

Tesco Debuts in U.S. With Bare-Bones Stores

By ELLIOT ZWIEBACH

LOS ANGELES — The British invasion is under way.

Tesco opened five Fresh & Easy Neighborhood Markets in Southern California last week, seven days after a soft opening of its first U.S. store in Hemet, Calif., about 100 miles southeast of here.

The company is scheduled to open five stores this week in Las Vegas and one in Chula Vista, near San Diego, with stores due in Phoenix later this year.

Tesco said it is looking at locations in Northern California, following reports it has already begun signing leases in the San Jose, Sacramento and Oakland areas while also considering sites in central California and Reno, Nev.

Each Fresh & Easy Neighborhood Market is 10,000 square feet, with a heavy emphasis on fresh produce and other perishables, including a wide selection of chilled meals to go. All the locations have a similar layout, a Tesco spokesman told *SN*.

The stores have a deliberately low-cost look — to reflect their everyday-low-pricing approach — featuring warehouse-style shelving for groceries, exposed ceilings and cement floors painted gray. Walls painted in different

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combinations of pastel blues, tans, greens and other soft hues add splashes of color.

Observers told *SN* that the limited product offering and low pricing levels at Fresh & Easy are closer to a Trader Joe's than to a supermarket. Both companies' stores offer a mix of branded and private-label items, with private label accounting for about 50% of the 3,500 SKUs at Fresh & Easy, compared with 80% of the 3,600-item offering at Trader Joe's.

Prices are about 2%-3% higher than Wal-Mart, but less than supermarkets, a store employee said.

Perishables at Fresh & Easy are positioned around the perimeter, with produce and fresh-cut flowers on one wall; chilled entrees and soups, desserts and baked goods on another wall; and frozen entrees, vegetables and desserts on a third wall. Most of a fourth wall is devoted to health and beauty care items.

Produce is located along the wall adjacent to the stores' entrance, displayed on racks that are neither chilled nor refrigerated, with each item in individual modular tubs.

Most produce is sold in multi-packs.

Stores have eight gondolas: five with 5-foot-high, warehouse-style shelving for dry groceries — most of which are displayed in cut cases — and a smattering of general merchandise (including energy-saving lightbulbs and batteries), plus three refrigerated cases closest to the store's

entrance displaying packaged produce, packaged meats and seafood, sliced meats and cheeses, and dairy items.

A demonstration counter, called "The Kitchen Table," is situated at the end of the produce section, offering samples of hot and cold foods, including private-label grocery items. It is the store's only service area.

Each store has eight checkstands — all exclusively self-checkout — that accept cash or credit cards but no checks.

Endcaps at the front of the store feature grab-and-go items, including sandwiches, salads and sushi. Endcaps in other sections feature seasonal items and specials advertised in the company's biweekly flyer.

The Hemet store, which opened a week early to help the company work out any bugs, was short on some products, with several spaces in the shelf displays sporting tags that read, "New product coming."

One industry observer who visited the Hemet store said he was not impressed with the grocery offering, "which reminded me of a 7-Eleven — runs of short and tall packages, in a random order, seemingly based on whatever would fit."

He said Fresh & Easy is unlikely to pose a serious threat to supermarket operators, adding that he believes the chain's small-format stores are a stalking horse for Tesco's ultimate plans to build full-size supermarkets in the U.S.

Industry sources said they expect Tesco to achieve

U.S. sales of \$2.3 billion to \$2.7 billion by the end of next year, when the company is expected to be operating more than 100 stores in California, Arizona and Nevada, and \$4.5 billion by the end of 2009, with market shares ranging from 1% to 4% in the Southwest over that period.

Perry Caicco, an analyst with CIBC World Markets, Toronto, said at least 40% of Fresh & Easy sales are likely to come at the expense of convenience stores and restaurants, "so the direct impact on the supermarket industry will be modest."

He said he expects gross margins to exceed 32%, "and Tesco [will] need enough regular drawing power to sustain sales at over \$12 per [square] foot per week; otherwise, it's simply not worth the trouble."

David McCarthy, London-based managing director for Citigroup Global Markets, New York, said he expects Tesco's U.S. stores will achieve sales of about \$20 per square foot per week or more, compared with a norm closer to \$10 per square foot per week

Continued on Page 46 for most U.S. food retailers and \$25 for Trader Joe's.

He also said he believes the 10,000-square-foot Fresh & Easy stores will match the sales of a typical U.S. supermarket of 20,000 to 25,000 square feet.

Neil Currie, an analyst with UBS New York, said Tesco tipped the odds in its favor for a successful U.S. operation by choosing the West Coast as its entry point, "because it is a large,

demographically attractive market; because the structure of the market is still relatively immature, with few supercenters and therefore generally high prices for Tesco to under-shoot; and because Californians tend to be early adopters of new retail formats.”

Herb Sorensen, global scientific director for shop-

per insights at TNS North America, said he expects Tesco to succeed because its format will be more attractive to consumers than that of supermarkets.

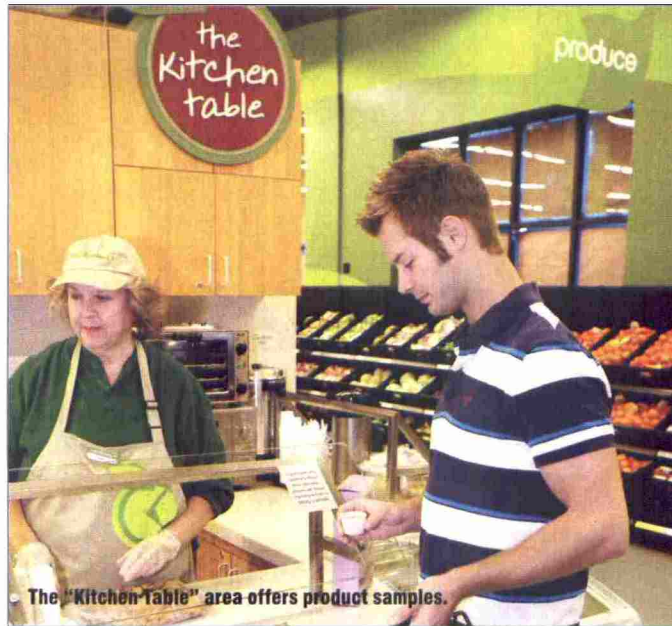
Noting that half of shoppers buy fewer than five items on an average trip to the supermarket, Sorensen said, “Supermarket operators challenge consumers

to come in and find what they can, with the hope they will buy more while they look for what they really want.”

By reducing the selection, he explained, Tesco is making it easier for consumers to find what they want quickly.



Baked goods and other products are positioned as healthful.



The “Kitchen-Table” area offers product samples.



Fresh & Easy merchandises produce in pre-packaged containers.