

Private Label

Private label merchandise enables Costco to generate higher gross margins while still offering quality and value. Costco's private label program primarily offers one brand, Kirkland Signature, while BJ's private label program includes 12 brands and Sam's private label program includes three brands. This chapter includes: private label strategy, data overview, competing with a private label SKU, Costco's program and pricing analysis. The data in this chapter was gathered in January, 2010.

Private Label Strategies

Warehouse clubs offer premium private label products that meet or exceed the quality standards of the competing national brand. Private label purchasing is done at the corporate level with buyers following nine strategies:

1. **Gross Margin** – Private label products should exceed traditional club gross margins of 8% to 12%.
2. **Savings** – Private label products should yield a 20% savings compared to the competing nationally brand.
3. **Quality** – Private label products should consistently exceed the standards of the competing national brand.
4. **Lack of Competition** – Private label products are generally developed for a category without a strong national brand.
5. **Item not Category** – Private label products are generally chosen based on a potential item's unit or dollar volume.
6. **One Supplier** – By selecting one manufacturer for a particular product, the clubs are able to negotiate the lowest possible cost by committing all their volume to that one manufacturer.
7. **Advertising and Marketing** – Advertising costs are kept to a minimum and items are promoted through product demonstrations, club magazines and overall private label brand acceptance.
8. **Merchandising** – Prime floor space is more common for private label items, increasing exposure.
9. **Negotiating Leverage** - Private label programs assist the clubs in negotiating the best possible price from competing branded manufacturers. In the January, 2001 issue of *The Costco Connection*, Dick DiCerchio, Costco's senior executive vice president and chief operating officer, said, "Some national brands weren't giving anyone a break [on price]. We needed to keep them honest, and that's what a quality private label can accomplish if done correctly."

Data Overview

The two charts in this section provide an overview of the private label programs at each club. The chart below on the left shows private label SKU development over the past five calendar years. The data is through January, 2010. The chart includes the total number of SKUs, the total number of private label items and the number of private label items in each category. The percentage next to the yearly private label total represents the ratio of private label items to overall SKUs. The column labeled key brands shows the number of key private label brands offered by each club. Costco's percentage of private label merchandise at 13% is the highest among the three clubs with Sam's at 10% and BJ's at 9%. However, in terms of total number of private label SKUs, BJ's leads the industry with 610 items followed by Sam's Club with 524 SKUs and Costco with 514 products.

Private Label	Total SKUs	Private Label SKUs	Key Brands	Categories												
				Apparel	Alcohol	Auto	Candy, Snacks	Dry Grocery	Perishable	Seasonal	Bed, Bath	Hard Goods	HBA, Baby	Pet	Sundries	
BJ's																
2006	6,896	900	13%	13	45	0	7	42	106	220	44	24	131	144	20	117
2007	7,167	904	13%	19	58	0	7	42	122	286	44	28	89	128	20	80
2008	6,792	688	10%	14	38	0	5	31	69	213	64	18	74	89	19	68
2009	6,621	610	9%	12	29	0	6	26	63	195	59	30	47	85	12	58
2010	6,981	610	9%	12	24	0	5	26	65	193	51	40	38	97	11	60
Costco																
2006	4,108	411	10%	1	15	3	38	16	37	141	30	12	14	69	7	29
2007	4,479	474	11%	1	20	9	41	19	43	149	40	2	32	85	8	26
2008	4,420	527	12%	1	20	10	49	21	58	163	35	21	32	85	8	25
2009	4,091	502	12%	1	23	8	33	22	61	172	26	20	25	76	8	28
2010	4,016	514	13%	1	14	7	33	23	67	172	39	19	17	87	8	28
Sam's Club																
2006	4,960	445	9%	3	78	3	4	8	47	101	23	0	26	103	11	41
2007	5,157	376	7%	3	79	0	3	6	41	92	13	0	21	74	11	36
2008	5,379	377	7%	3	5	0	4	5	47	115	14	0	38	95	11	43
2009	4,980	423	8%	3	4	0	2	9	53	140	18	2	66	75	8	46
2010	5,266	524	10%	3	4	0	4	6	45	159	27	21	84	92	8	24

The chart on the next page provides estimated sales for an average private label and branded SKU. The sales data is from calendar year 2009 and does not include ancillary businesses. A branded item at Costco generates \$515 weekly per club compared to a private label item which generates \$752 weekly per club. A branded item at BJ's generates \$135 weekly per club compared to a private label item which generates \$159 weekly per club and a branded item at Sam's generates \$251 weekly per club compared to a private label item which generates \$321 weekly per club.

Competing Against Club Private Label Items

Club manufacturers selling a branded product that competes with an existing private label item should not feel pessimistic about their prospects. Branded manufacturers have a couple of choices when putting together a strategy for competing against club private label products.

The branded vendor could choose to aggressively lower the club's cost so that the branded product offers a better value than the private label item. Another option is to include additional product features that provide a better value compared to the private label item. In both cases, if the argument is sound, the club buyer will have to consider deleting the private label item in favor of the branded item.

Club buyers are trained to evaluate each item on its own individual volume and gross margin merits. If an item does not meet certain thresholds, it will be deleted. It does not matter if that deleted item is a private label item or a branded item. Among the principles that club buyers follow, two relate to these examples.

1. Club buyers follow a strategy of an intelligent loss of sales. The clubs will only stock items that offer significant savings to their members. If a manufacturer prices an item too high or requires that the item be sold at the manufacturer's suggested retail price, a club will not stock the item. The clubs believe that if they cannot show a value to their members on a product, then that particular item should not be stocked.
2. Club buyers make item buying decisions and not category buying decisions. When buying for a category, as grocery store buyers do, the goal is to provide a broad selection. When item buying, as club buyers do, an item must meet certain sales and value thresholds. If an item does not meet those criteria, the club will not stock it. Since the clubs only stock a limited number of SKUs, the club buyer's goal is to maximize sales per square foot.

To compete against Costco and Sam's, BJ's will rely on high-end private label brands such as Wellesley Farms, Rozzano and Earth's Pride. To compete against supermarkets, BJ's will concentrate on its consumable brand, Berkley & Jensen. The chart above on the right details BJ's current private label assortment.

2009 Calendar Year		BJ's	Costco	Sam's
Total	AVG SKU 2 Years	6,801	4,053	5,180
	AVG Location 2 Years	183	558	733
	Yearly Product Sales less Ancillary (million)	\$8,862	\$64,047	\$50,878
	Yearly Sales per SKU	\$1,303,044	\$15,802,369	\$9,822,008
	Yearly Sales per SKU per Location	\$7,120	\$26,320	\$13,400
Branded	Weekly Sales per SKU per Location	\$137	\$545	\$258
	SKU	6,191	3,539	4,656
	Percent of Sales	89.6%	82.5%	87.4%
	Yearly Sales (million)	\$7,940	\$52,839	\$44,467
	Yearly Sales per SKU	\$1,282,564	\$14,930,425	\$9,550,552
Private Label	Weekly Sales per SKU per Location	\$7,009	\$26,757	\$13,029
	SKU	610	514	524
	Percent of Sales	10.4%	19.5%	12.6%
	Yearly Sales (million)	\$922	\$11,208	\$6,411
	Yearly Sales per SKU	\$1,510,898	\$21,805,885	\$12,234,023
	Yearly Sales per SKU per Location	\$8,256	\$39,079	\$16,690
	Weekly Sales per SKU per Location	\$159	\$752	\$321

WCF Research, Estimates.

Kirkland Signature



Costco – Kirkland Signature Macaroni & Cheese

In 1995, Costco introduced its Kirkland Signature private label brand. Costco's private label strategy initially focused on premium SKUs in high volume, "consumer need" categories. As members began to recognize the quality of the Kirkland Signature brand, Costco expanded its selection to categories that are not traditionally associated with private label such as baby formula and wine (see picture on the left of Kirkland Signature macaroni and cheese).

Costco's private label merchandise represents approximately 19.5% of overall sales with food and sundry private label penetration approaching 23%. Currently, Costco stocks 514 private label items (see chart below). In the October, 2009 issue of *The Costco Connection*, Jim Sinegal, Costco's chief executive officer, said, "We will always be known for name brands such as Michelin, Sony and Crest but we will continue to augment our product offerings with our own Kirkland Signature items."

In November, 2009, Costco held a financial analyst meeting in New York. The company said that over the next few years, it is going to aggressively expand its Kirkland Signature private label assortment. Overall, private label sales penetration could reach 27% in fiscal 2010 (ending August, 2010) and 37% in fiscal 2012 (ending August, 2012).

By category, food and sundries private label sales penetration could reach 30% in fiscal 2010 and 40% in fiscal 2012. General merchandise private label sales penetration could reach 10% in fiscal 2010 and 15% in fiscal 2012. Health and beauty aids private label sales penetration could reach 20% in fiscal 2010 and 30% in fiscal 2012. A clear focus of Costco's Kirkland Signature expansion plans is to convert all its fresh food products (meat, seafood, bakery and produce) to private label by fiscal 2012.

The following are assorted facts and information about Costco's private label program:

Costco	2009		2010	
	KS	Others	KS	Others
Alcohol	8	0	7	0
Apparel	23	0	14	0
Automotive	33	0	33	0
Bed and Bath	20	0	19	0
Candy, Snacks	22	0	22	1
Dry Grocery	61	0	67	0
Hard Goods	16	9	11	6
HBA, Baby	76	0	79	8
Perishable	172	0	172	0
Pet	8	0	8	0
Seasonal	15	11	17	22
Sundries	28	0	28	0
Total	482	20	477	37
Overall Total	502		514	

WCF Research - 2009, 2010

Quality – In the October, 2009 issue of *The Costco Connection*, DiCerchio said, “The working rule followed by Costco buyers is that all Kirkland Signature products must be equal to or better than the national brands, and must offer a savings to our members. We know we have met this goal when consumer groups consistently rate us highly compared to national brands.” For example, the December, 2009 issue of *Consumer Reports* ranked AA alkaline batteries and Costco’s Kirkland Signature alkaline SKU received the only “Best Buy” rating. The ratings were based on cost per pair of batteries and the cost per 50 digital camera pictures. Other alkaline batteries in the test were Panasonic, Duracell, Rayovac and Energizer.

Co-Branding - One of the more important strategies for the clubs in developing a strong private label program is member acceptance of the product. One way that Costco (as well as BJ’s and Sam’s) achieves this is to co-brand its Kirkland Signature label with existing brand-name products. By associating the Kirkland Signature name with an existing well-known consumer brand name, members associate the quality of the branded company to Costco and Kirkland Signature. This can only help to increase members’ positive perception of new and existing Kirkland Signature products.

In the April, 2004 issue of *Private Label Buyer*, Tim Rose, Costco’s senior vice president of merchandising for foods and sundries, said, “Co-branding immediately brings recognition to the product when you are introducing a new Kirkland Signature item with a name brand on it that has been in the marketplace for 40 or 50 years. That brings a lot of loyalty, and brings something important to the table. People see two great brands.”

Costco has placed its Kirkland Signature label on the following products: organic coffee with Starbucks, jelly beans with Jelly Belly, chicken nuggets and animal crackers with Disney, bacon strips with Hormel, grape juice with Newman’s Own and mattresses with Stearns and Foster.

Packaging – Rose said, “Every Kirkland Signature product goes through an exhaustive product development process that can put the vendor through the wringer.” An important step in that process is packaging. In the June, 2006 issue of *The Costco Connection*, JoLynn Sanchez, packaging graphics manager at the time at Costco, said, “Packaging is the first sale. Once a member puts the item in their cart, it becomes a traveling billboard for the product, for Kirkland Signature and Costco. It’s still working in the cart, in the parking lot and at home.”

Brand Consistency – One of Costco’s beliefs in growing its private label program is to focus on one brand, Kirkland Signature, instead of introducing numerous private label names in different categories. In the April, 2004 issue of *Private Label Buyer*, Bill Hansen, vice president and general merchandise manager of Costco’s Midwest division, said, “The reason why Kirkland Signature is on every item is because we want to keep that consistency throughout the building. We’ve been able to ensure we’re delivering quality, and over the years, Kirkland Signature has become a brand ... Jim Sinegal feels that instead of fragmenting private label, we should use it as one label.”

Wine – Costco’s Kirkland Signature wine program is constantly changing. Kirkland Signature wines are special blends produced exclusively for Costco or existing blends from respected vintners. Costco purchases approximately 2,000 cases of each wine. When a specific wine is sold out, it will not return. In the October, 2006 issue of *The Costco Connection*, Annette Alvarez-Peters, Costco’s national director of wine, spirits and beer, said, “I no longer call this a program but a series since we are offering so many collectible wines. All wines selected for the series must represent true expressions of their origins, embody the best of a wine region, come from leading varietals and exceed member expectations.”

Hot Dogs – In 2009, in many food court locations nationally, Costco replaced its kosher hot dog with a new Kirkland Signature private label quarter-pound all-beef hot dog. The primary reason for the switch is due to product supply. In 2008, Costco sold more than 82 million quarter-pound hot dogs. Annual hot dog sales will reach approximately 90 million in 2009 and will continue to grow annually. The problem is the availability of kosher raw materials. Since the mid-1980s, Costco’s food court operation relied on two kosher hot dog suppliers. However, in 2008, one of the original kosher hot dog suppliers exited the kosher meat business and the largest kosher raw ingredient supplier was closed down.

In 2007, Costco anticipated long term supply problems and began working on its Kirkland Signature hot dog. The result is a 100% all beef hot dog make with USDA choice meat or better. The new hot dogs are 10% heavier and longer than the older kosher-style. The private label hot dog is made without fillers, binders, phosphates, corn syrup and artificial colors and flavors.

Tuna – According to the March, 2009 edition of *The Costco Connection*, a recent trend in the tuna industry is that vendors are reducing the can size from 6-ounces to 5-ounces. However, the cost and retail price of the smaller size can is generally the same as the larger size can. Costco, however, increased the can size of its Kirkland Signature solid white albacore tuna in water from 6-ounces to 7-ounces. Jay Tilley, a Costco buyer, said, “We are bucking the tuna industry trend. We feel we are offering a great value for our members with our tuna.”

Detergent – When developing private label products, Costco buyers analyze all product components including packaging and distribution. Costco’s laundry detergent line includes: concentrated scented, concentrated unscented and environmentally friendly. When the company and its supplier developed the bottles for these items, a new design was offered that enabled the manufacturer to fit 120 bottles on a pallet compared to 90 bottles of a leading national brand.

This development improved shipping and distribution efficiency. More bottles could be ordered per truckload which lowered the trucking and distribution cost per bottle which enabled Costco to either offer a lower price or improve margins. In the October, 2009 issue of *The Costco Connection*, Deb Belcourt, a Costco buyer, said, "We designed the best bottle in the industry today. It's one part of the formula to offer this product at a savings of well over 20 percent versus the leading national brand."

Bed Sheets – Development of Costco's bed sheet line offers a glimpse at its detailed focus. Carole Speer, the manufacturer representative for Divatex (Costco's sheet vendor), said, "A lot of people look at thread count and don't look any further. They didn't notice that the manufacturer used an inferior type of cotton or dye or that it's not a 'true' 600 thread count, or that the sheets are actually smaller. There are so many factors that, when combined correctly, make an exceptional sheet." In the October, 2009 issue of *The Costco Connection*, Kathy Thull, assistant general merchandise manager at Costco, said, "It's accepted in the industry for a lot of retailers to test lower than 600, yet still claim that thread count. They allow this. We don't."

Other features of Costco's Kirkland Signature sheets include: the sheets are sewn with 11 to 12 stitches per inch compared to the industry average of six to eight, the sheets are pre-shrunk, a high quality elastic is sewn all the way around the fitted sheet and not just in the corners and hems are double folded then stitched leaving no raw edges.

Pricing Analysis

This last section analyzes two private label retail pricing charts. The first chart compares club private label pricing to each item's competing national brand. The second chart compares the pricing of a private label item which all three clubs stock. The data for each chart was gathered in January, 2010.

Club	Product	National Brand				Private Label				
		Brand	Pack	Retail	Per Unit	Brand	Pack	Retail	Per Unit	Savings
Costco	AA Batteries	Duracell	36 ct	\$13.69	\$0.3803	Kirkland Signature	48 ct	\$10.99	\$0.2290	66%
	Adult Multivitamin	Centrum	365 ct	\$18.59	\$0.0509	Kirkland Signature	500 ct	\$14.99	\$0.0300	70%
	Cetrizine (Allergy Medicine)	Zyrtec	75 ct	\$32.99	\$0.4399	Kirkland Signature	365 ct	\$16.29	\$0.0446	886%
	Diet Green Tea	Lipton	28-16.9 oz	\$12.99	\$0.0275	Kirkland Signature	35-16.9 oz	\$10.89	\$0.0184	49%
	Fabric Softener	Downy	168 oz	\$12.49	\$0.0743	Kirkland Signature	150 oz	\$8.69	\$0.0579	28%
	Facial Tissue (Upright)	Kleenex	12-85 ct	\$15.49	\$0.0152	Kirkland Signature	12-100 ct	\$13.69	\$0.0114	33%
	Ibuprofen (Pain Reliever)	Advil	325 ct	\$15.29	\$0.0470	Kirkland Signature	2-500 ct	\$8.99	\$0.0090	423%
	Solid White Albacore Tuna	Bumble Bee	8-7 oz	\$12.79	\$0.2284	Kirkland Signature	8-7 oz	\$11.99	\$0.2141	7%
	Aluminum Foil	Reynolds	2-250 sq ft	\$14.99	\$0.0300	Kirkland Signature	2-250 sq ft	\$11.99	\$0.0240	25%
	Canned Cat Food	Fancy Feast	36-3 oz	\$16.99	\$0.1573	Berkley & Jensen	36-3 oz	\$14.79	\$0.1369	15%
BJ's	Extra Heavy Mayonnaise	Hellman's	128 oz	\$9.99	\$0.0780	Executive Choice	128 oz	\$6.99	\$0.0546	43%
	Red Plastic Cup - 16 oz	Solo	136 ct	\$7.99	\$0.0588	Berkley & Jensen	180 ct	\$7.99	\$0.0444	32%
	Replacement Brushheads	Oral-B	6 ct	\$28.99	\$4.8317	Berkley & Jensen	6 ct	\$16.99	\$2.8317	71%
	Sandwich Bags	Glad	4-115 ct	\$6.99	\$0.0152	Berkley & Jensen	4-115 ct	\$5.99	\$0.0130	17%
Sam's Club	Scoopable Cat Litter	Scoop Away	40 lb	\$12.99	\$0.3248	Berkley & Jensen	40 lb	\$8.99	\$0.2248	44%
	Semi Sweet Morsels	Nestle	72 oz	\$8.99	\$0.1249	Berkley & Jensen	72 oz	\$7.99	\$0.1110	13%
	AA Batteries	Energizer Max	48 ct	\$17.98	\$0.3746	Member's Mark	48 ct	\$9.88	\$0.2058	82%
	Apple Juice	Mott's	2-86 oz	\$4.16	\$0.0242	Member's Mark	2-96 oz	\$3.98	\$0.0207	17%
	Bleach	Clorox	3-182 oz	\$8.12	\$0.0149	ProForce	4-128 oz	\$5.87	\$0.0115	30%
	Cat Food - Variety	Friskies	48-3 oz	\$17.88	\$0.3725	Member's Mark	48-3 oz	\$13.92	\$0.2900	28%
	Cooking Spray	Pam	2-8.5 oz	\$5.46	\$0.3212	Bakers & Chels	2-16 oz	\$5.88	\$0.1838	75%
	Cranberry Juice Cocktail	Ocean Spray	128 oz	\$4.74	\$0.0370	Member's Mark	2-64 oz	\$4.68	\$0.0366	1%
	Fabric Softener	Downy	129 oz	\$9.96	\$0.0772	Member's Mark	168 oz	\$9.48	\$0.0564	37%
	Mayonnaise	Ken's	128 oz	\$6.88	\$0.0538	Bakers & Chels	128 oz	\$5.68	\$0.0444	21%

WCF Research - January, 2010

National Brand Comparison – Eight private label items along with the competing national brand were selected at each club (see chart on the left).

The pricing for the private label and national brand products were compared. The unit retail price of each item was calculated and the savings determined. Private label savings range from 1% to 886%. For example, Costco stocks a case of thirty-five 16.9-ounce bottles of Kirkland Signature diet green tea for \$10.89 or 1.8-cents-per-ounce. The competing national brand is Lipton whose package includes twenty-eight 16.9-ounce bottles for \$12.99 or 2.8-cents-per-ounce. Costco's diet green tea offers a per-ounce savings of 49%.

Club Private Label Pricing Comparison – Ten private label items stocked by all three clubs were selected for this analysis (see chart below). The per-unit retail price was determined for each item. Sam's per-unit retail price was used as the base for the comparison. The per-unit retail price for BJ's and Costco was compared to Sam's per-unit retail price and the percentage higher or lower was calculated. That figure, which was multiplied by 100, appears in the differential (DIFF) column. A number above 100 indicates that club's per-unit retail price is higher compared to Sam's and a number below 100 indicates that club's per-unit retail price is lower than Sam's.

Product	Sam's Club				Costco				BJ's Wholesale					
	Brand	Pack	Retail	Unit Retail	Brand	Pack	Retail	Unit Retail	DIFF	Brand	Pack	Retail	Unit Retail	DIFF
AA Batteries	Member's Mark	1 48 ct	\$9.88	\$0.2058	Kirkland Signature	1 48 ct	\$10.99	\$0.2290	111	Berkley & Jensen	1 48 ct	\$9.99	\$0.2081	101
Almonds	Member's Mark	1 3 lb	\$9.28	\$3.0933	Kirkland Signature	1 3 lb	\$9.69	\$3.2300	104	Berkley & Jensen	1 3 lb	\$10.99	\$3.6633	118
Canned Chicken	Member's Mark	5 13 oz	\$9.98	\$0.1535	Kirkland Signature	6 12.5 oz	\$10.99	\$0.1465	95	Berkley & Jensen	4 12.5 oz	\$7.99	\$0.1598	104
Diapers - Size 3, 16 - 28 lb	Member's Mark	1 200 ct	\$32.32	\$0.1616	Kirkland Signature	1 208 ct	\$39.59	\$0.1903	118	Berkley & Jensen	1 174 ct	\$24.99	\$0.1436	89
Fabric Softener Sheets	Member's Mark	1 250 ct	\$5.48	\$0.0219	Kirkland Signature	2 246 ct	\$8.69	\$0.0177	81	Berkley & Jensen	2 160 ct	\$5.99	\$0.0187	85
Ibuprofen (Advil)	Member's Mark	2 500 ct	\$8.86	\$0.0089	Kirkland Signature	2 500 ct	\$8.99	\$0.0090	101	Berkley & Jensen	1 500 ct	\$6.99	\$0.0140	158
Plastic Wrap - 12" x 3,000'	Bakers & Chels	1 1 ct	\$11.22	\$11.2200	KS/Stretch Title	1 1 ct	\$11.99	\$11.9900	107	Executive Choice	1 1 ct	\$12.79	\$12.7900	114
Salted Butter Quarters	Member's Mark	4 1 lb	\$7.16	\$1.7900	Kirkland Signature	4 1 lb	\$6.59	\$1.6475	92	Wellesley Farms	4 1 lb	\$7.99	\$1.9975	112
Trash Bags - 33 gal - Drawstring	Member's Mark	1 90 ct	\$11.72	\$0.1302	Kirkland Signature	1 90 ct	\$12.99	\$0.1443	111	Berkley & Jensen	1 90 ct	\$12.99	\$0.1443	111
Tylenol PM	Member's Mark	2 150 ct	\$5.42	\$0.0181	Kirkland Signature	2 250 ct	\$8.99	\$0.0180	100	Berkley & Jensen	1 500 ct	\$7.99	\$0.0160	88

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For example, Sam's stocks a package of five 13-ounce cans of Member's Mark canned chicken for \$9.98 or 15.4-cents-per-ounce. Costco stocks a package of six 12.5-ounce cans of Kirkland Signature canned chicken for \$10.99 or 14.7-cents-per-ounce, a 5% savings compared to Sam's Club. BJ's stocks a package of four 12.5-ounce cans of Berkley & Jensen canned chicken for \$7.99 or 16.0-cents-per-ounce, 4% more compared to Sam's Club.