

The Future of Non-food Sourcing

The Sourcing Landscape



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China is the factory of the world - exports exceeded USD 1.2 trillion last year



- 80% of toys
- 80% of luggage
- 73% of digital cameras
- 40% of stationary

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The Pearl River delta



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Factors impacting China's competitiveness

- Depressed international demand following global economic slowdown
- Soaring prices of raw material
- Continuous RMB appreciation (up 17% against USD since 2005)
- Wages, production and transportation costs increased by up to 20% since 2007
- Higher safety standards and certification requirements in Europe

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Shifts in China business environment



- Labour-intensive to capital-intensive
- Pearl River to Yangtze River
- Coastal to interior
- Export-driven to domestic market-led
- Not supervised to tightened environment & quality standards

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Resulting trends

- De-localisation of Factories
- Outsourcing: further division of labour between large companies and SME's
- Upgrading: development of high added-value, designed, green products
- Opening up the domestic market

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China is here to stay

- Logistics infrastructure
- Experienced labour pool
- Operating capability to execute
- Low input costs
- Fast growing domestic consumer market
- Regulatory reforms

These are the raw materials for an economic boom

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The Indian subcontinent is the second largest sourcing location in the world

Pakistan

- Sourcing mainly for US
- Large inexpensive labour supply
- But safety and security are issues

Bangladesh

- Large low cost skilled labour force
- Duty free access to major markets
- Developing labour safeguards

India


- No 2 location for global sourcing
- Strong diverse raw material base
- Strong design capability
- Incentives and emphasis on exports
- But lack of infrastructure

Sri Lanka

- Environmental and ethical credentials
- Strong innovation & design
- Focus on niche products
- But civil unrest

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Southeast Asia is becoming important in world manufacturing and supply chain



Southeast Asia

- Labour cost advantages vs China
- Abundant natural resources
- Trade assistance schemes
- But political issues can be challenging

Cambodia

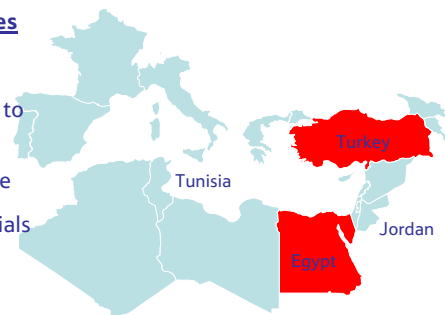
- Emerging location
- Many export privileges
- Sweatshop free reputation
- But lack of local raw materials

Vietnam

- Large, young population and low labour costs
- Export-led growth strategy
- But high inflation

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Turkey will become a regional hub leveraging cheaper neighbouring countries



Turkey advantages

- Young population
- Short supply chain to Europe
- Good infrastructure
- Ecological credentials
- Few ethical issues

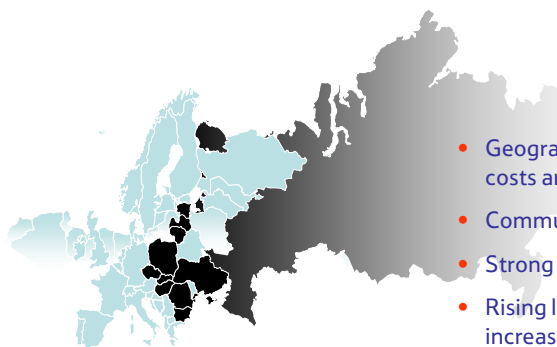
Turkey issues

- Rising labour and energy costs
- Strong currency
- Removal of EU quota on Asia imports

100 Turkish firms are investing c. USD4bn in Egypt

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Central and Eastern Europe can be competitive close to home



- Geographic proximity means lower freight costs and faster response times
- Communication infrastructure strong
- Strong skilled labour forces
- Rising labour & energy costs in China increase Europe competitiveness
- But geographical fragmentation and high labour costs remain an issue

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Central Asia is not competitive due to remoteness and lack of trade facilitation



- Good availability of raw materials
- Remoteness is an issue
- Trade barriers and poor transit systems compound this
- Labour availability is also an issue

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Latin America is best positioned to supply Northern America



- Geographical proximity and time zone compatibility mean it works for US
- Initiatives to increase trade
- Transportation costs to Europe decrease attractiveness
- There may be labour force constraints – lack of skill and scale

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Sub-Saharan Africa is not an attractive sourcing location at this time



- Exports mainly around primary commodities
- Political instability and civil conflict reduces attractiveness
- Regulatory systems weak
- Chinese are investing in natural resources related industries and infrastructure projects

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Tesco are in the right locations to maximise competitive advantage

- With hubs in Hong Kong, China, India, Bangladesh, Sri-Lanka, Turkey, Italy & Czech Republic, all key production locations are covered with strong people capabilities



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Changing Role of the Sourcing Office



Increasing collaboration with suppliers will bring further competitive advantage

- Supplier categorisation and rationalisation
- Technology – information sharing platforms
- Better planning and forecasting tools
- Supplier incentivisation, reward and penalties
- Leveraging suppliers' expertise and capabilities
- Process integration

Sourcing activities outside China will become more dispersed

- Model to enter new markets at very low cost and evolution model to full sourcing hub
- Knowledge management becoming key

Logistics will become a more important component of total product cost

- Detailed analysis on end-to-end costs in collaboration with service providers
- Increased local resource may be necessary

End market requirements becoming more significant for retailers and suppliers

- Consumer standards and sensitivities
- Regulatory requirements

In conclusion

- Tesco International Sourcing is a business of scale that continues to offer strong competitive advantage to the group through being closely aligned to Tesco customers
- To further increase competitive advantage in the future we will build strong collaborative relationships with suppliers
- For the foreseeable future, China will remain a key sourcing location. We remain close to emerging trends and are developing a flexible model to enable us to move to new locations quickly