TRUSIF

Costco Wholesale

Consumer Staples
NASDAQ: COST
Market Outperform| Buy

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Valuation

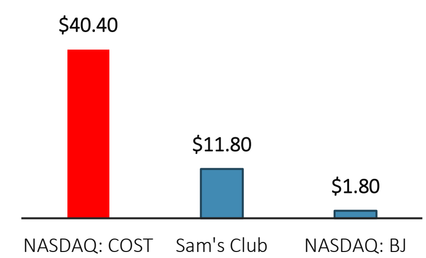
Current Share Price	$356.12
Target Price	$477.43
Dividend Yield	0.77%
Discount Rate	4.35%
TV/EBITDA	19.6x
Conviction	Buy

Market profile

52 Week Range	$271 - $393
Market Cap ($mm)	$161,669
Net Debt ($mm)	-$2,219
Enterprise Value ($mm)	$157,894
Beta (5 year)	0.66

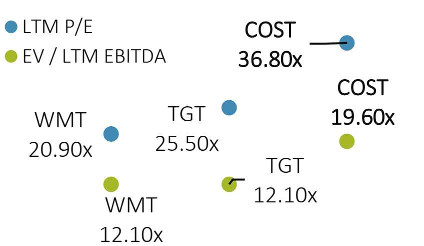
Metrics	2021 P	2022 P	2023 P
Revenue	$178,657	$191,617	$205,760
EBITDA	$7,640	$8,162	$8,731
EPS	$8.6	$9.4	$10.1
P/E	36.42x	33.21x	29.23x
EV/EBITDA	19.78x	18.41x	16.96x

Figure 1: Avg. Revenue per SKU



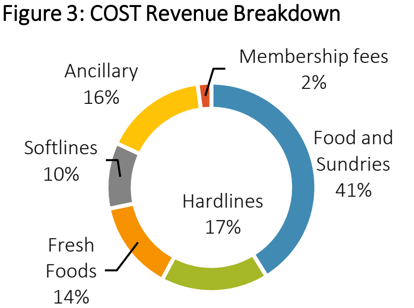
Source: CAPIQ

Figure 2: LTM P/E & EV / LTM EBITDA



Source: CAPIQ

Figure 3: COST Revenue Breakdown



Source: Company Model

Business Description

Costco Wholesale Corporation (NASDAQ: COST) is an American multinational corporation that operates a chain of membership-only warehouse clubs. The company offers its members discount prices on private label and brand name products.The corporation is the second-largest retailer in the world after Walmart.

Industry Overview

Costco's main competitor is Walmart which holds ~73% of the U.S. market share. Although Costco has a lower market share in the U.S. at ~21%, the company is much stronger in Canada by holding ~58% of the market. Walmart is second in Canada by holding ~19% of the market share.

Mandate Fit

ESG: Costco donates 1% of their pre-tax profits to charitable foundations focused on children, education, health, and human services to benefit the community. Their suppliers are subject to a Supplier code of conduct, promoting strategic and ethical collaboration.

Management: Craig Jelinek has been Costco's CEO since 2012. He has been with the company since its inception and has been an executive officer in the company since 1995. Craig Jelinek and his executive leadership team have a strong track record of returning capital to shareholders, managing Costco, growing revenues, and investing in beneficial projects.

Balance Sheet: Costco's total debt is around $11BN. However, the company has over $12BN in cash which can completely cover its debt. Costco's Net Debt/EBITDA is significantly low at (0.03)x compared to its main competitor Walmart's of 1.8x.

Growing Free Cash Flow: COST boasts a five-year FCF CAGR of 26%. The Company consistently returns value to shareholders and continues to allocate capital to expanding its number of warehouses throughout the U.S. and internationally. The 5y average EBITDA margin is ~4.3%. The company continues to invest in the U.S. and other countries to increase the number of its warehouses.

Competitive Advantage: One of the main advantages for COST is its subscription-based business model. This provides it with recurring revenue through membership fees that make up ~70% of EBIT. Additionally, COST boasts strong comparable store sales and comparable e-commerce growth, with its most recent fiscal year reporting 8% and 50%, respectively

Risks

COST's lack of buy-online, pick-up in-store ("BOPIS") is currently an area to consider as many competitors in the industry are offering this feature. The BOPIS trend gained momentum throughout the COVID19 pandemic. Current outlooks are varied if COST requires a BOPIS feature. COST already offers a strong e-commerce platform, and the ability to charge pick-up fees for BOPIS may eventually be removed, which offers little profitability for many retailers. Traffic trends at COST have generally returned to positive, in contrast to the majority of the retail industry. The Company also boasts a stronger sales velocity than any other retailer or club format store.

Investment Thesis

COST's target price was achieved through a five-year 50/50 blended Stable Growth DDM (4.3% WACC with a 2% terminal growth rate) and an EBITDA exit multiple of 16.6x. TRUSIF believes COST's premium valuation is warranted due to the Company's best-in-class business model and ability to offer resilient performance throughout the current economic conditions. COST has a devoted customer base boasting ~90% renewal rates and consistent comparable-store sales growth. The Fund will continue to monitor COST's performance and valuation to ensure it continues to fulfill the mandate. The corporation is defensive and has a reliable management team. Moreover, its self-service environment enables them to turn over their inventory far quicker than their direct competitors, with twice the inventory turnover ratio. Customers at Costco have high brand loyalty, with renewal rates over 90%, allowing the company to predict their revenue with some certainty.