



Membership has its perks

A unique shopping experience, value-minded pricing and a high-quality private brand continue to attract members to Costco stores.

By Michal Christine Escobar

While researching Issaquah, Wash.-based Costco Wholesale Corp., *Store Brands* came across several Internet lists of interesting facts about the retailer. While some facts are very well known (e.g., Costco has been selling a hot dog and a drink for a \$1.50 since 1985), others took us by surprise. For instance, a Costco membership card is considered to be an acceptable form of identification to get through the TSA's airport security checkpoints; Costco's rotisserie chicken has its own Facebook fan page where Costco members trade recipes; the retailer's Lancaster, Pa., location constructed a livestock parking stall for its Amish customers to park their horses and buggies; and in 2014, the retailer sold almost 400,000 cars — making it the second largest car dealer in the nation.

Another “fact” mentioned fairly regularly on these Internet lists is that consumers love Costco. And the retailer has the numbers to prove it. In its 2015 Annual Report, covering the

fiscal year ending Aug. 30, 2015, Costco reported that “member loyalty... continued to reach record levels in 2015: 91 percent of members in the U.S. and Canada and 88 percent worldwide” renewed their memberships. Members also are shopping at Costco stores more frequently. The 2015 Annual Report states the shopping frequency, year-over-year, increased 4 percent.

Who are these loyal Costco members? According to InfoScout, a consumer data firm based in San Francisco, Costco shoppers are more likely to be members of Generation X (primarily 35-44 years of age), have a relatively high income (\$80,000 or more per year) and have a household size between four and seven. Costco's shoppers are primarily white, but the retailer does over-index on both Asian and Hispanic shoppers as well.

The treasure hunt experience

For years, Costco has used the term “treasure hunt” to

describe its in-store shopping experience. It's been widely reported that as part of its retail strategy, Costco dedicates between 20 and 25 percent of its stock to limited-quantity items kept in stores for only brief periods of time, sometimes only a week. And these items are supposed to be "really unique and interesting items," states Sally Seston, director, Retail Category Consultants, Toronto. Costco shoppers, therefore, are prone to feeling the need to visit stores "early and often because there [is] a limited supply of these treasures."

However, some consultants, including Seston, believe that the treasure hunt experience is not as exciting now as in years past, especially when it comes to Costco's seasonal programs.

"Some of the luster is coming off the rose," Seston notes. "I hear people say that it used to be really fun in October when Costco first put out its Christmas items because it had such fabulous and short-supply specialty gifts. But now they say it's getting stale because it's the same Starbucks gift basket every year."

The treasure hunt experience also refers to how the retailer frequently moves its merchandise, specifically shopping staples such as light bulbs, detergent and paper towels, around the store. And it refuses to put up signage directing shoppers to where items are, states Timothy Campbell, analyst, Kantar Retail, Wilton, Conn.

"It wants members to get lost in the store so they'll come across more interesting things and buy more things," he notes.

Interestingly, consumers respond very well to this strategy.

"Its members aren't prone to say they like shopping Costco for being a one-stop shopping location or because



they can get in and out quickly," Campbell adds. "Members say they like shopping there because it is an experience."

The one and only

Introduced in 1995, Kirkland Signature — Costco's sole private brand — can be found in categories as wide ranging as dress shirts, alcohol, pet food, cookware, cooking oil, automotive parts, vitamins and peanut butter. According to the retailer's website, its brand is meant to offer customers the "perfect combination of quality and price."

Based on dollar spend, consumers seem to really enjoy the brand. Sara Al-Tukhaim, director of retail insights, Kantar Retail, says Kirkland Signature is a \$25 billion brand. Approximately 18 percent of Costco's 3,700 carefully curated in-store SKUs are branded Kirkland Signature, and about 26 percent of the retailer's sales come from the Kirkland Signature brand.

Data from InfoScout indicate that the Kirkland Signature brand is a big draw for club consumers. Costco shoppers who purchase Kirkland Signature products shop 2.2 times more frequently than Sam's Club shoppers who purchase Member's Mark products. These same Costco shoppers also spend 50 percent more money per trip. However, their overall average basket size is slightly below Sam's Club's average basket size.

But the retailer continues to have loftier goals for its store brand. It has a 35 percent store brand penetration goal that it refers to regularly, Al-Tukhaim says.

Costco's commitment to quality and value could be one reason Kirkland Signature has a good reputation among consumers.

"I would say [it] is overall the most respected private brand in America," says Jim Wisner, founder and president, Wisner Marketing Group, Libertyville, Ill.

That could be because the retailer decided to market Kirkland Signature as a high-quality brand for an exceptional value.

"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

Costco's digital strategy

During a recent earnings conference call, an investor asked Costco executives if the company would be getting more serious about its digital and e-commerce strategy, states Jason Goldberg, senior vice president commerce and content practice, Razorfish, Seattle. And a Costco executive replied: "Probably not." That same executive went on to say that even though Costco knows e-commerce is important, the retailer doesn't want to give its customers "a reason to stay home."

"In my view, that's striking and underscores their lack of sophistication around understanding the modern consumer's path to purchase," Goldberg adds. "The majority of shoppers in the United States use digital tools to pre-shop and ultimately walk into a store to buy the goods."

E-commerce makes up about 7 to 10 percent of all retail sales, but 54 percent of all purchases in the United States are digitally influenced, he goes on to say. So digital tools — such as Amazon reviews, online coupon websites, or price comparison tools — are helping consumers decide what to buy in the store, not what to buy online. Because Costco refuses to invest in this area, its customers end up using its competitors' digital tools, and this creates an opportunity for a competitor to win over the Costco customer, Goldberg suggests.



members,” says Craig Jelinek, president and CEO of Costco, on its website.

Data from InfoScout indicate that once consumers try the Kirkland Signature brand, they remain loyal purchasers. For instance, in the paper towel category, the Kirkland Signature brand is the No. 1 brand and makes up 50 percent of all sales; in the laundry category, it is the No. 1 brand and makes up 25 percent of all sales.

To ensure that its brand continues to offer shoppers a premium value, the retailer constantly looks to improve.

“We’re constantly looking at Kirkland Signature items, revisiting them with an eye to making them better,” says Jeff Lyons, Costco’s senior vice president of fresh foods, on the retailer’s website.

And the improvements are noticeable.

“Kirkland Signature offers continual improvements,” Campbell says. “For example, summer apparel will demonstrate visible improvements from one year to the next: better material, a complaint fixed, etc.”

Another potential reason Kirkland Signature is highly regarded by many consumers is Costco’s effective use of cobranding with national brands, lending a certain aura of quality and level of trust to some of the retailer’s own-brand products.

Not only is Costco’s use of cobranding unique, the retailer has also explored it more than most other retailers, Wisner states.

During a recent visit to a Costco warehouse, *Store Brands* found multiple instances of cobranding in just the coffee aisle. The retailer cobranded with Juan Valdez on its Kirkland Signature 100 percent Colombian Supremo Ground Coffee, for example, and with Starbucks on its Kirkland Signature Roasted by Starbucks Espresso Roasted Whole Bean Coffee.

Another way the retailer tries to ensure its private

brand lives up to consumer expectations is through authenticity. Costco will often go to great lengths to ensure Kirkland Signature products are as authentic as possible, Wisner notes. For instance, in June 2015, the retailer announced that it upgraded its Basil pesto to use Genovese basil, grown in Genoa, Italy. Costco said the basil is renowned for its sweeter taste and rich oil content and is the only basil that has a protected designation of origin on the market.

“Many people might not be able to discern the difference between the different basil,” Wisner says, “but Costco went to those lengths to say: ‘This is really what Kirkland Signature is all about.’ They’re sincere.”

Room for improvement

But not everyone is a fan of Costco’s treatment of its private brand. While the retailer is famous for having only the one store brand, Seston feels that it would fare better if offered at least one other tier: Kirkland Signature Organic. Costco is currently the largest organic grocer in the United States, with \$4 billion in organic sales, surpassing even Whole Foods. And while the retailer offers organic products under its store brand, it can’t communicate that fact very well to its customers because it cannot give the impression that every store brand product is organic, Seston says.

Additionally, while the quality of Kirkland Signature might be high, Seston feels the brand is not innovative.

“For a lot of consumers, they view Kirkland Signature as a great value but not a unique product,” she says.

Chuck Palmer, chief strategist for Columbus, Ohio-based Consumer X Retail, agrees.

“Kirkland Signature items are often the entry point, standard, basic item,” he says. “When there is some point of differentiation, it goes to a national brand. For example, the five-cheese tortellini will be Kirkland Signature, but next to it is the Lobster Tortellini — a more special item — under a national brand.”

What’s more, Palmer feels the Kirkland Signature packaging design could be improved on.

“The Kirkland Signature packaging design is generally not premium,” he says. “It usually says ‘value’ to the customer. It’s not consistent across categories. Overall, the packaging and presentation does not seem tight. I think they’re more interested in getting prices lower than in branding consistently across the warehouse. The only



consistency is that the logo is centered and at the top of the label.”

Marketing differently

One of the main other differences between Costco and other consumer packaged goods retailers is its marketing philosophy.

“Costco wants to drive down costs as much as possible, and it doesn’t have a marketing department intentionally so that it can keep costs low for its members,” Campbell says. “They rely on word of mouth.”

While some might criticize this approach, Palmer thinks they’ve “struck gold” with this strategy.

“They get their customers to do their marketing for them,” he says. “It’s self-perpetuating; it’s inexpensive. To get it right, you have to be really good at what you do, and they are.”

Plus, using traditional media such as TV and radio for marketing is costly and not always effective, Seston says. Millennials, for instance, watch fewer TV shows and, when they do, they skip through the commercials.

However, word of mouth does have its limitations. For instance, Campbell mentions that he’s heard stories of individuals who said they weren’t aware there was a Costco nearby because no official advertising reached them.

Costco does use its Facebook page to connect with shoppers.



“They do a fairly good job of maintaining a healthy social media presence,” Campbell adds. “People will often go on Costco’s Facebook page and ask the retailer to open a new location near where they live. You don’t see that as much with other retailers.”

And once in a while, the retailer will even use websites such as Groupon.com or LivingSocial.com to market itself and sell memberships. However, while these websites

Cover Story: **COSTCO** WHOLESALE

typically sell items with discounted prices — Costco will not discount its memberships. Instead it will include additional “freebies,” usually Kirkland Signature products, as a value-added proposition, Al-Tukhaim says.

The retailer also uses *The Costco Connection*, its member-only magazine, to market itself and its store brands.

“Kirkland Signature is a huge focus for [*The Costco Connection*],” Al-Tukhaim says.

“It resonates with members, as well as club managers, who have a lot of autonomy in deciding what goes where in the club and merchandising efforts in the box as well.”

To keep costs low,



Costco has a very minimalist in-store merchandising strategy, too. Interestingly, this no-frills shopping experience is one part of the draw to the store, Palmer says.

“The stores are bleak, undecorated, which is intentional,” he adds. “But it contributes to the perception of the value proposition. If they decorated at all, it would throw people off.

Perhaps the marketing strategy Costco is most famous for is its in-store sampling program.

“You almost take it for granted,” Wisner says. “But it’s critical. It’s part of the expectation of the shopping trip and perhaps even a small driver: ‘Let’s go snack at Costco and hunt for something new to buy.’”

While the retailer uses its sampling program to market national brands, private label items are sampled as well.

“Through highly organized merchandising and pervasive in-store product demonstrations, Costco is always focused on creating awareness of its Kirkland Signature private label products and merchandise,” states Jeff Hall, president, Second to None, Ann Arbor, Mich. “Food and beverage demonstrators are strategically placed throughout the warehouse, and [the retailer is] adept at positively connecting with members, while highlighting new, interesting and best-selling items. This creates an experiential and engaging selling environment.” **SB**