe few years? Are you seeing more of the growth come from the middle tier of the membership base? Presumably the most frequent members are tapped out. They can no -- they cannot grow the number of times they're going to Costco . So is it more so coming from the mid-tier of the membership population, or is it more like the least attached members are getting a little bit more attached?

Richard Galanti (EVP and CFO):

Maybe people in membership and operations know a little more than I do here. I -- and maybe there's some more opportunity -- yes, overall, over time, shops go up. As people are making more each year, as they're having family, whatever those issues are. And so certainly, an older member, in terms of how long they've been a member, that increases over time. But it's a lot of things. It's the merchandising. It's the frequency drivers, like fresh foods and gas. It's that incremental shop, because somebody, all of a sudden, needs a maintenance prescription. They've gotten to the age where they're going to come in one extra time a year, because of their timing of their need for a cholesterol-reducing drug or whatever. So it's a lot of little things, plus a few of those things, notable things, like fresh foods and gas. It's also executive membership. It's also the co-branded card and rewards. It really is all of the above. I don't -- there's different reasons.

Clearly, when we have new members, whether it was new millennial members, or 20 years ago, new Gen whatever members, they buy less when they start, they buy more over time. I can't tell you what millennials are going to do, relative to their predecessor age groups overall, not just at Costco but overall buying. If they have smaller houses, and they drive a little less, and they buy fewer sofas, that is not good for anybody. But at the end of the day, we think we're getting our share.

Michael Lasser: Okay. And my follow-up question is, how have you noticed, or how have you observed your membership population respond to different types of promotions? And when I say promotions, I'm talking about price investments, rewards through your card, maybe new merchandise offers. Can you give us what's been most -- a sense of what's been most impactful? And how it's -- how the response has been? Has it been to drive up basket? Has it been to allow you to sign up more members? Thank you so much.

Richard Galanti (EVP and CFO):

First of all, we're not going to share all the specifics. But at the end of the day, it's a little bit of all of the above. We work every day to try to improve the value proposition to the member. We work every day to try to up-size an item where it makes sense, because we do want more things and more dollars in that basket. We -- maybe something like the multi-vendor mailer, with the couponing. That grew dramatically from what was originally a six- or eight-week summer item, summer couponing booklet, to 11 or so times a year, for three-plus weeks each. And over time, we and our vendors figure out what works best, and what starts to slow down. So those things keep getting tweaked.

So again, there's -- we focus on trying to improve the value. If we can sell you a bigger pack size at a greater value, we're going to do that, and I think that's a catch, too. We don't just want to increase the size of something 50%, and sell it at the same price per ounce or price per number of units. We only want to raise it -- for the most part, we try to raise it only the quantity, when we can lower the price per unit to the member. And that serves us well, and it serves them well. So that's our religion.

Michael Lasser: Sure. I'm thinking more about the card. Does that have as much influence in the member's purchase decision or frequency as pricing or coupons, for example?

Richard Galanti (EVP and CFO):

I don't know if one has more than the other. We know that executive members shop a lot -- take a group of 100,000 members that are similar, in terms of shopping patterns and age groups and tenure as a member, and they're both growing. Both of those groups are growing at roughly the same rate each year. Get half of them to convert to executive member, and you see a dramatic change in their buying habits. But that's no change that we've seen over the years. That -- I think what surprises me personally is the continued (technical difficulty) penetration of that area. And maybe we've gotten a little better, in store, of doing that. Clearly, loyalty programs work, whether it's our executive member program or a reward-based co-branded credit card. And one of the things that's long-term exciting for us is, we feel that we can continue, even on our co-brand card, continue to improve the value proposition to our member, which hopefully gets them in here more often. But that's what we do every day.

Michael Lasser: Sure. All right. Good luck with the upcoming year. Thank you so much.

Richard Galanti (EVP and CFO):

Thank you.

Operator: Our next question comes from Peter Benedict from Robert Baird.

Peter Benedict: Hey, Richard, thanks for taking the question. A couple here. First of all, can you talk about the new member sign-up trends in the fourth quarter? I didn't hear -- if you did mention that, I apologize. I know they were down slightly in the third quarter.

Richard Galanti (EVP and CFO):

They were actually up in the fourth quarter, year over year. A combination of decent member sign-ups at existing warehouses, probably a few more international units in the quarter, on a comparable year-over-year basis in the quarter. I think we were up a little over 2 million members in the quarter, from a year ago, in terms of new sign-ups.

Peter Benedict: Okay. Great. And then, you mentioned, when you gave the regional color, you said that Texas was good. But can you talk about maybe trends in some of the specific energy markets, thinking like Houston, maybe somewhere up in Alberta? Like have you seen any kind of moderation in traffic or ticket, or what have you?

Richard Galanti (EVP and CFO):

You know, I just don't have that amount of granularity in front of me.

Peter Benedict: Okay. And then the thought process behind repatriating cash from Canada, why now? And then, you've got a $1.2 billion note that comes due in December. Is -- are your thoughts here to refinance that or pay it off?

Richard Galanti (EVP and CFO):

At this point, we'll probably pay it off. Part of the repatriation is, Canada is a very profitable country. So it's -- we've built up cash balances. At some point, we determined -- on an ongoing basis, we will determine whether we feel it needs to be permanently invested up there or not. And at such time, we'll make that decision. I think we've done that twice. About a year ago, we brought back a little over $1 billion. And in this case, it was favorable from -- a small favorable from a tax perspective. A year ago, I think it was the third or fourth quarter a year ago, it was slightly unfavorable. But again, we determined -- but small. We determined it was the right time to bring it back, from a reinvestment standpoint.

Peter Benedict: Okay. Fair enough. And then last question, just on CapEx, $2.8 billion to $3 billion this year. It's almost double what you did maybe a few years ago. I understand you've got some of the investments you're doing, the higher store growth. Is that a level you think is one that we should assume holds for several years, assuming you can open 30-plus stores per year? Or are some of the investments you're doing in IT and systems and distribution, do those taper off a bit, maybe in the out years? Just how are you thinking about that?

Richard Galanti (EVP and CFO):

I hope IT tapers off a little, but it's -- that's not the biggest piece of it. I think -- I'm certainly comfortable with saying it's going to be in $2.5 billion to $3 billion range, is the $2.8 billion to $3 billion this year. [102] -- likely be [102] higher than the following year. Maybe, I don't see that $2.8 billion to $3 billion going to $3.5 billion next year. So yes, something in the high $2 billions is probably a good guesstimate for the next few years.

Peter Benedict: Yes. Okay, that makes sense. Thank you.

Richard Galanti (EVP and CFO):

Thank you.

Operator: Our next question comes from Scott Mushkin from Wolfe Research.

Scott Mushkin: Thanks for taking the question. Actually had some follow-ups on some of the questions that were already been asked, but I wanted to get some clarity. So I think Michael Lasser was asking about the Visa card. And I guess real specifically, do you anticipate that, that card will actually drive membership growth, Richard?

Richard Galanti (EVP and CFO):

When we get there, we'll let you know.

Scott Mushkin: Okay. And then, following up a little bit on John Heinbockel, and he's the technology. When you're looking at your executive members, do you guys have clarity to the data? Say, okay, how many -- are these executive members using our ancillary services? What are they using? And what the penetration rates are?

Richard Galanti (EVP and CFO):

Yes, absolutely. But we're not going to share with you what those are. Each ancillary business is a little different. Some of them take a decade to really get some good footing. But they're all great values, and yet another reason why somebody wants to be a member. And we'll keep improving those values. So those are -- whether it's KS or organic or commodities, or these items, those are all things, I think, that gives us a good competitive position.

Scott Mushkin: And do you think there's an opportunity to drive additional ancillary business growth with your core members?

Richard Galanti (EVP and CFO):

Absolutely. (multiple speakers) Absolutely.

Scott Mushkin: Okay, then the --

Richard Galanti (EVP and CFO):

I would recommend that you try Costco Travel. You'll be amazed.

Scott Mushkin: I'm looking right now at a Costco car buying program, so I hear that's wonderful, as well.

Richard Galanti (EVP and CFO):

That, as well. I think we're approaching 0.5 million new cars a year on that, and there's a reason. We use our buying power to get our members a great savings on cars.

Scott Mushkin: And when you think about getting a little bit more involved in technology, and that relationship with your customers, is one area that you would think could be a lever that could be thrown?

Richard Galanti (EVP and CFO):

I'm sorry, say that again?

Scott Mushkin: When you're looking at data mining, knowing your customers a little bit better, marketing a little bit more aggressively, I think you [mentioned] at the beginning, is this an area that will get a focus, do you think?

Richard Galanti (EVP and CFO):

At some point. And we're a little self deprecating when we talk about that. At the end of the day, there's a lot of opportunities to do a lot of that stuff. We look at it, the 80/20 rule. We're doing a little of it, which we're getting some benefits. There will be plenty of opportunities to do some of that in the future. But we -- our main focus is on driving value. And a lot of those other things take care of themselves. And certainly, Craig Jelinek, as our CEO, has told people in e-commerce, people in membership marketing, try some things. And they're trying some things. And we'll keep going in that direction.

Scott Mushkin: Perfect. And I had just one last follow-up. This is when Bob was talking about the remodels. I'm trying to understand, our local Costco is under remodel in the fresh department. And if you look at 2016 and 2017, is that the focus of the remodels? Are you expecting to do more of them? And is it focused on fresh? It seemed like that's where the focus is; I just wanted to get clarity. And is it going up, year over year?

Richard Galanti (EVP and CFO):

I think, as a general rule, it's been going up. But it's up. It's a big number. And I don't know if it keeps going up from there. I know the one you across the street here, we, again, added 10,000 or 15,000 feet. We expanded greatly the walk-in coolers for customers, in produce and dairy. When you're doing, in some of these units $200 million, $250 million, $300 million, you can drive some true incremental good sales by not only expanding the -- everything, in terms of the traffic patterns and the ingress and egress in and outside of the warehouse, but adding some of these things like refrigeration, fresh foods. And it will still continue to be a big number.

Scott Mushkin: All right. So you're doing more fresh remodels, fresh drives traffic. Is the focus in that fresh area on organics, or just general? Or is it related towards organics? Do you know?

Richard Galanti (EVP and CFO):

I think in terms of CapEx-related, it's everything. Organics is just a piece of that.

Scott Mushkin: All right. Perfect. Thank you so much. Really enjoyed the answers. Thanks.

Operator: Our next question comes from Greg Melich from Evercore ISI.

Greg Melich: Thanks. You've gone over an hour, and I still have a couple questions. So wanted to follow up on gas. What was the average gas price in the quarter versus last? And if you could give us the gallons, as well, that would be great.

Richard Galanti (EVP and CFO):

The average price in Q4 was $3.65 a year ago, and $2.88 this current fourth quarter. So down 21.2%.

Greg Melich: Great. And if that's the case, I guess going back to gas profitability, understanding it's been a tailwind. I guess it's that incremental drop, even from last quarter, that's really allowed the profitability to boost up again. Is that a -- are we thinking about that right?

Richard Galanti (EVP and CFO):

Actually, the price was -- from a quarter ago, the price was up about $0.20 a gallon. But I think there's a little bit of a new normal. It's not just how it is year over year. It's, when it's low, it's better from a profitability standpoint, and it's relative to competition. Gas Buddy has continued to say that we're the lowest price out there nationally, and I think we're still pretty good at being very competitive. We get a lot of good kudos for that.

Greg Melich: So basically, you can keep your competitive advantage, but the penny profit might be better than it used to be, the way the market is.

Richard Galanti (EVP and CFO):

Yes, I think when prices are low, we make more than we used to on average, per gallon or per gas station, and that's good.

Greg Melich: And then the second question was going back to membership fee income. I think you said it was 6%, if you exclude FX?

Richard Galanti (EVP and CFO):

Yes.

Greg Melich: I believe that's 100 or maybe 200 bps below the trend the last year or two. Is that just fewer openings last year? Or I think last quarter, you mentioned sign-ups per club was actually negative, but it was a comparison issue. Could you just help us understand?

Richard Galanti (EVP and CFO):

I think overall, it's just fine. There's a little bit, in Canada, of the auto-renewal issue, when we switch over. And we'll see that again a year hence, over the next year, starting next year. That's a small piece of it. I don't think, beyond that, there's a whole lot there, in that regard. There's always going to be the timing. Because when membership fee dollar increases, or we use deferred accounting for it, and so that makes it a little more squishy number. But overall, the number was in line with what we felt was pretty good.

Greg Melich: And with the auto renewals -- I'll sneak a third one in -- if I remember correctly, AmEx is roughly 40% of the tender in the stores. So to think of the magnitude that had in Canada when you did the changeover, what was AmEx there?

Richard Galanti (EVP and CFO):

There's one big difference. In Canada, the portfolio was not purchased. While I can't guarantee it will be purchased, the contract states that it should be, and we're working towards that -- or Citi and AmEx are working towards that end. That's a different scenario, in terms of auto renewal. Up there, you basically have to re-sign people up. They have to apply for credit. They get authorized. They have to re-sign up -- opt in for auto renewal. I don't expect that to be an issue in the US.

Greg Melich: Got it.

Richard Galanti (EVP and CFO):

At this point.

Greg Melich: And the tender there is roughly the same as here, that 40%?

Richard Galanti (EVP and CFO):

I think it was a little less. But mind you, the market share of our provider up there historically had a lower market share there, relative to Canada, than they do in the US. They have a stronger market share down here.

Greg Melich: Okay, got it. Thank you.

Richard Galanti (EVP and CFO):

Why don't we take one more question.

Operator: Our final question comes from Matthew Fassler from Goldman Sachs .

Matthew Fassler: Thank you so much for keeping the flame burning just for another moment. First question relates to Spain. And just curious, on your learnings from your first Spain opening, and how you expect your Continental European stores to differ from your other international markets, based on what you saw from that first unit?

Richard Galanti (EVP and CFO):

Like any first unit, with maybe the exception of Australia, which was off the charts high to start with, you learn a lot. You learn what sells and doesn't sell. I think, if I recall from when we first opened in Seville 1.5 years, 2 years ago, we had less -- we had stronger nonfood than we would have expected, and not as strong fresh food. Usually, in a new market, you've got stronger fresh food. Given our great success in countries like Korea and Taiwan and Japan, we have to remind ourselves that Korea and Taiwan, they were not very good for several years. You start off with slower sales in most countries, other than Australia, when you first enter -- when we first entered a market. And that was consistent. Probably the worst economy we started was in Spain.

But we're seeing some traction. Membership sign-ups are just fine, and membership renewals have been just fine. But it's -- one data point does not a story make here. Madrid certainly is a much bigger market than Seville. And we've got, again, one unit coming next month, and a second one in and around Madrid coming, I believe, next spring. Certainly sometime in the middle of the calendar year. So that will be more telling, in our view, than anything we've seen so far.

Matthew Fassler: Great.

Richard Galanti (EVP and CFO):

We continue to be very confident that we've got a good model, and that it works. And we're patient, as well.

Matthew Fassler: A quick second question. On the online and e-commerce piece, Instacart, I know, is a particularly prominent partnership among the ones that you've got. An it's a concept that from a -- in terms of the number of retailers it's doing business with, and how long that's hung in, seems to be gaining some traction. Any sense as to how that relationship has evolved? In particular, how the economics look for you, relative to some of the alternatives?

Richard Galanti (EVP and CFO):

Again, we're not going to disclose any specifics. We have a good working relationship with Instacart, with -- certainly, with Google Shopping Express , as well. And Instacart is in more cities, and anybody you know out there that wants to buy from us, you call us.

Matthew Fassler: Fair enough. And then finally, I think Greg -- one element of Greg's questions might not have gotten answered was gallon comps. You talked a bit about the gas prices. But I remember, when gas prices first started coming under pressure, gallon comps surged into double digits. Are you still seeing that, with prices down here today?

Richard Galanti (EVP and CFO):

I'm not sure if it's double digits, but it's certainly positive. And we generally haven't given that out. Sometimes, in a moment of weakness, I share it with you guys. But the comps have continued to go in the right direction, in terms of gallons.

Matthew Fassler: Thank you so much.

Richard Galanti (EVP and CFO):

Thank you everyone. Have a good day.