



SHOPPING

Store Wars

Sam's Club wants you—and so does Costco, as they battle to win big-spending small-business customers.

By P.B. Gray

Ted Werth loves a bargain—and that's understandable. The 43-year-old engineer has four small children to feed and a fledgling computer-servicing business to tend in Bedford, Mass. So twice a month he spends a couple of hours grazing at his local branch of the Costco discount-warehouse chain. "I get copy paper, some steaks, eggs, a few breakfast cereals, maybe a new printer or a phone for the business," he says. His monthly tab for such practicalities: \$400—not including the occasionally indulged whim. "I went to get toilet paper and came home with a trampoline," he admits. "It was only a couple of hundred bucks until my wife made me go back and get the safety netting ... but hey, the kids just loved it."

Werth and big spenders like him are the prize in a battle heating up between warehouse giants Costco and Sam's Club, a division of Wal-Mart Stores. The two are fighting for supremacy in the lucrative, growing discount-warehouse market, whose primary customer is the well-to-do small-business owner. What does that mean for those who regularly prowl their concrete aisles? You're going to reap the spoils of war: lower prices and a host of new services like payroll processing and benefits management.

Miles of Aisles

How the two warehouse mammoths stack up.

Costco		Sam's Club
420	Number of stores	530
\$100	Average transaction	\$60
Nautica	Top brands	Ralph Lauren
Sony		Polo
Titleist		Dockers
Hallmark		Cuisinart
		Waterford
\$41.7 billion	Revenues (fiscal 2003)	\$31.7 billion

Sam's Club launched the first salvo last spring, a few months after a new management team took over. The 530-store chain lowered prices on commodities such as ground beef, prescription drugs, printers, and phones. Costco fired back with price cuts at many of its 420 stores. But it is also holding firm on its strategy of appealing to small-business customers not only with low prices but also with a broader selection of luxury items—from trampolines to fine wines—than Sam's offers. Both sides have already been bruised

in the brawl. In August, Costco said that profits for fiscal 2003 would be flat, at about \$700 million, though year-end sales were up 10%, to \$41.7 billion. Sam's posted sales of \$16.4 billion for the six months ended July 31, up 7.5% from the same period last year. Operating profits rose just 4.7%, to \$513 million. (A smaller rival, BJ's Wholesale Club, based in Natick, Mass., caters more to the general consumer.)

While both warehouse giants were founded in 1983, Sam's has long been a disappointment for its corporate parent: It has never been as successful or innovative as Costco. In fact, Costco is one of the few businesses that can say they have beaten Wal-Mart in a corner of the retail game. Costco outsells Sam's with fewer stores and fewer members: 19.7 million vs. 46 million. (Membership fees typically run \$45 a year.) Analysts estimate that Costco's sales per warehouse—a crucial barometer in this sector—are \$112 million, compared with Sam's \$60 million.

Still, Sam's is growing faster. This fiscal year it will open at least 30 stores, while Costco christens 26. To lead the charge, Wal-Mart plucked Kevin Turner, 37, who started his career at the company as a cashier in Ada, Okla. Turner, who took over as president in August 2002, declined FSB's requests for an interview. But he must know he is sitting in a spring-loaded seat: He is the company's sixth president since 1990. That revolving door is a result of top executives' "poor performance, and their inability to overcome difficult challenges," says Michael G. Clayman, editor of Warehouse Club Focus, an industry newsletter.

Both Sam's and Costco are after what they consider to be the most desirable demographic: you. Small-business owners tend to be wealthier than the average American, and most are homeowners with room there, and at the office, to store items bought in bulk. "We've spent 20 years catering to the upscale customer," says Richard Galanti, Costco's chief financial officer. "We know exactly what they want." Sam's vows to get to know them better. Turner recently decreed that store managers should be on the floor every day, greeting customers and asking what more they can do to help their businesses, according to Jolanda Stewart, a spokesperson for Sam's Club, which is headquartered with its parent in tiny Bentonville, Ark. After convenience-store owners lamented the disappearance of small brown paper bags from Sam's shelves, store managers alerted headquarters; the bags are now back.

In recent months Sam's has added several small-business services as well. For a fee Sam's will take over members' payroll processing and benefits management. "We can be your human resources department," says Stewart. But Costco has been offering such services for years. It's now busy turning itself into a bank and a telephone company; Costco has begun offering small-business loans and lines of credit as well as rock-bottom rates on conference calls. (Frequent users pay 5 cents a minute.)

Although warehouse shoppers want to save pennies on the basics, they'll splurge on indulgences. Costco's managers were the first to hit on that notion. At its wine and jewelry departments, shoppers can pick up a \$299 Chateau Mouton Rothschild Bordeaux or a ten-carat diamond ring for \$28,000. Costco won't sell a pallet of those rocks, but dangling them in front of its customers is important. Why? Even in a warehouse, retail is show biz. "We work hard to create a treasure-hunt atmosphere," says Costco's Galanti.

That's one reason its members can sound more like recreational shoppers than cheapskates. "I'm the Costco queen," says Sheila Albrecht, owner of an event-planning business in Bedford, Mass., whose annual tab at the store runs about \$30,000. Albrecht shops for her business, her household, and her husband's software company. "I outfitted my home and my husband's office at Costco: furniture, carpets, lamps, faucets, mirrors, bunk beds for the kids, artwork—everything," she says. Sam's carries jewels and wines as well, but its stock is considerably less expensive. The chain recently introduced a new line of high-end diamonds. Top price: \$3,000.

Still, no one at Costco is ignoring the threat posed by a newly energized Sam's Club. Costco dispatches a flock of comparison shoppers every day, keeping tabs on the latest markdowns and matching them quickly. That's a game at which Wal-Mart has traditionally excelled—and one Costco will have to play at a higher level. Both giants, it seems, need to become as nimble and competitive as the small-business owners they're trying to lure.

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