

Tesco – analysing the environment essay sample



Tesco is one of Britain's leading food retailers and has 586 stores though out Great Britain. From 1992 Tesco has grown greatly and has increased its market share from 10.4% to 15.2%. This increase in customers has also given Tesco a large amount of profit.

Tesco has 164,500 shareholders. Tesco's profit is about 505 million pounds after the tax has been deducted; about 50% of this is then distributed to the shareholders as dividends. The rest roughly 250 million pounds is held back for investment in stores and improving services for the customers. The average shareholder holds between one and one thousand shares, but also a large amount of shares are held by banks, pension funds and building societies. Tesco's share prices have risen since February 1997 when it was 349p to 586p on the 21st April 1998. The shares have peaked a high price of 603p. With this growth Tesco's is now the largest super market chain in the U. K.

PEST Analysis

A PEST analysis was undertaken of factors which would have an impact on Tesco or which need to be addressed by it.

Political Environment

The environment comprises of laws, government agencies and pressure groups that influence and limit Tesco PLC.

* With the increase in market concentration in recent years the UK's leading grocery retailers have come increasingly under the scrutiny of the Office of Fair Trading (OFT) for allegedly exerting monopsony powers in agricultural

markets. It was suggested that these retailers abused their dominant position by dictating particularly favourable terms and conditions on suppliers such as farmers.

* Public concerns about the operation of the grocery retail sector-one campaign on " rip-off" Britain had highlighted the fact that food prices in the UK were consistently above those in other European countries-lead to a referral to the Competition Commission (formerly the Monopolies and Mergers Commission) in 1999.

* Public disquiet about the effect of out of town superstores on town centres has grown and both current and future planning policies will seriously hamper future development. Though conversions of existing stores allows some increase in selling space it is limited.

* Community organisations have since gained momentum consequent to the Competition Commissions ruling and have been lobbying neighbourhoods to boycott supermarkets and large food manufacturers and instead support small independent suppliers, processors and retailers at the expense of large supermarkets like Tesco..

Economic Environment

* The UK food retailing market is mature and highly competitive. In order to improve margins large grocery retailers has moved into non food retailing where it now claims a 4% market share of non-food goods with a target of 6%. While non food items have higher margins they do have marginally higher costs in that they require adjustments to the supply chain process.

- * The UK market has been affected by negative inflation in the food sector. This negative inflation has been driven by the so-called 'Wal-Mart effect' i. e. downward pressure on prices from Asda / Wal-Mart's aggressive 'Every Day Low Price (EDLP)' strategy, It was not just the Wal-Mart effect that pressurised retailers into a price war but.
- * The saturation of domestic markets and the desire for growth have fuelled increasing globalisation in retailing through self-start, merger and acquisition and franchising. The increasing merger activity in the retail sector has also been partly driven by global shortages of real estate available to retailers to build stores, particularly with strong growth restrictions in Western Europe..
- * Scarce land resources compounded by government legislation on planning restrictions on out of town shopping facilities makes it difficult to expand into these locations.
- * Britain's supermarkets are racing to open small high street stores to cash in on demand for convenience shopping in urban areas.

Social Environment

- * The over powering proposition of the "everything under one roof" format has been a major factor in the demise of the small independent grocer, butcher and green grocer in recent times thus replacing the high street as the focal point of community life.
- * With no strong attachments to Local communities, supermarkets readily use job cuts as a safety net to ensure profits. Consequently local communities are haemorrhaging quantities of meaningful skilled jobs. The <https://assignbuster.com/tesco-analysing-the-environment-essay-sample/>

British Retail Planning Forum of 1998 revealed that every time a large supermarket opens an average of 276 jobs are lost

- * Declining meal preparation consequent to demographic changes such as an increasing number of single-person households and working women is forcing UK retailers to focus on added-value products such as the booming ' food-to-go' sector (eating out is now the UK's favourite leisure time pursuit).
- * Time pressures have increased during the 1990s giving rise to the expression ' money rich, time poor' consumers. Despite this, there has been a trend towards increased spending on leisure, which rose by 2. 89% pa between 1971 and 1987, and a shift away from food and housing.
- * Changes in work patterns has necessitated retailers to be more flexible in opening hours as well as adding extra shopping days e. g. Sunday shopping.
- * The U. K population on a whole is far more health conscious than in previous years. There has been a trend away from genetically modified foods towards organic foods
- * The increase in disposable income among Britons has led to more sophisticated customer preferences and demands for greater choice and comfort in the shopping experience.

Technological Environment

- * The Grocery retail sector is a major user of new technology. The increasing use of electronic data interchange, laser and self-scanning and other point-

of-sale equipment has been a feature of recent innovations by retailers. The use of loyalty cards and the provision of financial and other services have also involved the introduction of sophisticated computer-based systems.

* The development of supply-chain partnerships have helped to improve competitiveness. The supply chain has been one of the main catalysts for improvements in quality and costs, and the best partnerships between manufacturers and large food retailers have led to close long-term trading relationships and encouraged innovation.

* Almost every major food retailer in the UK has experimented with home shopping, home delivery and/or e-tailing. Order fulfilment has proved to be very costly whether centrally based or store based. Also, many customers have found the experience of Web-based grocery shopping dissatisfying, with software problems and general unreliability of the Web causing frustration. Tesco's home delivery and on-line schemes have proved most successful of these experiments.

Legal

* Government legislation has made it increasingly difficult to obtain planning permission for building out of town stores where land is cheaper.

* Proposals from the European commission to clamp down on predatory pricing policies to prevent the selling of goods below cost price such as exist within France Germany, Ireland and Spain. These proposals could cause Tesco and others who rely on loss leaders and aggressive pricing policies to draw consumers in a great deal of damage.

SWOT ANALYSIS

Strengths

* Tesco is a market leader in the U. K, holding 20. 6% of the market followed by Sainsbury 14. 5% and Asda; 11. 2% Market share respectively.

* It has clear market positioning and a strong “ own brand” which includes 20, 000 food and non-food products.

* The company’s long term strategy of self-financing growth has made the company less vulnerable to cyclic shocks over time.

* Tesco has engendered significant levels of customer loyalty through its very popular Club Card. The Card was pivotal to Tesco’s CRM (customer relationship management) strategy, providing the company with vital customer information including what, where and how customers were and were not buying. As a result of Tesco’s efforts to delight its customers, profits and market share have risen tremendously over time.

* Tesco has maintained strong like for like growth and margins healthy growth rate in the UK market despite concurrently expanding its operational expansion. This has kept the company on extremely good footing with its financiers.

* Tesco’s has been an excellent record of innovation. For example it has developed an innovative Tesco Information Exchange (TIE) System which allows suppliers to view supply chain information in near real time thus increasing their ability to deal with day to day supply chain issues.

Weaknesses

- * Vulnerable to concerted price campaign from competitors emanating from the much trumpeted Wal-Mart or EDLP (Every day low prices) effect.
- * Still scope for improvement in many non food areas.
- * Tesco in entering conservatively into the online grocery arena did not build much excess capacity into their software or facilities. Consequently there is the risk of being overtaken in this area by a competitor with greater capacity without some significant investment in this area.
- * The expenditure required to maintain its leadership in the UK market while executing its international expansion strategy exceeds its operating cash flows. Tesco has been forced to borrow to fund its financing shortfalls resulting in reduced financial flexibility³.

Opportunities

- * Further “ ready meal” development as it is one of the fastest growing segments of the food market.
- * The declaration of bankruptcy by Kmart in the united States has presented the opportunity to Tesco to set up in Wal-mart’s back yard
- * Despite the difficulty of bringing several new national enterprises rapidly through to critical mass and to steady profits, the consequent diversity of Tesco’s portfolio presents numerous opportunities for future strength.

* Tesco operates what is believed to be the only profitable online grocery in Tesco. Com and generated sales of £356 Million⁴ in 2001/02 which is the best performance of a grocery home shopping service recorded. This bodes well for the future of the company.

* Tesco's most recent U. K acquisition of T&S takes its share of the UK £20bn convenience market to 5%. This acquisition of the 850 store chain will ostensibly Increase its presence in many neighbourhoods across the country and bolster its share of a growing market.

Threats

* Should the shadow of the Global recession be cast over the U. K it could threaten its customer base in the U. K which could create serious financing concerns for Tesco.

* Concentration on various obstacles posed by its international expansion may distract attention from its core UK business.

* The U. K data protection Act has significantly reduced the breadth and use of the customer data that was captured by Tesco when it first introduced its Club Card in 1995. Strict limits have been placed on what detail and how long data can be kept. These strictures will no doubt have an effect on the accuracy of the customer data that Tesco will use to make its operational decisions⁵.

* Changes in planning regulations can stifle development.

* Food scares tend to have a serious short to medium term effect the company's bottom line. An example of this is the B. S. E beef crises of 2001 which within weeks saw the sales of British meat in stores falling by 54% during the year.

* The price wars sparked by the Wal-Mart/Asda policy of "every day Low prices" have forced Tesco into cutting prices thereby risking reductions in its levels of profits. If an all out price war were to occur then Wal-Mart's deeper pockets (i. e. a turnover of US\$150 billion or $\frac{1}{2}$ 100 Billion, compared to Tesco's $\frac{1}{2}$ 20 Billion) would doubtless guarantee it victory.

Porters Five Force Analysis

This is a means of identifying the forces which affect the level of competition in the retail industry.

Threat of New Entrants

* Economies of scale in terms of square footage of shopping area and breadth of distribution channels are all critical factors in the U. K market. Larger stores can stock and sell many more products faster which is consistent with both their customers and suppliers preferences.

* Brand loyalty of customers in the sector is relatively high in that existing players have built a certain amount of goodwill with customers through loyalty and "own branded" credit cards.

- * Scarcity of suitable real estate for shopping centres consequent to the absorption by the existing players as well as government legislation placing strictures on further out of town development.
- * New entrants have limited access to U. K distribution channels as these channels are controlled by existing players. Access is typically be gained through mergers and acquisitions.
- * There are very low switching costs to customers in the market and so market share can typically be gained by leveraging price and product range variables.
- * Existing players have accrued cost advantages due to experience curve effects of operation with fully depreciated assets,

Power of the Supplier

- * Supplier power tends to be relatively low for the most part in the U. K market as there are a small number of significant operators in the market. However in certain segments of the market for example washing powder where Procter and Gamble and Unilever enjoy a virtual duopoly.
- * As “ own brands” are emerging as a growing segment of the goods portfolio of large grocery multiples due to the higher margins available (Table 3) even large suppliers manufacturers such as Unilever, Nestle, PepsiCo have been increasingly producing for own labels despite potential competition to their own brands. Some however such as Kellogg’s Coca Cola and Gillette do not agree to such arrangements as they consider it prejudicial to their quality reputation.

Power of the Buyer

- * Buyer power is particularly strong in the U. K grocery retailing industry where there is an extremely high concentration of buyers. Tesco, Sainsbury and Asda dominate the market.
- * For smaller retailers joining a buying group is an important element of survival and give members' enhanced economies of scale in purchasing. These groups however play only a small and declining role in the market since they do not buy on the scale of the large supermarkets and also cannot guarantee sizeable shelf space to major suppliers. Consequently they obtain lower discounts than the major chains.
- * Wholesaling and distribution have been internalised and the retailer controls them directly.
- * The cost of switching suppliers in the U. K market is very low and involves negligible risk.

Threat of substitutes

- * Though Tesco has successfully improved its margins by increasing the ratio of non-food to food in its superstores it has moved into other competitive arenas e. g. its foray into furniture and household appliances has put it on a collision course with household appliance retailers like Curry's and Argos.
- * Changes in public consumption; e. g. the loss of confidence in British beef during the B. S. E beef crises of 2001 or fear of the long term implications of consuming genetically modified foods.

Competitive rivalry

- * Four major firms dominate the U. K market at present but concentration has increased markedly in the 1993-1996 period with major multiples pursuing active policies of new store development. Over this period Tesco has overtaken Sainsbury to become the market leader while Asda has since being newly acquired by Wal-Mart been threatening to take Sainsbury's slot.
- * There is no genuine differentiation between products therefore the principal rivalry tends to revolve around pricing and perceived value for money . Own-Label is increasingly becoming an important differentiator.
- * Information Technology offers modern retailers the potential to speed up stock replenishment while reducing the cost of distributing products as well as strengthening links between the retail chains and their customers. Players which are most innovative in adapting technologies for these purposes tend to have a decisive advantage in the market.
- * Strategies of the larger players are fairly similar in that larger players typically employ growth by international acquisition in emerging markets and by increasing their exposure to the non - food segment of the market. Players in the lower echelon such as Sainsbury's have since embarked upon a strategy of consolidation around a core business of food while maintaining a presence in the international arena.
- * Other Global competitors such as Carrefour/Promodes just across the channel may gain entry positions to the U. K market by way of acquisition of weaker companies.

Macroeconomic and International Environment

The underlying fundamentals of the UK economy have been reasonably healthy. The economy has been largely characterised by low inflation, high levels of employment, and sharp rises in house prices. These factors have provided the substrate for the explosive growth in consumer spending that have marked a growth nourished by windfalls accruing to consumers due to mortgage rates falling to their lowest for some 40 years. These low rates have supported rising house prices and have also led to an increase in household debt. Consumers have borrowed against the increased value of their homes and consequently household debt levels have reached 111 per cent of disposable income - against the 95 per cent reached after the 1980s boom.

The Jobs market has been supported by huge increases in government spending and public sector employment. Another part of the problem appears to be that the concept of a job for life has been eroded so that once uncertainty creeps in everyone feels vulnerable.

Though Large supermarkets, department stores and clothing and footwear stores performed particularly well, overall volume annual growth in seasonally adjusted sales by clothing & footwear retailers slowed in November to its lowest rate for three years. Prices in non-food stores continued to fall in November. Consumers it would appear are beginning to show signs of cautious spending and retail continuous price cuts and stiff competition between stores, sales has been affected, particularly the non-

food sector. Consumers have been hit by worries surrounding the volatility of world financial markets and uncertainty over house prices.

Food has typically been unaffected by cyclical fluctuations because of its generally low-income inelasticity. After all, richer or for poorer we all need to eat. Non-food items on the other hand are typically more vulnerable and recent changes in the product portfolios of the major players in the grocery retail will doubtlessly have a negative effect on their business. Tesco for example has shifted a large proportion of their business into non-food and so it is likely that a continuation of the business slowdown will have deleterious effects on its overall business.

Though the U. K has not yet adopted the euro, its close ties to the Euro zone have also left it exposed to the adverse effects of prevailing problems plaguing the zone. For instance the weakened Euro has been having a dampening effect on price levels and also reduced external demand on the economy. If and when the U. K does indeed join the Euro there are many implications for U. K Businesses particularly those with strong links with Euro Land including greater competition and price transparency.