

Stores of Knowledge: No.1 Retailer in Britain Uses `Clubcard' to Thwart Wal-Mart --- Data From Loyalty Program Help Tesco Tailor Products As It Resists U.S. Invader --- Ms. Fiala Changes Detergent

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CHESHUNT, England -- When Wal-Mart Stores Inc. entered the British market in 1999 by buying a chain of stores here, many expected it to dominate. Instead, Wal-Mart's largest non-American operation has been struggling recently, and its top local rival is thriving.

That rival is Tesco PLC, Britain's largest retailer. Its big weapon is information about its customers. Tesco has signed up 12 million Britons for its Clubcard program, giving cardholders discounts in exchange for their name, address and other personal information. The Clubcard has helped boost Tesco's market share in groceries to 31%, nearly double the 16% held by Wal-Mart's Asda chain, according to market-research firm Taylor Nelson Sofres.

The data let Tesco tailor promotions to individual shoppers and figure out quickly how new initiatives are working. After Tesco introduced Asian herbs, cooking oil and other ethnic foods in neighborhoods with many Indians and Pakistanis, the data showed the new products were also popular with affluent white customers. The company quickly expanded the rollout.

Tesco's computers often turn up counterintuitive results. Shoppers who buy diapers for the first time at a Tesco store can expect to receive coupons by mail for baby wipes, toys -- and beer. Tesco's analysis showed that new fathers tend to buy more beer because they are home with the baby and can't go to the pub.

The data-driven strategy puts Tesco at the vanguard in retailing as traditional advertising loses effectiveness. Procter & Gamble Co., Coca-Cola Co. and Kimberly-Clark Corp. are among the consumer-products companies that buy analyses based on Tesco data.

The British retailer is increasingly battling Wal-Mart around the globe. It plans to open a chain of small stores on the West Coast of the U.S. next year, its first foray onto Wal-Mart's home turf. Wal-Mart wants to expand in Central Europe, where Tesco has a firm foothold.

As the U.S. market becomes saturated, Wal-Mart is looking overseas for growth. It has had some successes, including Mexico and Canada, but many of its overseas ventures are hurting. Its Japanese unit has suffered losses. Last month, Wal-Mart abandoned an eight-year effort in South Korea by selling its 16 outlets there to a local competitor for \$872 million. Tesco says its 39 Korean stores are successful.

Asda in the U.K. accounts for about 10% of Wal-Mart's overall business and 45% of its international sales. The unit thrived under Wal-Mart's ownership for several years but Wal-Mart says sales were "slightly negative" last year and profits were "below plan." (It doesn't report exact figures.)

Tesco has used its knowledge of shoppers to fight Wal-Mart's core appeal: low prices. After Wal-Mart bought Asda, Tesco searched its database and singled out shoppers who buy the cheapest available item. They were most likely to be tempted by Asda, Tesco figured.

Tesco then identified 300 items that these price-sensitive shoppers bought regularly. One was Tesco Value Brand Margarine. Tesco lowered the price of the margarine, along with other products with similar profiles. As a result, shoppers didn't defect to Asda, says Clive Humby, chairman of Dunnhumby, a British research firm that is majority-owned by Tesco and analyzes customer data for the retailer. Tesco's sales jumped 17% to \$79

billion in the year ended Feb. 25, and net income rose 17% to \$2.96 billion.

Founded in 1919 as a grocery stand in East London, Tesco grew into a supermarket chain after World War II and opened its first superstore in 1968. The company's name comes from its first private-label product, Tesco Tea, which founder Jack Cohen named by combining the initials of a tea supplier, T.E. Stockwell, with the first two letters of his own last name.

In the 1990s, as space for new big stores became scarcer, the retailer refined its strategy. Today it operates 2,306 stores in Britain in four sizes: huge supercenters stocking everything from lawn furniture to apples; large stores that have a limited range of nonfood items; regular supermarkets; and "Tesco Express" convenience stores with merchandise tailored to neighborhood tastes.

Tesco's size is raising antitrust concerns in the U.K. Last month, the British government ordered an investigation into the power of the country's four biggest supermarket chains. Tesco Chief Executive Terry Leahy said the company isn't doing anything improper to block competition. He said Tesco is successful because "millions of ordinary consumers vote with their feet when they go shopping."

As Wal-Mart is increasingly doing in the U.S., Tesco tries to appeal to both affluent and bargain shoppers. It has several private labels, ranging from the "Tesco Finest" line that includes duck pate and cashmere sweaters to the "Tesco Value" brand, which offers baked beans and the like. The idea for the Finest line came a few years ago when Clubcard data showed that higher-spending customers weren't buying wine, cheese and fruit from Tesco. The retailer upgraded its offerings in those categories.

In 1995, Tesco introduced the Clubcard under Mr. Leahy, then head of marketing. Today, about 80% of Tesco shoppers are Clubcard members. They join by filling out an application form at a store, which includes optional questions about the size of their household, the ages of their children and dietary preferences.

Members receive a plastic card in the mail, which they use at the checkout to receive a point for every pound they spend. (They must spend at least GBP 150, about \$280, to begin getting points.) Each point is a penny off future purchases, or it can be converted into miles in frequent-flier programs. On top of the points, big spenders get discount coupons every three months on particular products, keyed to their buying profile in Tesco's database.

Adele Fiala, a 36-year-old homemaker in London, recently used air miles earned from her Clubcard for a weekend trip to Seville, Spain, with her husband. While she tosses promotional mailings, "I always open the mail from Tesco," she says. She recently switched from powdered laundry detergent to liquid capsules after receiving a one-pound-off coupon in the mail from Tesco.

To help analyze the mountains of data that Clubcard generates, Tesco turns to consultancy Dunnhumby, named for its two founders -- Mr. Humby and his wife, Edwina Dunn. Dunnhumby is also active in the U.S. as an adviser to supermarket chain Kroger Inc., analyzing customer data and running its loyalty-card program. Dunnhumby's offices in Ealing, just outside London, receive data on 15 million Tesco shopping baskets every week.

Each product is scored on 50 dimensions such as price and the size of the package. The computer looks for customers whose shopping baskets have similar combinations of scores. Dunnhumby classifies shoppers in six segments. The "Finer Foods" segment, for example, is made up of affluent, time-strapped shoppers who buy upscale products. "Traditional" shoppers are homemakers with time to buy ingredients and cook a meal.

Many retailers consider loyalty programs expensive to manage and think they slow down the checkout line. Neither Wal-Mart nor its Asda unit has a frequent-shopper card, though Asda tried one for four years before dropping it in early 1999. Asda argues that it can get nearly the same information for less money by combining Wal-Mart's powerful sales-tracking computers with targeted market research such as focus groups.

"There clearly are benefits to having loyalty-card information but there are costs as well," says Jon Owen, head of research and pricing at Asda. "We prefer to give our customers the value in different ways."

Asda executives believe Tesco's databases have little to do with its success. Instead, they say Asda fell behind because it failed to reach out to higher-end shoppers with products such as better produce and gourmet ready-to-eat meals. It also lost its crown as the low-price leader. Andy Bond, Asda's chief executive, said this March in a conference call with analysts that Tesco and other supermarkets were matching Asda's prices.

Mr. Bond said last December that the unit is "operationally failing." Mike Duke, the chief executive of Wal-Mart's international division, says: "We took our eye off the customer." Recently, Asda has upgraded its foods and, in a shift from Wal-Mart's supercenter strategy, opened small discount stores like those Tesco operates.

Tesco doesn't disclose its investment in Clubcard but spokesman Jonathan Church says it is "worth every penny."

A typical quarterly coupon package Tesco sends to customers includes three coupons for products they regularly buy and three for goods that they might like, or that Tesco wants them to try. While industry adage says that only 1% or 2% of all coupons ever get redeemed, about 15% to 20% of all Tesco coupons are redeemed.

The package also includes vouchers through which Clubcard members can redeem their accumulated points. If a member has spent GBP 300, she will get a voucher for GBP 3 off any purchase. Tesco says 95% of these vouchers are redeemed, suggesting that they help entice shoppers to return to the store.

Tesco statements mailed to Karen Masek, an actor and mother of two in London, reflect her preference for fresh produce, environment-friendly cleaning products and organic meat. "They definitely know your shopping habits," she says. "They've never sent me anything totally off the mark."

Recent mailings to Ms. Masek, 43, have included coupons for new vegetables, cooking sauces, and nuts or seeds. Ms. Masek, who made sure her nanny had a Tesco loyalty card as well, says she often redeems the coupons and uses Clubcard points to pay for video rentals.

Martin Hayward, director of consumer strategy at Dunhumby, says such cases show why loyalty cards are worth the trouble. "You couldn't do that just with data" from checkout receipts, he says.

The data are also useful for consumer-product makers. Five years ago, Kimberly-Clark introduced a premium version of its Andrex toilet paper in Britain infused with aloe vera. Clubcard records helped the Irving, Texas, company track who was buying the toilet paper and whether shoppers stayed loyal to it. Dunhumby also found that regular buyers of Andrex Aloe Vera were also big buyers of skin-care products. Kimberly-Clark then sent direct mail to 500,000 customers, offering them free beauty treatments if they could show that they bought the toilet paper twice.

Tesco's recent rollout of an ethnic-food line called "World Foods" shows how customer data can shape decision-making at almost every step of the way. The idea got its start when Clubcard records showed shoppers at a small store in the town of Slough weren't buying full meals. Many people in the town have South Asian or Arab roots.

Tesco decided to replace the store with a supercenter. Focus groups confirmed that people in Slough were buying some products at Tesco but turning to smaller markets for many staples -- large stacks of rice, big canisters of cooking oil and Asian brands. Many criticized the small plastic packages of herbs at Tesco and said they wanted loose bunches that they could touch and smell.

When the new Slough store opened in August 2005, it offered more than 800 foreign products, up from 150 in the previous store. It has a large halal butcher shop, the latest movies from India, newspapers in Arabic, Urdu, Punjabi and Bengali, and a jewelry counter with bangles in yellow 22-karat gold popular in India. The shopping carts are lower and flatter to fit big sacks of rice and flour.

Tesco wanted to know if the strategy was working, so it turned to Dunhumby. The analysis found that 36% of Slough shoppers were buying goods from the World Foods line. That figure roughly matched the proportion of Slough's nonwhite population.

Dunhumby then checked addresses of World Foods buyers against government census data that identify immigrant neighborhoods. It turned out that more than a quarter of the World Foods customers were coming from largely white neighborhoods. By examining the shopping baskets of these customers, Dunhumby concluded that upscale white shoppers with an interest in non-European food were responsible for some of the success of the World Food line.

In the following days, executives huddled over big maps showing Britain's ethnic makeup. They outlined a plan to roll out the World Foods line to 300 stores in immigrant areas as well as to 25 stores in mostly white parts of

the country.

A few weeks later, Tesco stores in places like Holland Park, a leafy part of west London, and Bar Hill, an affluent town near Cambridge, were stocking fragrant herbs and frozen samosas. Tesco says the Bar Hill store is selling World Foods better than any of its other stores. Dunnhumby is running numbers to get the details.

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