

# Costco (COST-US)

## Sector: Consumer Staples

### Company Overview

Costco (COST) is a leading global retailer with a member-based model, offering low prices on a limited set of high-quality, bulk-sized SKUs. In F2022 (ended in August) Costco had 838 warehouses in operation (578 in U.S. & Puerto Rico, 107 in Canada, 40 in Mexico, 36 in Europe, 31 in Japan, 17 in Korea, 14 in Taiwan, 13 in Australia, and 2 in China).

### Suitability/Ethical Considerations

According to MSCI, Costco's business ethics practices lead those of global peers. It has a detailed anti-corruption policy, backed by staff training and audits on ethics standards. In FY 2022, Costco derived 33% of its revenue from private label brand, Kirkland, for which its reliance on third-party manufacturers is high; this may expose it to risks tied to potential supply chain labor violations. The company also has a whistleblower policy that protects reporting individuals from retaliation. Costco handles significant volumes of customer data and primarily operates in the US, where data protection laws are stringent. New evidence indicates improvements in its data protection measures, such as conducting vulnerability tests and strengthening information security systems. In fiscal 2020, Costco published its multi-year 10-Point Climate Action Plan which aligns with the UN's SDGs and the company met and exceeded its targets for fiscal 2021.

### Investment Thesis

BMO Capital Markets (BMO CM) believes that COST's advantaged business model (low GM%, higher-margin online business, membership fee income stream), consistent execution, increasing connection with its loyal membership base (solid renewal rates, increasing Executive penetration, and increasing digital connection), and potential catalysts make it deserving of its premium valuation, a rarity among retail/consumer staples.

### Recent Developments

COST's F2Q24 was strong, supported by continued membership growth & strength in renewal rates. EPS of \$3.92 was ~9% ahead of Consensus driven by a beat on SG&A dollars and higher interest income, and a lower-than-expected tax rate. While BMO CM expects no shift to Costco's overall strategy and discipline on extreme value with leadership changes at Costco, Gary Millerchip, who took over as CFO on March 15, may bring a unique perspective for Costco on: personalization/data, advertising & payments.

### Price Target & Methodology

BMO CM's \$800 target price is based on 45-46x 2025E EPS.

### Key Risks

1) The consumer tends to limit spending on higher margin and more discretionary product categories during times of belt tightening; 2) rising product cost inflation and increased competitive pricing could adversely impact merchandise margins; 3) SG&A leverage is primarily predicated on top-line growth; if comps slow, EPS would likely be disproportionately impacted; and 4) deterioration in membership renewal rates and/or new member sign-ups would impact near- and long-term earnings potential.

Costco Wholesale Corporation			
BMO CM Rating	Outperform	Target Price	800.00
Current Price	732.63	Dividend	3.84
52-Week High	787.08	Yield	2.67%
52-Week Low	476.75	BVPS	56.59
Market Cap (\$M)	324,924	P/ BV	12.9x
FYE (MM/ DD) 9/ 3	2023A	2024E	2025E
EPS	14.76	16.45	17.91
P/ E	49.6x	44.5x	40.9x
EPS Growth	-	11.5%	8.8%

