Annual Report 1998

The Right Way To Shop

PRICESMART™ Membership Shopping

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Online Information

www.*pricesmart*.com

www.*psvacations*.com


Asia
America

Chairman's Letter

Dear Stockholder:

PriceSmart Inc. recently completed its first year of operations as an independent publicly traded company. The separation from Price Enterprises Inc. which occurred on August 29, 1997, has encouraged all of us to focus energy and attention on building a successful international merchandising business. As you will read in the accompanying letter from PriceSmart's President, Gil Partida, many good things have happened during the past 12 months.

On behalf of your Board of Directors, I want to tell you what I think are the two most important decisions we made during this past fiscal year. One was to adopt a strategic plan for the roll-out of warehouse club stores, primarily in Latin America. The implementation stage for this strategy is well under way. The other Board action occurred in December 1997, with the announcement that Gil Partida had been appointed President and CEO of PriceSmart Inc. Since joining the Company in January 1998, Gil has worked tirelessly to build a talented and effective management team, completing joint venture agreements and positioning PriceSmart Inc. for future growth.

As a stockholder and Chairman of the Board of PriceSmart, I take great pride and pleasure in working with Gil, with PriceSmart's employees and with PriceSmart's Board members. I look forward to fiscal year 1999 as a year of continued growth and improvement.

Robert E. Price

Robert E. Price,
Chairman of the Board

Board of Directors

Robert E. Price, Chairman; Directors: Lawrence B. Krause, Gilbert A. Partida, Leon C. Janks, Katherine L. Hensley,

President's Letter

Dear Stockholder:

In addition to being the first annual report for PriceSmart Inc., this report also marks the first eight months of my tenure as its President and CEO. I firmly believe that our value proposition of delivering quality goods and services at low prices transcends language and cultural barriers. With the strength of our balance sheet, management talent and the soundness of our concept, I believe the Company is well positioned for future growth.

The following summarizes our 1998 results. Revenues for fiscal year 1998 were $97.2 million which included $83.8 million from the Company's international business, $5.8 million from its travel business and $7.6 million from other businesses. Net income for the year was $3 million or $.50 per diluted share. Income resulted from the travel and auto programs profits, investment income from cash balances, marketable securities and notes receivable, and non-reoccurring gains on the sale of properties. Income was reduced by international business losses and losses from the service center pilot program with Ralphs Grocery Company.

Our business strategy is simple. Grow the international membership merchandising business in markets that (i) are receptive to U.S. quality goods and services and (ii) permit majority foreign ownership in the retail sector. It is our belief that an equity model, where PriceSmart employees control the management of the stores, will provide more long-term, substantial earnings to our stockholders.

The Latin American consumer market is receptive to U.S. goods, and commercial statutes generally allow foreign ownership in the retail sector. Therefore, it is our primary international target market. Our strategy, set at our April 20, 1998 Board meeting, was to have deals for two stores in Latin American countries by August 1998 and deals for ten stores by May 1999. In early July 1998, we announced an agreement with Guatemalan-headquartered Grupo Solid to form a new joint venture company that will open two stores in Guatemala City. In early September 1998, we entered into an agreement with PSC, S.A. to form a joint venture company which plans to open nine stores in Costa Rica, the Dominican Republic, El Salvador, Honduras and Nicaragua.

The Asian markets, while presenting attractive opportunities, generally restrict foreign ownership in the retail sector. As a result, our business in Asia is operated through licensees. With the unfolding of the Asian political and economic crisis, our strategy was to provide the necessary management and technical support to help our licensees, but to nonetheless carefully manage political, economic and credit risk. As a necessary, but unfortunate result of the Asian crisis, (i) we terminated our license agreements for the Philippines and Indonesia and (ii) our licensee in the Mariana Islands closed its Guam store. As a result of closely managing economic, political and credit risk, PriceSmart suffered little economic loss from its Asian exposure. However, we remain committed to the right opportunities in Asia, especially joint venture arrangements. Although such equity opportunities would require laws to be changed, we are hopeful that could very well happen in some attractive markets in the near term.

The success of our business is based on each store's performance. Accordingly, learning from our Panama experience, our job is to focus on profitability at the store level. With two stores open in Panama in 1998, our intent was to develop a model and determine if a 50,000 square foot store could achieve the sales necessary to become a profitable business. (Based on our pro forma model, the target sales level per store was set at U.S.$25 million.) Currently, combined sales for both stores are annualizing at approximately U.S.$60 million. We have also implemented two new businesses in Panama – a tire center and an affinity auto insurance program. We are committed to developing new businesses and services that provide additional value for our member-customers.

Focusing on our core business has caused us to rethink some areas. In May 1998, we allowed our agreement with Ralphs Grocery Company to expire. While the concept was popular with customers, it did not generate sufficient volume to be viable. In August 1998, we entered into an agreement to sell our auto referral program, effective November 1, 1999. The program was sold for a net gain of $.4 million. The travel business remains profitable. We will continue to grow it and determine the best approach to maximize stockholder value. Finally, we are actively engaged in selling our remaining real estate holdings. The value of property currently held for sale is $4.9 million.

Our people management model is built on alignment of vision, management goals and compensation. Through an intensive strategic planning process, this has been achieved. The Board further adopted, subject to stockholder approval, the "1998 Equity Participation Plan" ("1998 Plan") to further align the interests of the employees and shareholders. Under the 1998 Plan, management invested in PriceSmart stock, showing its commitment and confidence in our business. The Board also authorized a 700,000 share stock repurchase program so that the 1998 Plan would not dilute the ownership interest of our current stockholders; it also increased the Company's book value per share.

I would like to thank Robert and the Board for allowing me to assume this exciting leadership position. I would also like to personally thank the 150 employees who make this business work every day.

Gilbert A. Partida
President & CEO

Gilbert A. Partida
President and CEO

PriceSmart…
is an international membership shopping concept modeled after the first membership merchandising chain in the United States, Price Club. The concept is to deliver significant value to the member-customer through an effective and efficient pipeline that leverages economies of scale in aggressive buying, low-cost distribution and streamlined operations.

Vision
To become part of our members' quality of life.

The Company Values…
- Honesty and Integrity
- Fairness
- Talent and Passion
- Entrepreneurialism
- Teamwork and Communication
- Accountability (to mission)

Mission
A strategically focused volume-driven and entrepreneurial membership merchandise and services leader delivering quality, value and low prices to the rapidly emerging consumer class in Latin America and Asia.

History of a Merchandising Concept

In 1976, Sol and Robert Price developed the membership merchandising concept and founded Price Club, where member-customers could take advantage of high-volume, low-cost operations to obtain the best possible prices on a wide array of merchandise. Today, we continue to maintain our pioneering commitment to provide quality, value and low prices for member-customers of PriceSmart, the newest generation of warehouse clubs.

Sol Price created the discount store industry in the United States by launching FedMart in 1954. Over the last forty-four years, the evolution of the industry in the United States has created more than 26 million card holders shopping at wholesale clubs. In the United States, the membership merchandising concept generates in excess of $45 billion in annual sales.

Today, PriceSmart is taking this proven concept to international markets.

Our History

1954 - Sol Price launches FedMart discount store concept

1976 - Pioneers of the membership warehouse shopping concept, Sol and Robert Price launch The Price Club

1980 - The Price Company goes public - generates sales of $148 million

1993 - The Price Company merges with Costco Inc. - generating 15.2 billion in combined sales

Membership merchandise concept launches internationally as Sol and Robert Price take membership concept to Asian and Latin American markets.

1995 - Membership shopping warehouses open in Guam and Saipan in Micronesia

1996 - Warehouses open in Panama City, Panama and Medan, Indonesia

1997 - Two warehouses open in Beijing, China and one each in Panama City, Panama and in Jakarta, Indonesia

1997 - PriceSmart traded on NASDAQ under the symbol "PSMT"

1998 - PriceSmart enters joint venture agreements to open warehouses in Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, and Nicaragua

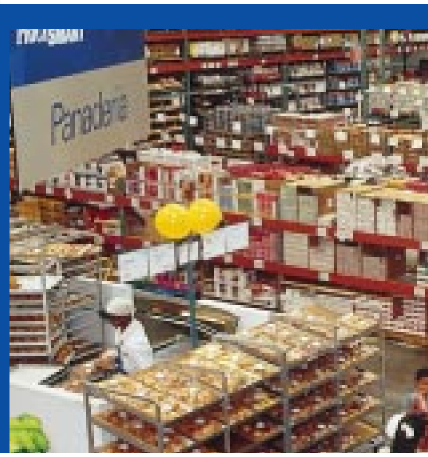
International Membership Merchandising in U.S.-Style Shopping Warehouses

A PriceSmart card allows access to American Warehouse Shopping. The right way to shop for...

- **Low Prices**
  On American, international and local products
- **High Quality**
  Merchandise and services
- **Excellent Value**
  On name-brand products for less

PriceSmart products and services include

Clothing	Groceries
Electronics	Fresh Beef, Poultry, Fish
Business Supplies	Quality Produce
1 Hour Photo	Frozen Foods
Tire Centers (select locations)	Fresh Hot Bakery
Home Furnishings	Rotisserie Chicken
Health & Beauty Aids	New York-Style Fresh Pizza
Snacks & Beverages	Deli



The Travel Program

The Company's Travel Program offers discounted prices on cruises, travel packages, car rentals, hotels and airline tickets. The Company's operating strategy is based on generating a large sales volume rather than high margins on individual sales. The Company has been successful in obtaining discounts not available to most travel agencies because of the large volume of reservations made through the Company's Travel Program. The Company's strategy allows it to satisfy its customers' demands for low-price travel products, while the Company benefits from higher commissions and additional incentives available to high-volume travel agencies.

www.*psvacations*.com   www.costcotravel.com

The Auto Referral Program

The Company's Auto Referral Program offers Costco members a low-price, "no-hassle" alternative for buying a new car. The Company has established relationships with approximately 1,600 new car dealerships in Costco markets in the United States. Under the Company's program, customers are given the opportunity to meet with selected sales representatives at participating dealerships and to purchase cars based on a fixed price.

The Company recently announced the sale of the Auto Referral Program, effective November 1, 1999. The Company will continue to own and manage the program through October 31. 1999.

www.costcoauto.com

"Vacations Magazine" is a traveler's guide to savings and features interesting destination editorials and useful travel tips.

"Travel Magazine" features discounts at hundreds of preferred travel partners across the nation. Six million copies are distributed annually through Costco locations in the United States.

Direct mail advertising for auto and travel programs reach two million Costco members a month.

"Ventajas" is the exclusive magazine for PriceSmart member-customers in Latin America.

PriceSmart brings

Value, Distribution Know-How and U.S.-Style Management to

Concept and Store Operations

- U.S.-style, volume-driven store operations concept with low prices, quality merchandise and excellent value
- A market approach that stands for value
- U.S. brand identity
- U.S.-style management, expertise and personnel training techniques
- Strategically focused marketing programs targeted at capturing membership and stimulating sales growth
- State of the art technology with efficient operating systems

Technology

- Integrated operations, merchandise, membership accounting and financial reporting systems
- Specialized store design and construction methods

Merchandise

- U.S. and international product sourcing
- Merchandise selection specifically focused on the needs of member-customers in the local marketplace
- High-quality, value-based PriceSmart-branded products
- Low-cost, efficient product sourcing and distribution

Distribution

Through product consolidation, buying in bulk and using the right transportation vehicle for each given situation, we are able to manage transportation costs. PriceSmart's team of distribution and transportation specialists implement:

- Streamlined supply chain management
- Utilization of technology and electronic data interchange from vendor to selling outlet
- Training program for distribution facility management
- Efficient low-cost approach to handling "floor-ready" merchandise
- Evaluation and analysis of local distribution environment
- Assistance in international transportation negotiations
- Assistance in export and import regulations, requirements and procedures

Sourcing - Our Commitment to Buying Right

To deliver value, it is essential for us to obtain merchandise at low cost from suppliers. As such, merchandise programs are tailored to each market based on member-customer demands.

Our strategy is to provide high-quality merchandise, excellent value and low prices.

A New Concept in Emerging Markets

PriceSmart is an American style shopping warehouse designed for the growing economies of Latin America and Asia. The PriceSmart target customer group is the rapidly emerging consumer class who purchases supplies for business and consumer products for family and personal use. The product mix includes high-quality U.S. brand name, private label and locally-sourced merchandise that appeals to all consumers, government agencies and large business groups, making for a rather broad customer base.

PriceSmart is positioned to respond to the needs of a rapidly emerging consumer class with a higher income level, those oriented toward value pricing and convenience, and consumers with an increased desire for U.S. goods and services.

PriceSmart's American warehouse-style shopping is the right way to shop for high-quality, name-brand products and services for less.

the International Marketplace

Selling and Operations

We combine our innovative approach to selling and operations with our local joint venture partner's expertise to create an appropriate and efficient system to better serve our local member-customers. The PriceSmart operations team provides expertise and assistance through:

- Teaching a sound operational philosophy
- Establishing an operating format that can be implemented quickly and efficiently
- Eliminating the need for intermediate storage and inventory on most items
- Implementing cost controls for a low cost operating business, with the potential of yielding superior financial benefits
- Controlling operating expenses, facility cost and shrink using our "low-cost operator" philosophy
- Designing and developing a merchandise mix allowing for a low margin price structure that passes savings on to the customer
- Providing training programs and material
- Providing assistance through in-country high-level management
- Providing continuous review of business by senior management

Unique Challenges

Every country and market presents unique challenges and opportunities. As a merchandise business, our ability to respond to local needs is vital. PriceSmart's expansion strategy clearly recognizes this need for local expertise, and the key to the success of the PriceSmart concept is the marriage and on-going cooperation between PriceSmart, our joint venture principals and local suppliers.

The membership merchandising business was founded based on

"The Six Rights of Merchandising"

The PriceSmart concept utilizes a simple set of fundamentals created by Sol Price called "The Six Rights of Merchandising." The Six Rights were first applied in every aspect of the business in 1954, when Sol Price founded FedMart, and again in 1976 at Price Club. The Six Rights continue to provide the basis of our merchandising philosophy and business practices and are emphasized in operations at all levels.

Our merchandising philosophy, very simply stated, requires that we have the Right Merchandise, in the Right Place, at the Right Time, in the Right Quantity, in the Right Condition, at the Right Price.

We are dedicated to providing:

The Right Merchandise
High-quality, U.S. brand name and private label merchandise augmented with key locally sourced products.

The Right Place
Strategy, systems and standards for placement of merchandise on the sales floor to maximize sales, provide security, and reduce labor costs of handling and storage.

The Right Time
Utilize technology throughout the distribution and sales process to maintain in-stock and avoid over-stock conditions. Stocking seasonal merchandise "in" and "out" early to prevent surplus after season's end.

The Right Quantity
Implement and utilize just-in-time flow of product concept when ordering and purchasing to maintain the delicate balance between having too much or too little merchandise on hand.

The Right Condition:
Merchandise will be premarked in the appropriate language and prepared for handling at the selling location. Warehouse store displays, signs and fixtures will not be broken, soiled or damaged.

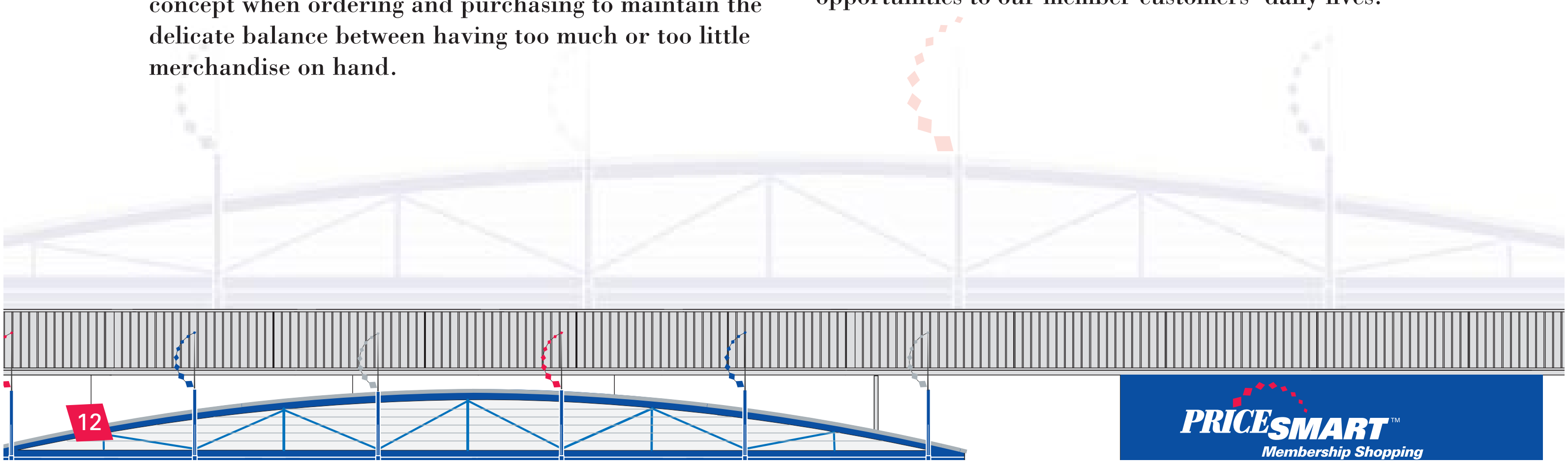
The Right Price:
A purchasing strategy to assure low pricing through volume buying. High value is presented to our member-customers by reducing expenses associated with merchandise handling, on-hand inventory, in-store stocking personnel and large facility costs. Merchandise will be priced competitively and featured to emphasize our strengths allowing the business to operate on a small markup structure while retaining profitability.

Besides years of experience in buying and operations, we also bring:

The Right Service
PriceSmart will meet or exceed customer expectations with an emphasis on delivering quality and creating a positive shopping experience.

What is Right for the Member-Customer
Focusing on "The Six Rights of Merchandising" allows PriceSmart to bring value to the marketplace. In everything we do and say, our commitment to our member-customers, joint venture principals and suppliers is unwavering.

We strive to introduce new and innovative products and businesses that bring value and new opportunities to our member-customers' daily lives.



Financial Information

Selected Financial Data (In Thousands, Except Earnings Per Share)

Prior to fiscal year 1997, the Company operated as certain subsidiaries of PEI. Accordingly, the financial data of the Company during each of the four fiscal years ended August 31, 1997 included herein has been prepared on a historical basis as though the Company had been a stand-alone business operating the businesses and the assets acquired as a result of the Distribution. See Footnote 1 of "PriceSmart, Inc., Notes to Consolidated Financial Statements" included in this report for a description of the businesses and the assets included in PriceSmart's historical financial statements. The Company has independently owned and operated its businesses throughout fiscal 1998.

The following table sets forth selected historical financial data of the Company for the five fiscal years ended August 31, 1998. The selected historical financial data as of August 31, 1998, 1997, 1996, and 1995, and for each of the four years ended August 31, 1998, have been derived from the audited financial statements of the Company. The selected historical financial data as of August 31, 1994 has been derived from the unaudited books and records of the Company, and in the opinion of management, includes all adjusting entries (consisting of only normal and recurring adjustments) necessary to present fairly the information set forth therein.

	Fiscal Years (1)				
	1998	1997	1996	1995	1994
Income Statement Data:					
Merchandise sales (2)	$ 81,100	$ 59,042	$ 36,211	$ 66,573	$ 53,015
International royalties and fees	2,720	3,139	2,164	553	-
Auto, travel and other program revenues	13,368	12,194	9,875	8,769	5,846
Cost of goods sold (2)	74,684	55,947	34,644	62,756	49,449
Selling, general and administrative (3)	26,854	26,607	31,069	33,337	15,095
Operating loss	(4,350)	(8,179)	(17,463)	(20,198)	(5,683)
Real estate operations, net income (loss) (4)	1,532	(1,480)	(8,359)	(2,238)	(16,354)
Interest and other income, net (5)	5,960	2,717	7,663	6,031	6,636
Income (loss) before provision (benefit) for income taxes	3,142	(6,942)	(18,159)	(16,405)	(15,401)
Net income (loss)	3,028	(24,843)	(11,423)	(12,517)	(9,087)
Earnings Per Share:					
Basic (6)	$ 0.51	$ (4.20)	$ (1.93)	$ (2.12)	$ (1.54)
Diluted (6)	0.50	(4.20)	(1.93)	(2.12)	(1.54)
Balance Sheet Data:					
Cash and equivalents	$ 8,643	$ 58,383	$ -	$ -	$ -
Marketable securities	56,133	-	-	-	-
Total assets	124,576	125,885	97,981	107,085	188,431
Stockholders' equity (7)	103,081	107,172	86,990	92,556	129,389

(1) Effective September 1, 1997, the Company changed its 52/53 week fiscal year which ends on the Sunday nearest August 31 to a fiscal year end of August 31. For ease of presentation, all fiscal years in this report are referred to as having ended on August 31.

(2) Merchandise sales and cost of goods sold relate to international and electronic merchandising businesses.

(3) Prior to fiscal year 1998, PEI provided administrative services to the Company. Amounts allocated to the Company for corporate administrative expenses for fiscal years 1997, 1996, 1995, and 1994 were $1,065, $1,350, $1,363, and $752, respectively.

(4) Real estate operations relate to properties held for sale which were transferred to PriceSmart in connection with the Distribution and reflect rental revenue, rental expenses, gain or loss on sales of properties and provisions for asset impairment related to these properties.

(5) Interest and other income includes interest income, loss on sale of investment, equity in the income and losses of international joint ventures and minority interest of partners in merchandising joint venture businesses.

(6) For each of the fiscal years 1994 through 1997, earnings per share is based on the 5,908,235 shares issued in connection with the Distribution.

(7) Prior to fiscal year 1998, stockholders' equity represents the net assets transferred and the earnings of the businesses and assets comprising PriceSmart on a historical basis.

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis compares the results of operations for the three fiscal years ended August 31, 1998, and should be read in conjunction with the consolidated financial statements and the accompanying notes included elsewhere in this report. All dollar amounts are in thousands.

	August 31,		
Store Locations	1998	1997	1996
Joint Ventures	2	1	-
Licensees	3	5	2
Total	5	6	2

The Company had three new locations open in fiscal 1998: one under a joint venture arrangement in Panama and two owned and operated by licensees, one in China and one in the Philippines.

The Asian financial crisis resulted in store closures in Guam and the Philippines and the termination of the Indonesian licensing arrangement (two stores).

The Company recently completed two new joint venture arrangements to open a total of 11 new stores in six Latin America countries. See - "Liquidity and Capital Resources."

Merchandise Sales

	International				Electronic Shopping	
	Store Sales	Percent Change	Export Sales	Percent Change	Sales	Percent Change
Fiscal 1998	$ 48,287	122%	$ 32,813	-10%	$ -	-100%
Fiscal 1997	21,750	100%	36,335	43%	957	-91%
Fiscal 1996	-	-	25,441	-	10,670	-

Store Sales- During fiscal 1998, store sales increased due to the opening of a second store in Panama in December 1997 and increased sales from the first Panama store, which was open for the full year. During 1997, store sales were from the first store which opened in Panama in October 1996.

Export Sales - During fiscal 1998, export sales to licensees and trade sale customers decreased, primarily due to the Asian economic crisis, and the decision in 1997 to discontinue the export trading business, which had been selling U.S.-sourced goods to customers in Hong Kong and Mexico. Export sales decreased to licensees in Guam, Indonesia and the first China location. The decreased sales were partially offset by sales to new locations in Philippines and China, and increased sales to Saipan.

During fiscal 1997, export sales increased primarily due to sales to new licensee stores in Indonesia (2 stores), and China and increased sales to Saipan and Guam.

Electronic Shopping Sales - Electronic shopping sales were reduced to zero in fiscal 1998, because the business was discontinued in fiscal 1997. Fiscal 1997 sales declined sharply from 1996 because the business was closed in January 1997.

Merchandise Gross Margin

	International						Electronic Shopping		
	Store Gross Margin	Percent Change	Percent of Sales	Export Gross Margin	Percent Change	Percent of Sales	Gross Margin	Percent Change	Percent of Sales
Fiscal 1998	$ 5,671	140%	11.7%	$ 745	-52%	2.3%	$ -	-100%	-
Fiscal 1997	2,364	100%	10.9%	1,567	58%	4.3%	(836)	-245%	-87.4%
Fiscal 1996	-	-	-	992	-	3.9%	575	-	5.4%

Store Gross Margin - During fiscal 1998, store gross margin dollars and percentage increased primarily due to higher store sales.

Export Gross Margin - During fiscal 1998, export gross margin percentage decreased by 2% due to lower export sales that have higher gross margin percentage.

During fiscal 1997, export gross margin increased due to higher export sales, described above, and due to a slightly higher gross margin percentage.

Electronic Shopping Gross Margin - During fiscal 1997, gross margin was negatively impacted by reserves of $0.9 million associated with markdowns to sell certain returned and discontinued merchandise.

Other Revenues

	International Royalties & Fees	Percent Change	Auto Referral, Travel and Other Programs	Percent Change
Fiscal 1998	$ 2,720	-13%	$ 13,368	10%
Fiscal 1997	3,139	45%	12,194	23%
Fiscal 1996	2,164	-	9,875	-

During fiscal 1998, international royalties and fees decreased due to reduced know-how and construction fee income; partially offset by increased royalty income generated from higher store sales at licensed locations and increased membership income from Panama. Increased sales for the Auto Referral, Travel and other programs was due to increased Auto Referral advertising revenue resulting from more Costco locations, and increased travel commissions on car rentals and cruises.

During fiscal 1997, international royalties and fees increased primarily as a result of the newly established licensee operations in China (Beijing). With respect to the Auto Referral, Travel and other programs, increases in cruise sales to Costco members and increases in car rental referral commissions accounted for substantially all of the revenue increase.

Selling, General and Administrative

	International	Percent Change	Electronic Shopping	Percent Change	Auto Referral, Travel and Other Programs	Percent Change
Fiscal 1998	$ 12,773	12%	$ -	-100%	$ 10,552	7%
Fiscal 1997	11,400	39%	4,296	-64%	9,846	4%
Fiscal 1996	8,196	-	12,098	-	9,425	-

During fiscal 1998, international expenses increased due to the addition of a second store in Panama (opened December 1997) and a full year of operations for the first Panama location (opened October 1996). These increased expenses were partially offset by decreases in home office international expenses, including the reversal of $.7 million of prior year’s reserve for doubtful accounts receivable. Auto Referral, Travel Program and other expenses increased by 7% as a result of additional staffing and related overhead expense required to support the 10% increase in revenues. Electronic shopping expenses were eliminated in fiscal 1998 due to discontinuing the business in fiscal 1997.

During fiscal 1997, international expenses increased largely due to increased staffing, higher travel expenses to support the needs of licensees in Indonesia and China (Beijing), establishment of a reserve for doubtful accounts and expenses related to the Company's pursuit of international licensing opportunities in additional countries. At the end of fiscal 1996, expenses associated with the electronic shopping program began to decline significantly upon the expiration of certain contractual obligations to pay Costco $4.5 million per year for marketing-related activities and location rent expense. Auto Referral and Travel Program expenses were generally consistent with the prior year's comparable period as expansion of the car rental referral and Costco cruise programs did not generate any significant increase in expenses.

Corporate Administrative Expenses

	Amounts	Change	Percent Change
Fiscal 1998	$ 3,529	$ 2,464	231%
Fiscal 1997	1,065	(285)	-21%
Fiscal 1996	1,350	-	-

During fiscal 1998, corporate administrative expenses increased due to additional salaries, benefits and other expenses associated with becoming a separate, publicly held company and increased marketing salaries and related expenses. Prior to fiscal 1998, the Company operated as certain subsidiaries of PEI. Certain general and administrative costs of PEI were allocated to the Company, principally based on PEI's specific identification of individual cost items or otherwise based upon estimated levels of effort devoted by its general and administrative departments to individual entities or relative measures of size of entities. During fiscal 1997, corporate expenses decreased primarily due to a decrease in legal fees.

Real Estate Operations (Net)

	Revenues	Expenses	Gain On Sales	Provision for Asset Impairment	Total
Fiscal 1998	$ 1,791	$ (1,185)	$ 926	$ -	$ 1,532
Fiscal 1997	3,031	(2,900)	389	(2,000)	(1,480)
Fiscal 1996	2,798	(3,355)	240	(8,042)	(8,359)

Real estate operations relate to properties held for sale which were transferred to the Company in connection with the Distribution and reflect rental revenue, operating expenses, gain or loss on sales of properties and provisions for asset impairment related to these properties. The Company expects the remaining properties to be sold during fiscal 1999.

The increase in net income from real estate operations in fiscal 1998 was primarily due to increased gains on sales of properties and no additional provision for asset impairment. The improvement also reflects reduced operating expenses resulting from the disposition of non-income producing properties. During fiscal 1997 and 1996, the non-cash charges for provision for asset impairment reflected in the table above were taken to write down the carrying value of real estate properties which were being held for sale and which are expected to generate net sales proceeds below their book values.

Other

Interest Income. Interest income for the Company reflects earnings on marketable securities, cash balances, City Notes and certain secured notes receivable from buyers of formerly owned properties. During fiscal 1998, interest income increased primarily due to increased balances in cash and marketable securities. Interest income for fiscal 1997 declined primarily as a result of principal repayments of specific City Notes during fiscal 1997.

Minority Interest. For fiscal 1998 and 1997, minority interest relates to an allocation of the Panama joint venture earnings to the 49% partner in this venture. During fiscal 1996, minority interest represents the allocation of losses on the international merchandising business to Costco until the time that the cumulative amount of such losses equaled the cumulative amount of Costco's capital contributions. Once the book value of Costco's investment reached zero during the third quarter of fiscal 1996, the Company began to absorb 100% of losses from these joint ventures which were funded with stockholder advances by the Company and borrowings from PEI.

Provision (Benefit) For Income Taxes. The Company’s provision for income taxes decreased to $114,000 in fiscal 1998 from $17.9 million in fiscal 1997. In fiscal 1998, the provision for income taxes relates to foreign taxes on the profit of the Company’s Panama joint venture. In fiscal 1997, deferred tax assets of approximately $22.0 million were charged to income tax expense because the realization of deferred tax assets is no longer more likely than not, and therefore, a valuation allowance was established. As of August 31, 1998, the Company has Federal and California net operating loss carryforwards of approximately $29 million and $10 million, respectively. The Federal and California tax loss carryforwards will begin expiring in 2010 and 2001, respectively, unless previously utilized.

Liquidity and Capital Resources

Cash provided by (used in) the Company's operations for the fiscal years ended August 31, 1998, 1997 and 1996 was $(1.6) million, $2.6 million and $(7.9) million, respectively.

The Company expects to satisfy short-term liquidity requirements through its cash and marketable securities, cash from operations of the Company's businesses, and principal and interest payments on the City Notes and other note receivable. The Company also expects to generate cash from sales of the properties held for sale. Certain borrowings by the Company's joint ventures, secured by assets of the joint ventures discussed below, are anticipated.

In 1998, the Company announced programs to repurchase up to 700,000 shares of the Company's common stock. Prior to year-end, 550,000 shares under this program had been repurchased at a cost to the Company of $8.6 million. In September 1998, the Company repurchased the remaining 150,000 shares for $2.3 million.

In November 1998, the Company announced that it would use up to an additional $5.0 million to repurchase shares of the Company's common stock from time to time in blocks of 50,000 shares or more.

In July 1998, the Company entered into an agreement with a Guatemalan headquartered company to form a new joint venture that plans to open two PriceSmart membership shopping warehouses in Guatemala. It is anticipated that the stores will be built in a "build to suit" arrangement with local landowners. The total cost of the project is approximately $6.7 million of which $4.6 million has been contributed in cash by the partners and $2.1 million will be borrowed. PriceSmart owns 66% of this venture.

In September 1998, the Company entered into a joint venture agreement with PSC, S.A., whose stockholders are Latin American businessmen, to open nine PriceSmart membership shopping warehouses in Costa Rica, the Dominican Republic, El Salvador, Honduras, and Nicaragua. The total cost of the project is approximately $84.4 million of which $33.8 million will be contributed in cash by the partners and $50.6 million will be borrowed. PriceSmart owns 60% of this venture.

In September 1998, the Company made a $5.9 million, five year term loan to its Panama joint venture. The loan yields interest at a rate of 3-month LIBOR + 1 3/4%. Loan proceeds were used to repay Panama's bank borrowings of $3.7 million, with the remaining portion to be used in future business opportunities.

Additionally, the Company estimates that it will spend approximately $.3 million for central office fixtures and equipment, and $10 million for business opportunities that may arise. Actual capital expenditures, investment in merchandising businesses and net proceeds realized from property sales for fiscal 1999 may vary from estimated amounts depending on business conditions and other risks and uncertainties to which the Company and its businesses are subject.

The Company believes that its cash balances, marketable securities and net cash provided by operating activities, principal and interest payments on notes receivable and sales of its properties held for sale and bank borrowings will be sufficient to meet its working capital expenditure requirements for at least the next 12 months. Management intends to invest the Company's cash in excess of current operating requirements in short-term, interest-bearing, investment-grade securities.

In August 1998, the company entered into an agreement to sell the Company's Auto Referral Program, effective November 1, 1999. The Company will continue to own and operate the Program through October 31, 1999 delivering automotive referral services to Costco members. The Program was sold for a net gain of $.4 million.

Certain Asian markets served by the Company have experienced a significant devaluation of local currencies relative to the U.S. dollar. Because the Company transacts its business in the Asian markets in U.S. dollars, the Company does not bear exchange rate risk. However, devaluation of local currencies relative to the U.S. dollar causes U.S. merchandise to be less affordable, and generally has a negative impact on the Company's sales of U.S.-sourced goods to the affected markets, location sales and royalty income. The Company's licensees in Indonesia and Guam were particularly affected by the economic crisis, which largely contributed to the cancellation of the Indonesian license agreement and the closing of the Guam store in fiscal 1998. Neither of these issues resulted in a material economic loss to the Company.

The Company has an immaterial risk of loss in certain markets most affected by the Asian economic downturn discussed above, as these are licensing arrangements.

In November 1998, Honduras and Nicaragua were severely damaged by a hurricane. It is unclear to what extent the storm damage will impact the Company's planned expansion in these countries.

Seasonality

Historically, the Company's merchandising businesses have experienced moderate holiday retail seasonality in their markets. In addition to seasonal fluctuations, the Company's operating results fluctuate quarter-to-quarter as a result of economic and political events in markets served by the Company, the timing of holidays, weather, timing of shipments, product mix, and cost of U.S.-sourced products. Because of such fluctuations, the results of operations of any quarter are not indicative of the results that may be achieved for a full fiscal year or any future quarter. In addition, there can be no assurance that the Company's future results will be consistent with past results or the projections of securities analysts.

Impact of Year 2000

The year 2000 issue results from computer programs and hardware being written with two digits rather than four digits to define the applicable year. As a result, there is a risk that date sensitive software may recognize a date using "00" as the year 1900, rather than the year 2000. This potentially could result in system failure or miscalculations causing disruptions of operations, including a temporary inability to process transactions or engage in normal business activities.

The Company has already received letters of year 2000 compliance from its key hardware and software vendors regarding the Company's core transaction processing systems, including both the point of sale and back room processes. In addition, the Company plans to conduct its own internal testing of year 2000 compliance by February 1999. Further, certain custom programs are planned to be modified by February 1999. The total cost of the year 2000 project is not expected to exceed $100,000, which excludes the cost of the recently purchased hardware and software, which was already 2000 compliant.

The Company plans to initiate formal communications with its significant suppliers and customers regarding year 2000 compliance. However, the Company's systems interface with its suppliers is minimal, which makes the Company less vulnerable.

The costs of the year 2000 project and the estimated completion date are based on management's best estimates, which are derived utilizing numerous assumptions. However, there can be no guarantee that these estimates will be achieved and actual results could differ materially from the estimates. Specific factors that might cause material differences include, but are not limited to, the availability and cost of trained personnel, the ability to locate and correct all relevant computer codes, and similar uncertainties.

Quantative and Qualitative Disclosures About Market Risk.

Not Applicable.

Financial Statements

PriceSmart, Inc.
Index to Financial Statements

Report of Ernst & Young LLP, Independent Auditors

The Board of Directors and Stockholders
PriceSmart, Inc.

We have audited the accompanying consolidated balance sheets of PriceSmart, Inc. as of August 31, 1998 and 1997 and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended August 31, 1998. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of PriceSmart, Inc. at August 31, 1998 and 1997 and the consolidated results of its operations and its cash flows for each of the three years in the period ended August 31, 1998 in conformity with generally accepted accounting principles.

San Diego, California
October 16, 1998

PriceSmart, Inc.
Consolidated Balance Sheets
(Amounts in Thousands, Except Share Data)

	August 31, 1998	August 31, 1997
Assets		
Current assets:		
Cash and equivalents	$ 8,643	$ 58,383
Marketable securities	56,133	-
Receivables, net of allowance for doubtful accounts of $414 and $1,000 in 1998 and 1997, respectively	6,503	4,806
Merchandise inventories	9,160	5,518
Prepaid expenses and other current assets	965	578
Property held for sale, net	4,886	19,913
Total current assets	86,290	89,198
Property and equipment:		
Land	2,250	2,250
Building and improvements	6,905	4,578
Fixtures and equipment	6,659	4,712
	15,814	11,540
Less accumulated depreciation	(2,841)	(1,946)
Property and equipment, net	12,973	9,594
Other assets:		
City notes receivable	21,501	23,052
Other notes receivable	3,812	4,041
Total Assets	$ 124,576	$ 125,885
Liabilities and Stockholders' Equity		
Current liabilities:		
Bank borrowings	$ 3,782	$ -
Accounts payable, trade	5,463	4,901
Other payables and accrued expenses	6,622	8,376
Total current liabilities	15,867	13,277
Minority interest	5,628	5,436
Commitments		
Stockholders' equity		
Preferred stock, $.0001 par value, 2,000,000 shares authorized, none issued	-	-
Common stock, $.0001 par value, 15,000,000 shares authorized, 5,453,603 shares outstanding in 1998 and 5,908,235 shares outstanding in 1997, net of 550,000 shares in treasury in 1998	1	1
Additional paid-in capital	100,230	107,171
Notes receivable from stockholders	(697)	-
Unrealized gains on marketable securities	519	-
Retained earnings	3,028	-
Total stockholders' equity	103,081	107,172
Total Liabilities and Stockholders' Equity	$ 124,576	$ 125,885

See accompanying notes.

PriceSmart, Inc.
Consolidated Statements of Operations
(Amounts in Thousands, Except Per Share Data)

	Years Ended August 31, 1998	1997	1996
Revenues			
Sales:			
International	$ 81,100	$ 58,085	$ 25,541
Electronic shopping	-	957	10,670
International royalties and other fees	2,720	3,139	2,164
Auto referral, travel and other programs	13,368	12,194	9,875
Total Revenues	97,188	74,375	48,250
Expenses			
Cost of goods sold:			
International	74,684	54,154	24,549
Electronic shopping	-	1,793	10,095
Selling, general and administrative:			
International	12,773	11,400	8,196
Electronic shopping	-	4,296	12,098
Auto referral, travel, and other programs	10,552	9,846	9,425
Corporate administrative expenses	3,529	1,065	1,350
Total Expenses	101,538	82,554	65,713
Operating Loss	(4,350)	(8,179)	(17,463)
Other			
Real estate operations, net	1,532	(1,480)	(8,359)
Interest income	6,152	2,776	3,076
Minority interest	(192)	(59)	4,587
Total Other	7,492	1,237	(696)
Income (loss) before provision (benefit) for income taxes	3,142	(6,942)	(18,159)
Provision (benefit) for income taxes	114	17,901	(6,736)
Net Income (Loss)	$ 3,028	$ (24,843)	$ (11,423)
Earnings (loss) per share			
Basic	$ 0.51	$ (4.20)	$ (1.93)
Diluted	$ 0.50	$ (4.20)	$ (1.93)
Shares used in per share computation			
Basic	5,912	5,908	5,908
Diluted	6,062	5,908	5,908

See accompanying notes.

PriceSmart, Inc.
Consolidated Statements of Stockholders' Equity
For the Three Years Ended August 31, 1998
(Amounts in Thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Notes Receivable from Stockholders	Unrealized Gains on Marketable Securities	Retained Earnings	Total
Investment by PEI at August 31, 1995	5,908	$ 1	$ 92,555	$ -	$ -	$ -	$ 92,556
Net loss			(11,423)	-	-	-	(11,423)
Net return to PEI	-	-	5,857	-	-	-	5,857
Investment by PEI at August 31, 1996	5,908	1	86,989	-	-	-	86,990
Net loss	-	-	(24,843)	-	-	-	(24,843)
Net return to PEI	-	-	45,025	-	-	-	45,025
Balance at August 31, 1997	5,908	1	107,171	-	-	-	107,172
Issuance of common stock for cash and notes receivable	71	-	1,093	(697)	-	-	396
Exercise of stock options	25	-	214	-	-	-	214
Purchase of treasury stock	(550)	-	(8,643)	-	-	-	(8,643)
Stock based compensation	-	-	395	-	-	-	395
Unrealized gains on marketable securities	-	-	-	-	519	-	519
Net income	-	-	-	-	-	3,208	3,028
Balance at August 31, 1998	5,454	$ 1	$100,230	$(697)	$519	$3,028	$103,081

See accompanying notes.

PriceSmart, Inc.
Consolidated Statements of Cash Flows
(Amounts in Thousands)

	Years Ended August 31,		
	1998	1997	1996
Operating Activities			
Net income (loss)	$ 3,028	$ (24,843)	$ (11,423)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation	1,409	1,374	2,259
Provision for asset impairments	-	2,000	8,042
Provision for doubtful accounts	(586)	1,000	-
Net loss on disposition of property and equipment	111	-	-
Income tax (benefit) charge	114	17,901	(6,736)
Minority interest	192	59	(4,587)
Stock-based compensation	395	-	-
Change in operating assets and liabilities			
Accounts receivable and other assets	(5,140)	(180)	4,332
Accounts payable and other liabilities	(1,104)	5,241	209
Other	(44)	-	-
Net cash flows provided by (used in) operating activities	(1,625)	2,552	(7,904)
Investing Activities			
Purchases of marketable securities	(86,378)	-	-
Sales of marketable securities	30,801	-	-
Additions to property and equipment	(5,094)	(8,131)	(2,560)
Proceeds from sale of property and equipment	-	97	147
Additions to notes receivable	-	-	(1,337)
Payments of notes receivable	1,780	8,614	3,105
Net cash flows provided by (used in) investing activities	(58,891)	580	(645)
Financing Activities			
Change in property held for sale	15,027	6,594	(190)
Proceeds from bank borrowings	3,782	-	-
Proceeds from exercise of stock options	214	-	-
Issuance of common stock for cash and notes receivable	396	-	-
Purchases of treasury stock	(8,643)	-	-
Net investment by PEI	-	45,025	6,994
Contributions by Panama JV partner	-	3,632	1,745
Net cash flows provided by financing activities	10,776	55,251	8,549
Net increase (decrease) in cash	(49,740)	58,383	-
Cash and equivalents at beginning of year	58,383	-	-
Cash and equivalents at end of year	$ 8,643	$ 58,383	$ -

See accompanying notes.

PriceSmart, Inc.
Notes to Consolidated Financial Statements

Note 1 – Organization and Basis of Presentation

Formation of the Company

PriceSmart, Inc. ("PriceSmart" or the "Company") owns and operates certain merchandising businesses. The Company's primary business is international merchandising consisting of membership shopping stores similar to, but smaller in size than, warehouse clubs in the United States. As of August 31, 1998, there were three stores licensed to and owned by in-country business people and two stores owned 51% by the Company. Additionally, the Company operates domestic auto referral and travel businesses marketed to Costco members.

In June 1997, the Price Enterprises, Inc. (PEI) Board of Directors approved, in principle, a plan to separate PEI's core real estate business from the merchandising businesses it operated through a number of subsidiaries. To effect such separation, PEI first transferred to the Company, through a series of preliminary transactions, the assets listed below. PEI then distributed on August 29, 1997 all of the Company's Common Stock pro rata to PEI's existing stockholders through a special dividend (the "Distribution").

Assets transferred to PriceSmart were comprised of: (i) the merchandising business segment of PEI; (ii) certain real estate properties held for sale (the "Properties"); (iii) notes receivable from various municipalities and agencies ("City Notes") and certain secured notes receivable from buyers of properties; (iv) cash and cash equivalents of approximately $58.4 million; and (v) all other assets and liabilities not specifically associated with PEI's portfolio of 27 investment properties, except for current corporate income tax assets and liabilities.

Basis of Presentation

The consolidated financial statements include the assets, liabilities and results of operations of the Company and its majority owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

	Ownership	Basis of Presentation
Ventures Services, Inc.	100%	Consolidated
PB Real Estate, S.A.	51%	Consolidated
Price Costco de Panama, S.A.	51%	Consolidated

The financial statements prior to fiscal 1998 present the Company as if it were a separate entity from PEI. PEI's historical basis in the assets and liabilities of the Company have been carried over. Changes in additional paid-in capital represent the net income (loss) of the Company plus the net change in cash and non-cash items transferred between the Company and PEI prior to distribution.

Certain amounts in the prior period financial statements have been reclassified to conform to the current presentation.

Note 2 – Significant Accounting Policies

Fiscal Year

Effective September 1, 1997, the Company changed its reporting periods to 12 months ending August 31, with each quarter consisting of three months. Prior to the change, the Company generally reported 13 periods (ending on the Sunday closest to August 31) of four weeks each, with the first quarter consisting of 16 weeks, and each remaining quarter consisting of 12 weeks.

Cash and Equivalents

Cash and equivalents represent cash and short term highly liquid investments with maturities of three months or less when purchased.

PriceSmart, Inc.
Notes to Consolidated Financial Statements (cont.)

Marketable Securities

In accordance with Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Debt and Equity Securities," marketable securities are classified as available-for-sale. Available-for-sale securities are carried at fair value, with the unrealized gains and losses reported in a separate component of stockholders' equity. The amortized cost of securities in the category is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization is included in interest income. Realized gains and losses in value judged to be other-than-temporary, if any, on available-for-sale securities are included in interest income. The cost of securities sold is based on the specific identification method. Interest and dividends on securities classified as available-for-sale are included in interest income.

The Company invests its excess cash primarily in investment grade debt instruments, marketable debt securities of U.S. government agencies, and high grade commercial paper. Management has established guidelines relative to diversification and maturities that maintain safety and liquidity.

Property and Equipment

Property and equipment are stated at cost. Depreciation is computed on a straight-line basis over the estimated useful lives of the assets, as follows:

Building and improvements	10-25 years
Fixtures and equipment	3-7 years

Merchandise Inventories

Merchandise inventories which include merchandise for resale are valued at the lower of cost (average cost) or market.

Revenues Recognition

The Company recognizes international sales when title passes to the customer. Revenues from the auto referral program are recognized on a monthly basis when billed, pursuant to contracts which are generally month-to-month. Revenues from travel programs are recognized as services are performed.

Income Taxes

Income taxes have been provided for in accordance with SFAS No. 109, "Accounting for Income Taxes." That standard requires companies to account for deferred taxes using the asset and liability method. Accordingly, deferred income taxes are provided to reflect temporary differences between financial and tax reporting, including asset write-downs of real estate and related assets, accelerated tax depreciation methods, and international fees. Additionally, deferred taxes were transferred to the Company as a result of the Costco spin off in 1994.

In fiscal year 1997, the Company was included in the consolidated Federal and in various combined state tax returns of PEI. The Company was allocated the benefit of its tax net operating losses used in PEI's consolidated or combined tax returns. Benefits realized by PEI were not paid to the Company but were deemed to be reductions in PEI's investment in the Company.

Asset Impairment

SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. No such indicators of impairment were present in fiscal 1998 and 1997.

SFAS No. 121 also addresses the accounting for long-lived assets that are expected to be disposed of. The Company estimated the sales value, net of related selling costs, on its real estate properties which are being held for sale and recorded impairment losses of $2.0 million and $8.0 million in fiscal 1997 and 1996 respectively. No impairment losses were recorded in fiscal 1998. See Note 4.

PriceSmart, Inc.
Notes to Consolidated Financial Statements (cont.)

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Concentration of Credit Risk

The Company sells its merchandise primarily to its international licensees. Credit is generally extended based on letters of credit.

Stock-Based Compensation

Stock-based compensation expense is measured using either the intrinsic-value method as prescribed by Accounting Principle Board Opinion No. 25 or the fair-value method described in SFAS No. 123. The Company adopted SFAS No. 123 in fiscal 1997 using the intrinsic-value method; accordingly, there has been no effect on the Company's financial position or results of operations.

Capital Stock

The Company's authorized stock consists of 15 million shares of $0.0001 par value common stock and 2 million shares of $0.0001 par value preferred stock. No preferred stock has been issued. In August 1998, the Board of Directors authorized the repurchase of up to 700,000 shares of its common stock. At August 31, 1998, 550,000 shares have been repurchased at an aggregate cost of $8.6 million.

Earnings (Loss) Per Share

In the second quarter of fiscal year 1998, the Company adopted SFAS No. 128, Earnings per Share. SFAS No. 128 replaced the previously reported primary and fully diluted earnings per share with basic and diluted earnings per share. Unlike primary earnings per share, basic earnings per share excludes any dilutive effects of options, warrants, and convertible securities. Diluted earnings per share is very similar to the previously reported fully diluted earnings per share. Shares used in computing diluted earnings per share include 150,000 shares related to the dilutive effect of stock options. In fiscal years 1997 and 1996, loss per share amounts are based on the 5,908,235 shares issued in connection with the Distribution.

Comprehensive Income and Segment Information

The Financial Accounting Standards Board issued SFAS No. 130, "Reporting Comprehensive Income" and SFAS No. 131, "Segment Information" which are required reporting for the Company in fiscal 1999. SFAS No. 130 requires that all components of comprehensive income including net income be reported in the financial statements in the period in which they are recognized. Comprehensive income is defined as the change in equity during a period from transactions and other events and circumstances. The impact of adopting SFAS No. 130 cannot be determined at this time. SFAS No. 131 amends the requirements to report financial and descriptive information about its reportable operating segments. The financial information is required to be reported on the basis that is used internally for evaluating the segment performance. The Company does not believe that SFAS No. 131 will have a material impact on income or financial statement presentation.

Pre-Opening Costs

The Company capitalizes pre-opening costs related to store openings and amortizes these costs over twelve months. As of August 31, 1998 and 1997, capitalized pre-opening costs totaled $129,000 and $243,000, respectively. The Company is required to adopt Statement of Position 98-5 "Reporting on the Costs of Start-up Activities" in fiscal 2000. The statement requires that pre-opening costs be charged to expense as incurred, and will have the impact of accelerating expense recognition in the year of adoption by a yet undetermined amount.

PriceSmart, Inc.
Notes to Consolidated Financial Statements (cont.)

Note 3 – Marketable Securities

The following is a summary of short-term investments classified as marketable securities as of August 31, 1998 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Values
U.S. Government Securities	$55,614	$519	$ -	$56,133

Gross realized gains and losses were not material during fiscal 1998. As of August 31, 1998, the average maturity for these marketable securities is 17 months.

Note 4 – Property Held For Sale

Property held for sale primarily includes former membership warehouse club facilities and unimproved land, which the Company expects to dispose of in the next twelve months. Property held for sale consists of the following (in thousands):

	August 31, 1998	August 31, 1997
Land and land improvements	$ 3,811	$ 16,181
Building and improvements	1,894	10,120
Deferred rents	-	601
Deferred leasing costs, net	-	423
	5,705	27,325
Accumulated depreciation	(594)	(2,617)
Provision for asset impairments:		
Unimproved land	-	(755)
Properties with buildings	(225)	(4,040)
	(225)	(4,795)
Property held for sale, net	$ 4,886	$ 19,913

Because the properties are held for sale, the net results of the real estate operations are presented on the consolidated statement of operations, and consist of the following (in thousands):

	Years Ended August 31, 1998	1997	1996
Rental income	$ 1,791	$ 3,031	$ 2,798
Gains on sales of real estate	926	389	240
Total revenue	2,717	3,420	3,038
Operating, maintenance and administrative	642	1,690	1,724
Property taxes	421	672	857
Depreciation and amortization	122	538	774
Provision for asset impairments	-	2,000	8,042
Total expenses	1,185	4,900	11,397
Real estate operations, net	$ 1,532	$ (1,480)	$ (8,359)

PriceSmart, Inc.
Notes to Consolidated Financial Statements (cont.)

Provision for asset impairments represent non-cash charges taken to write-down the carrying value of real estate properties which are being held for sale, and which are expected to generate net sales proceeds below their book values.

The Company determines the estimated carrying value of properties held for sale based upon the expected net sales proceeds to be received, taking into consideration existing sales contracts, past and current sales negotiations and relevant market data.

Certain properties held for sale generate future minimum rental income of approximately $.4 million per year. These properties are leased under noncancelable leases with remaining terms ranging from 4 years to 9 years.

Note 5 – City Notes Receivable

The City Notes include amounts loaned to municipalities and agencies to facilitate real property acquisition and improvements and carry interest rates which range from 8% to 10%. Repayment of the majority of these notes is generally based on that municipality's allocation of sales tax revenues generated by retail businesses located on a particular property associated with such City Note. City Note repayments are calculated in accordance with specific revenue sharing agreements; and, under the terms of most City Notes, the unpaid balance of the note is forgiven on its maturity date. The carrying values of these notes was established when PEI was spun out from Costco. The carrying values are evaluated by the Company in accordance with Statement of Financial Accounting Standards (SFAS) No. 114, "Accounting by Creditors for Impairment of a Loan." Interest income is recognized based upon the stated interest rates of the various notes and amounted to $1.9 million, $2.1 million, $2.5 million for the years ended August 31, 1998, 1997 and 1996, respectively. At August 31, 1998 and 1997, the aggregate stated principal value plus compounded interest amounted to $71 million and $67 million , respectively. As a result, the total carrying value of the City Notes is less than the stated principal value and interest by $50 million and $44 million, respectively. As of August 31, 1998, twelve City Notes were outstanding with maturity dates ranging from 1999-2028.

Note 6 – Profit Sharing and 401(k) Plan

Substantially all of the employees of the Company are participants in PriceSmart's defined contribution profit sharing and 401(k) plan. Profit sharing contributions, if any, are based on a discretionary amount determined by the Board of Directors and are allocated to each participant based on the relative compensation of the participant, subject to certain limitations. The Company makes a matching 401(k) contribution equal to 50% of the participant's contribution up to an annual maximum matching contribution of $250.

Profit sharing contributions of approximately $363,000, $406,000, and $158,000 were made for the benefit of PriceSmart plan participants during fiscal 1998, 1997, and 1996, respectively. Employer contributions to the 401(k) plan were approximately $26,000, $24,000, and $31,000 during fiscal 1998, 1997, and 1996, respectively.

Note 7 – Stock Option Plan and Equity Participation Plan

On August 6, 1997, the Company adopted the 1997 Stock Option Plan of PriceSmart, Inc. (the "1997 Plan") for the benefit of its eligible employees, consultants and independent directors. Under the 1997 Plan, 700,000 shares of the Company's common stock are authorized for issuance. The Compensation Committee of the Board administers the Plan with respect to grants to employees or consultants of the Company, and the full Company Board administers the Plan with respect to director options. Options issued under the 1997 Plan typically vest over 5 years and expire in 6 years.

Certain employees and directors of the Company participated in the PEI stock option plan. Upon consummation of the Distribution, the unvested PEI options held by these individuals were canceled. To replace those canceled options, the Company granted options to purchase PriceSmart common stock at share amounts and prices per share so that the employees and directors were in substantially the same economic position as they were prior to the Distribution.

PriceSmart, Inc.
Notes to Consolidated Financial Statements (cont.)

Stock option activity relating to the 1997 Plan was as follows:

	Shares	Weighted Average Exercise Price
Balance at August 31, 1997	-	$ -
Granted	734,500	13.39
Exercised	(24,801)	8.63
Cancelled	(75,963)	10.40
Balance at August 31, 1998	633,736	13.94

As of August 31, 1998, options to purchase 41,662 shares were exercisable under the 1997 Plan. As of August 31, 1998, there were 675,199 shares of Common Stock reserved for future issuance in connection with the 1997 Plan.

The following table summarizes information about stock options outstanding at August 31, 1998:

Range of Exercise Prices	Outstanding as of 08/31/98	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Exercisable as of 08/31/98	Weighted-Average Exercise Price
$7.15 - $8.94	216,177	2.4	$ 8.59	32,146	$ 8.59
8.94 - 10.73	35,893	5.4	9.49	8,273	9.65
10.73 - 12.52	7,093	4.3	11.74	412	11.69
14.30 - 16.09	5,409	7.5	15.21	417	14.69
16.09 - 17.88	369,164	5.3	17.53	414	17.88
$7.15 - $17.88	633,736	4.3	$13.94	41,662	$ 8.98

The weighted-average fair value of the stock options granted during 1998, 1997, and 1996 were $5.04, $3.48 and $2.69, respectively.

Pro forma information regarding net income is required by SFAS 123, and has been determined as if the Company had accounted for its employee stock options under the fair value method prescribed by SFAS 123. The fair value of each option grant is estimated on the date of grant using the "Black-Scholes" option pricing model with the following weighted average assumptions used for grants in fiscal 1998, 1997 and 1996:

	1998	1997	1996
Risk free interest rate	6%	6%	6%
Expected life	3 years	3 years	3 years
Expected volatility	31.5%	26.5%	26.5%
Expected dividend yield	0%	0%	0%

For purposes of pro forma disclosures, the estimated fair value of the options granted is amortized to expense over the options' vesting period. The Company's pro forma information for the years ended August 31, 1998, 1997, 1996 follows:

	1998	1997	1996
Pro forma net income (loss) (in thousands)	$ 2,558	$ (25,002)	$ (11,580)
Pro forma income (loss) per share (diluted)	$ 0.42	$ (4.23)	$ (1.96)

The pro forma effect on net income for 1998 and net loss for 1997 and 1996 is not likely to be representative of the pro forma effect on reported income or loss in future years because these amounts reflect less than full vesting of options granted during these periods.

PriceSmart, Inc.
Notes to Consolidated Financial Statements (cont.)

In August 1998, the Company adopted, subject to stockholder approval, the 1998 Equity Participation Plan (the "Equity Plan") for the benefit of its eligible employees, consultants and independent directors. The Plan authorizes 700,000 shares of the Company's common stock for issuance. Options issued under the 1998 Equity Plan typically vest over 5 years and expire in 6 years. As of August 31, 1998 options to purchase 446,041 shares have been granted, subject to stockholder approval, at an exercise price of $15.50 per share. The stock option data presented above does not include the options to be granted under the Equity Plan.

The Equity Plan also allows the Company to make loans to participants for the purchase of shares or exercise of options. As of August 31, 1998 officer loans outstanding were $697,000. Interest is payable semi-monthly at 6% with the principal due in six years.

Note 8 – Income Taxes

Significant components of the income tax benefit (provision) are as follows (in thousands):

	Years Ended August 31,		
	1998	1997	1996
Current:			
Federal	$ -	$ (3,612)	$ (3,431)
State	-	-	(807)
Foreign	114	-	-
	114	(3,612)	(4,238)
Deferred:			
Federal	-	20,945	(1,935)
State	-	568	(563)
Foreign	-	-	-
	-	21,513	(2,498)
Total provision (benefit)	$ 114	$ 17,901	$ (6,736)

The reconciliation of income tax computed at the federal statutory tax rate to the (provision) benefit for income taxes is as follows (in thousands):

	Years Ended August 31,		
	1998	1997	1996
Federal taxes at the statutory rate	$ 1,068	$ (2,430)	$ (6,355)
State taxes, net of federal benefit	188	(416)	(1,091)
Tax losses (income) of 51% owned subsidiaries	(130)	-	708
Increase (decrease) in valuation allowance for deferred tax assets	(1,027)	20,683	-
All other, net	15	64	2
Total provision (benefit)	$ 114	$ 17,901	$ (6,736)

PriceSmart, Inc.
Notes to Consolidated Financial Statements (cont.)

Significant components of the Company's tax assets as of August 31, 1998 and 1997 are shown below. A valuation allowance has been recognized to offset the deferred tax assets as realization of such assets in uncertain (in thousands).

	August 31, 1998	August 31, 1997
Deferred tax assets:		
Real estate properties	$ 18	$ 6,961
City notes receivable	11,615	12,535
Net operating losses	10,567	5,437
International revenues and expenses	127	228
All other, net	1,677	1,913
Total deferred tax assets	24,004	27,074
Deferred tax liabilities:		
Deferred rental income	-	(261)
Deferred state income taxes	-	(693)
Unrealized gains on marketable securities	(207)	-
Total deferred tax liabilities	(207)	(954)
Valuation allowance	(23,797)	(26,120)
Net deferred tax assets	$ -	$ -

As of August 31, 1998, the Company has federal and California net operating loss carryforwards of approximately $29 million and $10 million, respectively. The federal and California tax loss carryforwards will begin expiring in 2010 and 2011, respectively, unless previously utilized.

Pursuant to Section 382 of the Internal Revenue Code, annual use of the Company's net operating loss carryforwards will be limited because of cumulative changes in ownership of more than 50% which occurred during 1995. However, the Company does not believe such change will have a material impact upon utilization of these carryforwards.

Note 9 – Bank Loan

During fiscal 1998, the Company's Panama subsidiary entered into a seven year bank term loan with an original principal amount of $4.2 million. The loan required minimum monthly payments including principal and interest of $50,000. Interest was payable at LIBOR plus 1.75%. The loan was secured by Panama land and building. Subsequent to August 31, 1998, the loan was repaid in full.

Note 10 – Commitments

The Company leases one of its facilities in Panama under an operating lease which expires in March 2008. Rent expense totaled $580,000 for the year ended August 31, 1998. Future annual lease payments are as follows for each of the next five fiscal years (in thousands):

1999	$ 750
2000	750
2001	750
2002	750
2003	788
Thereafter	3,712
Total	$ 7,500

Note 11 – Sale of Auto Referral Program

In August 1998, the Company entered into an agreement to sell the Auto Referral Program, effective November 1, 1999. The Company will continue to own and operate the Program through October 31, 1999, delivering automotive referral services to Costco members.

Note 12 – Related Party Transactions

As a result of the Distribution to stockholders of the Company and for the purpose of governing certain of the ongoing relationships between the Company and PEI after the Distribution, and to provide mechanisms for an orderly transition, the Company and PEI have entered into various agreements, and have adopted policies, as described below.

The Company and PEI have entered into an Asset Management and Disposition Agreement dated as of August 26, 1997 calling for PEI to provide asset management services with respect to certain properties distributed to the Company. As consideration for such services, the Company pays PEI management fees, leasing fees, disposition fees and developer's fees. Such agreement has a two-year term; provided that either the Company or PEI may terminate the agreement upon 60 days written notice. The Company paid PEI $225,000 in fiscal 1998 in connection with this agreement.

The Company and PEI entered into a Transitional Services Agreement dated as of August 26, 1997 pursuant to which the Company and PEI provided certain services to one another. Fees for such transitional services (which do not include real estate management services) reflect the costs of providing such services, which may include cash management services, certain accounting services, litigation management or any other similar services that the Company or PEI required. There were no significant costs associated with this agreement in fiscal 1998. The Transitional Services Agreement expired June 30, 1998.

The Company and PEI have entered into a Tax Sharing Agreement dated as of August 26, 1997 defining the parties' rights and obligations with respect to tax returns and tax liabilities for taxable years and other taxable periods ending on or before the Distribution Date. In general, PEI was responsible for (i) filing all Federal and state income tax returns of the Company, PEI and any of their subsidiaries for all taxable years ending on or before or including the Distribution Date and (ii) paying the taxes relating to such returns to the extent attributable to pre-Distribution Date periods.

The Company leases 42,000 square feet of office space from PEI to house the Company's headquarters. The Company pays $25,704 per month pursuant to a two-year lease commencing on August 26, 1997 with five renewal options of two years each. On December 1, 1997, the Company and PEI entered into an Office Services Agreement which provided that the Company would provide certain office services (such as receptionist, mail room, telecommunications and voice mail, utilities and copy services) to PEI, which occupies space in the same building, for $13,450 per month for the first nine months and $7,600 per month for the last twelve months of the term of the agreement. On June 1, 1998, PEI and the Company terminated the Office Services Agreement and amended the headquarters lease to provide that PEI would provide office services to the Company for a fee based on a percentage of PEI's estimated expenses for providing such services.

In fiscal 1998, the Company sold a 15-acre property to PEI, for $3,950,000 resulting in a realized gain of $293,000. The sales price was based on an independent appraisal.

In August 1998, the Company repurchased 200,000 shares of common stock from the Sol and Helen Price Trust, of which Sol Price is trustee, at a price of $15.00 per share.

PriceSmart, Inc.
Notes to Consolidated Financial Statements (cont.)

Note 13 – Geographic Areas and Major Customers (in thousands)

	Year Ended August 31,	
	1998	1997
Revenues:		
United States	$ 47,709	$ 51,806
Latin America	49,479	22,569
	$ 97,188	$ 74,375
Operating income (loss):		
United States	$ (4,741)	$ (8,299)
Latin America	391	120
	$ (4,350)	$ (8,179)
Identifiable assets:		
United States	$ 103,778	$ 113,749
Latin America	20,798	12,136
	$ 124,576	$ 125,885

The Latin American operations consist of a 51% interest in a joint venture in Panama whose currency is the U.S. dollar. Foreign operations were not significant in fiscal 1996.

Export sales were approximately $32.8 million, $36.3 million and $25.2 million for fiscal 1998, 1997 and 1996, respectively. Approximate revenues attributable to a single customer represented 28%, 37% and 48% of total revenues for fiscal 1998, 1997 and 1996, respectively.

Market For Common Stock And Related Stockholder Matters

The Company's Common Stock has been quoted and traded on the NASDAQ National market under the symbol "PSMT" since September 2, 1997. As of November 16, 1998, there were approximately 564 holders of record of the Common Stock.

	High	Low
Calendar Quarter - 1997		
Third Quarter		
(beginning 9/2/97)	18.250	15.250
Fourth Quarter	18.875	15.750
Calendar Quarter - 1998		
First Quarter	17.875	16.000
Second Quarter	17.000	15.250
Third Quarter		
(through 8/31/98)	17.563	14.000

The Company has never declared a cash dividend on its Common Stock and does not anticipate doing so in the foreseeable future.

Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Directors

The table below indicates the name, position with the Company and age of each director:

Name	Position with the Company	Age
Robert E. Price	Chairman of the Board	56
Gilbert A. Partida	President, Chief Executive Officer and Director	36
Rafael E. Barcenas	Director	54
Katherine L. Hensley	Director	61
Leon C. Janks	Director	49
Lawrence B. Krause	Director	68

Robert E. Price has been Chairman of the Board of the Company since July 1994 and served as President and Chief Executive Officer of the Company from July 1994 until January 1998. Mr. Price also serves as Chairman of the Board of Price Enterprises, Inc. ("PEI"), having held that position since July 1994, and was President and Chief Executive Officer of PEI from July 1994 until September 1997. Mr. Price was Chairman of the Board of Price/Costco, Inc. ("Costco") from October 1993 to December 1994. From 1976 to October 1993, he was Chief Executive Officer and a director of The Price Company ("TPC"). Mr. Price served as Chairman of the Board of TPC from January 1989 to October 1993, and as its President from 1976 until December 1990.

Gilbert A. Partida has been a director of the Company since July 1997 and has been President and Chief Executive Officer of the Company since January 1998. Mr. Partida was President and Chief Executive Officer of the Greater San Diego Chamber of Commerce from January 1993 until December 1997. Prior to joining the Chamber of Commerce, Mr. Partida was an attorney with the law firm of Gray, Cary, Ames & Frye in San Diego, California from 1987 to 1992.

Rafael E. Barcenas has been a director of the Company since April 1998. Mr. Barcenas has also been a director and officer of PriceCostco de Panama, S.A., and P.B. Real Estate, S.A., which are subsidiaries of the Company, since their formation in September 1995 and July 1997, respectively. Additionally, Mr. Barcenas has been a principal of BB&M International Trading Group, a Panamanian company (which is the 49% owner of both PriceCostco de Panama, S.A. and P. B. Real Estate, S.A.) since March 1995. Mr. Barcenas also has been Vice President of Boyd, Barcenas, S.A., the largest advertising agency in Panama, since April 1971.

Katherine L. Hensley has been a director of the Company since July 1997 and served as a director of PEI from December 1994 until July 1997. She is a lawyer and a retired partner of the law firm of O'Melveny & Myers in Los Angeles, California. Ms. Hensley joined O'Melveny & Myers in 1978 and was a partner from 1986 to February 1992. Ms. Hensley is a trustee of Security First Trust, an open-end investment management company registered under the Investment Company Act of 1940.

Leon C. Janks has been a director of the Company since July 1997 and served as a director of PEI from March 1995 until July 1997. He has been a partner in the accounting firm of Alder, Green & Hasson in Los Angeles, California since 1980. Mr. Janks has extensive experience in domestic and international business serving a wide variety of clients in diverse businesses.

Lawrence B. Krause has been a director of the Company since July 1997. Mr. Krause has been a Professor and the Director of the Korea-Pacific Program at the Graduate School of International Relations and Pacific Studies at the University of California, San Diego since 1986. He became a Professor Emeritus in 1997. Mr. Krause also serves on advisory boards for a number of institutions including the Institute for International Economics, the Korea Economic Institute, the Committee on Asian Economic Studies and the U.S. National Committee for Pacific Economic

Cooperation.

Executive Officers of the Company

The executive officers of the Company and their ages as of November 16, 1998 are as follows:

Name	Position with the Company	Age
Gilbert A. Partida	President and Chief Executive Officer	36
Robert M. Gans	Executive Vice President, Secretary and General Counsel	49
Thomas D. Martin	Executive Vice President	42
Kurt A. May	Executive Vice President and Chief Operating Officer	45
Karen J. Ratcliff	Executive Vice President and Chief Financial Officer	46

Gilbert A. Partida has been a director of the Company since July 1997 and has been President and Chief Executive Officer of the Company since January 1998. Mr. Partida was President and Chief Executive Officer of the Greater San Diego Chamber of Commerce from January 1993 until December 1997. Prior to joining the Chamber of Commerce, Mr. Partida was an attorney with the law firm of Gray, Cary, Ames & Frye in San Diego, California from 1987 to 1992.

Robert M. Gans has been Executive Vice President, General Counsel and Secretary of the Company since August 1997 and was Executive Vice President and General Counsel of PEI from October 1994 until July 1997. Mr. Gans graduated from the UCLA School of Law in 1975 and actively practiced law in private practice from 1975 until 1994. From 1988 until October 1994, Mr. Gans was the senior member of the law firm of Gans, Blackmar & Stevens, A.P.C., of San Diego, California.

Thomas D. Martin has been Executive Vice President of the Company since October 1998 and served as Senior Vice President of the Company since August 1997. Mr. Martin previously had served as Vice President of PEI from August 1994 until July 1997, directing merchandising strategies and product sourcing for its international merchandising business, in addition to managing its trading company activities. Prior to joining PEI as Vice President in August 1994, Mr. Martin served as Vice President of Costco from October 1993 to December 1994 and had served in various management roles for TPC.

Kurt A. May has been Executive Vice President and Chief Operating Officer of the Company since October 1998. Prior to joining PriceSmart, Mr. May was employed by GTE Corporation for twenty-three years, serving in a wide range of functional disciplines including his most recent role as Area President of GTE Wireless since 1995.

Karen J. Ratcliff has been Executive Vice President and Chief Financial Officer of the Company since September 1997. From October 1995 to September 1997, Ms. Ratcliff operated a financial advisory firm in Orange County. From January 1991 to August 1995, Ms. Ratcliff worked for a publicly traded company, Vans, Inc., serving first as Vice President and Controller and, subsequently, as Vice President and Chief Financial Officer. Ms. Ratcliff also spent a number of years working at the Securities and Exchange Commission in Washington, D.C. and at KPMG Peat Marwick. Ms. Ratcliff graduated from California State University at Dominguez Hills in 1983 with Bachelor of Science Degrees in Accounting and Business Information Systems and is a Certified Public Accountant.

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