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Analysis of Costco's Business Model and Its Entry to Chinese Market

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Abstract: This paper examines Costco's strategic practices in entering the Chinese market against the backdrop of globalization. Using the SWOT model, the analysis highlights its robust financial strength, unique membership-based culture, and employee relations advantages, while also pointing out its over-reliance on the North American market. In the Chinese market, its value-for-money positioning has successfully attracted rationality-conscious younger consumers, though it must contend with intense competition from rivals such as Sam's Club. Furthermore, through the PLOC management functions framework, the paper elaborates on how Costco adapts and executes its core business model locally via planning, organizing, leading, and controlling. The study concludes that, despite facing complex localization challenges, Costco holds promising prospects in the Chinese market, owing to its strong membership system and precise middle-class positioning.

Keywords: Warehouse Club Model; Market Entry Strategy; Retail Internationalization; Localized Operation.

1. Introduction

According to the Management of Globalization (2021), globalization is the meaning of an increase in the flows of goods, services, and financial resources across nation-state borders [8]. Harmon (2023) indicated that international trade is one of the globalization, which helps improve a country's economy by increasing its gross domestic product (GDP), or the total value of goods and services produced [7]. However, with the popularity of international trade these years, it has caused a fierce competitive environment, which attracted the attention of CEOs. As a result, more companies began to attach importance to it because internationalization is correlated to both economic development overseas and the potential risk, which can influence the future prospects of a company.

This essay will explore the impact of Costco's entry into the Chinese market. Firstly, give a brief description of the Costco business itself. Then, from the perspective of the SWOT model, the essay evaluates the internal and external factors that impact the company's business practices and strategies in the Chinese market due to globalization. Additionally, it will explain how the management functions can be applied with the model of PLOC in order to address the problems caused by the internal and external factors. Finally, this essay will analyze the benefits and complexities of Costco in the Chinese market. The theory named The Human Relations will be used to explain the management of Costco, which is directed at improving the whole business entity through the social and corporate efficiency of its members and products (Omodan et al., 2020) [16].

2. Costco and its entry to China

Costco Wholesale Corporation is a publicly traded retail company that uses a membership-based warehouse club business model to deliver low prices on brand-name products and merchandise (Greene et al., 2024) [6]. In 1976, Costco began operations as Price Club. The world's first membership-based warehousing wholesale Club Price Club was established in San Diego, California (Meet Costco, 2019) [13]. The idea of setting up Costco came to Jeff Brotman while he saw the French market that combined discount supermarkets with department stores. Jeff Brotman believed that if this management model can be used in the United States, it will surely enjoy great popularity among people. Afterwards, he found his partner called Jim Sinegal and created Costco in joint efforts. Since 2019, Costco has entered the Chinese market from Shanghai and received good reviews in China. Now, the Costco company has even expanded worldwide, which includes more than 890 warehouse locations and nearly 129.5 million cardholders (Greene, 2024) [6].

3. SWOT Analysis

This essay will use the SWOT model to analyze the internal and external factors that might impact the company's business practices and strategies in the Chinese market.

3.1. Strength

3.1.1. Financing

Relatively speaking, the most important internal factor in business is financing. That is because it is a valuable resource for a company to drive growth, create value and sustain operations. Costco (2024) announced its operating results for the fourth quarter and the full year of the fiscal year 2024. The data shows that its total revenue reached 254.4 billion dollars and its net profit was 7.367 billion dollars, which demonstrates that the company has strong profitability to develop (Costco Wholesale Corporation, 2024) [4]. This further explains that Costco has full capacity to better operate the business entity itself and even put Costco in a beneficial position in the Chinese market.

3.1.2. Organizational Culture

Costco offers a rich salary and welfare for their employees. It is said that Costco uses all its funds for the company's operations, with 70% of the funds allocated to employees (https://xueqiu.com/3998325123/220057617., 2022). The organizational culture of Costco is that employees are the

most important asset, which is the second important internal factor for Costco to develop prosperously. Since the foundation of Costco, Costco has devoted themselves to providing employees with both opportunities and welfare. This kind of organizational culture not only reduces employee turnover, but also inspires employee enthusiasm and loyalty that is correlated with the theory of Human Relations [16].

3.2. Weakness

3.2.1. High dependence on North America

Sales in the United States and Canada account for over 80 percent of Costco's revenue (FourWeekMBA, 2024) [5]. This is not a suitable circumstance because the development of Costco can be hindered due to a few internal management factors. Firstly, it is the supply chain risk. Assume that the supply chain in the American market rises costs and even disrupts, it can lead to some negative impacts on Costco itself. Secondly, it is the challenge of cultural adaptation. The successful business model in the United States may not be suitable for other countries, which need to be changed connected with the local culture.

3.3. Opportunity

3.3.1. The attraction to young customers

Customer is the critical external factor and can decide the future of a business entity. How to attract more customers in the market is the key to business success. Costco has already applied the LOW COST principle well to attract customers from all over the world. With this principle, Costco successfully attracted the attention of young customers. There is a trend that young people become more prudent, pay attention to cost performance and attempt to seek low prices while ensuring quality (Beijing News, 2024) [2]. According to Sohu (2024) [18], on the first day of opening in the Shenzhen store, Costco attracted a large number of customers, mainly youngsters. They lined up to scan goods and punch in between the huge shelves to take photos. This news illustrated that Costco provides the choice for young people's opinions, which simultaneously acquires the opportunity to develop Costco itself.

3.4. Threats

3.4.1. Competitive Industry

As the external factor, competition is the largest threat to Costco itself. Costco operates in a highly competitive industry, where players mainly compete based on price, merchandise quality and customer service (Marketline Company, 2024) [11]. There are many threats brought by the same competitive industry. To attract shoppers, companies such as Amazon, Walmart, and Target are offering discounts and new merchandise (Kang, 2024) [9]. What makes Costco reputable is "benefits." It is said that whether it is Feitian Moutai, which is 1 yuan lower than the market guidance price, or its widely circulated profit red line standard of "gross profit rate of more than 14% requires the signature of the CEO"(New Business Knowledge, 2020) [15]. Cost performance has become a powerful weapon for Costco to cut into the Chinese market. Relatively speaking, Sam's Club is unarguably the biggest competitor to Costco, which leaves a deep impression on the consumers with the word "quality." What makes Sam's quality so highlighted is the strict selection system: the beef is fed for 100 days with special cattle breeds and dosage scales. The selection criteria for red jujube are more than 12 grams and a meat yield of 90% (New Business Knowledge, 2020) [15]. However, with the development of society, it may generate a new competitive landscape in which new enterprises enter and old rivals surround.

4. Costco Management Functions in The Chinese Market

This essay will explain how the management functions can be applied within Costco itself to expand globally, especially focused on when they entered the Chinese market, which will use the PLOC model including planning, leading, organizing and controlling.

4.1. Planning

Planning means looking ahead and developing guidance for future action (MSG, no date) [14]. It can help business entities identify future opportunities and threats. It is said that Costco's plan when entering China was to keep the core strong and focus on the customer. Ton (2024) stated that Costco can stick to the core by connecting each decision to operations, competitiveness, and profitability [20]. In addition, Costco puts its sight on the Chinese middle class, which needs the ultimate cost-effective goods. To guarantee the company's future, Costco should learn about the different preferences in different regions. After all, this strategy can not only contribute to the progress of Costco, but also improve customers' satisfaction. After learning about the different local preferences, Costco can build up a stable relationship with the local community, which can promote cultural exchanges as well.

4.2. Organizing

Surbhi (2021) stated that organizing is the second key management function, which arranges resources, coordinates human efforts and incorporates that helps in the achievement of objectives [19]. It is said that Costco uses the membership retail model because this model receives a positive reflection and is a key to Costco's profitability. Data from 2023 showed that Costco's global membership has exceeded 100 million, which provides a solid foundation for its continued low price policy (Baidu, 2024) [1]. What Costco has been using is such a special model that produces positive feedback on both customers' commitment and the business's income. However, in order to survive in the Chinese market, Costco has to overcome the pressure brought by crossing borders and need to invest more funds. For example, the different taxes in China, the various systems and the need to increase publicity. Therefore, it is important for Costco to enhance the ability of localization through arranging the resources and fully making use of the human labor.

4.3. Leading

According to the Project Management Report (no date), leading guides employees to work as a team toward the organization's goal [17]. It can keep employees motivated, inspired, and focused to work. To begin with, motivation is critical to the organization as a whole. Costco is known as the company that cares about employees, so the strategy Costco used should inspire enthusiasm. To illustrate, give employees a higher salary, a comprehensive benefits plan and a suitable working environment. Furthermore, Costco recommends teamwork, which is aimed at strengthening collaboration and minimizing conflict. From the above mentioned, these contents are correlated to the theory of the Human Relations

[16].

4.4. Controlling

Controlling involves monitoring performance in order to ensure the organization achieves desired results and reaches its goals (Project Management Report, no date) [17]. As a foreign company, Costco has found strategies to increase publicity in the Chinese market. Through effective control in low price and high quality, Costco could not only ensure the building of corporate image, but also expand the market shares. In addition, to better control the whole company, Costco should build the perfect incentive mechanism, which will improve work efficiency and increase commitment from the Human Relation's theory [16].

5. Costco's Benefits and Complexities of Business in China

In the background of globalization, Costco has great ambition to expand its market all over the world. After joining the World Trade Center Organization, China has attracted more attention from various countries, and the business environment has greatly improved. As a consequence, an increasing number of companies are willing to choose to invest in China, so it is no doubt that the Chinese market is crucial to the development of Costco itself. According to Mckinsey (2021) [12], China accounted for 18 percent of global GDP, as much as the entire European Union and second only to the United States. Therefore, in order to expand business in China, Costco ought to fully utilize its benefits and correct its complexities in line with the preferences of Chinese.

5.1. Benefits

The membership system is a successful strategy used by Costco compared to many retail industries. As a members-only warehouse club, Costco saw a steady rise in its membership from 44.6 million in 2015 to 539 million members in 2019 (Bisht, Nair, 2021) [3]. Moreover, this system is indispensable to the theory of Human Relations [16]. That is because the membership system increases the commitment of customers, especially for the Chinese middle class, who need convenient service and cost-effective productions. It has been proven in the fact that 90% of members will continue to renew after a quarter (Kang, 2024) [10].

5.2. Complexities

When entering China, Costco faced a different marketing environment, which tested Costco's ability to localize. Additionally, it needs a long time for Costco to learn how to make selections that needed accurate understanding of China's customers. In addition, it is important for Costco to seek innovative strategies to attract Chinese consumers in the long run of management.

6. Summary

In conclusion, it is the right choice for Costco to expand to China. After introducing the background of globalization and Costco itself, this article discusses the characteristics through the SWOT model and uses the PLOC model to remedy the management functions of Costco. Though the process that entered the Chinese market has many difficulties, it is worth for Costco to invest efforts to cater for the demanding needs of Chinese consumers.

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