



A blueprint for profitable retailing in China

Ken Towle, CEO Tesco China

Tesco in Asia 2010, 21st–23rd November

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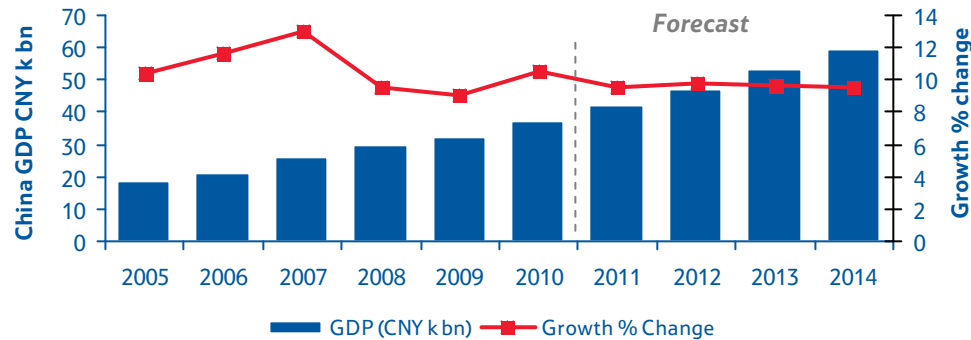
- Introduction
- Market opportunity
- Our vision: best retailer in China
- A plan for profitable growth
- Summary: a winning strategy for China

A clear blueprint has been developed for profitable retailing in China

- China offers an unrivalled opportunity in a large, rapidly growing market
- The prize is enormous but the challenge is complex – China is a vast continent, with cities the size of small countries
- As a leading international retailer in Asia, Tesco has the experience, skills and scale to be a market leader in China
- Tesco has spent six years learning about the local market and developing a strategy for profitable growth
- We're making good progress with the foundations – investing in infrastructure and capability – that will create long-term value
- The path to long-term profitability is now clear – leveraging our substantial up-front investment as we grow our scale

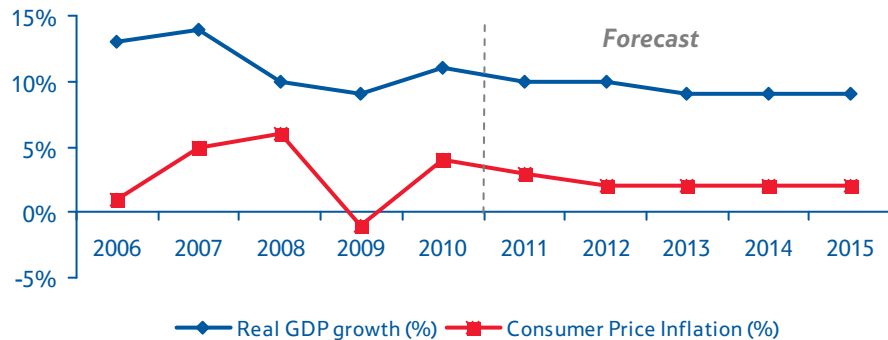
China Economy: an outlook of strong and stable growth

China: GDP 2005-2014



Source: Planet Retail

Real GDP and CPI growth % 2006-2015

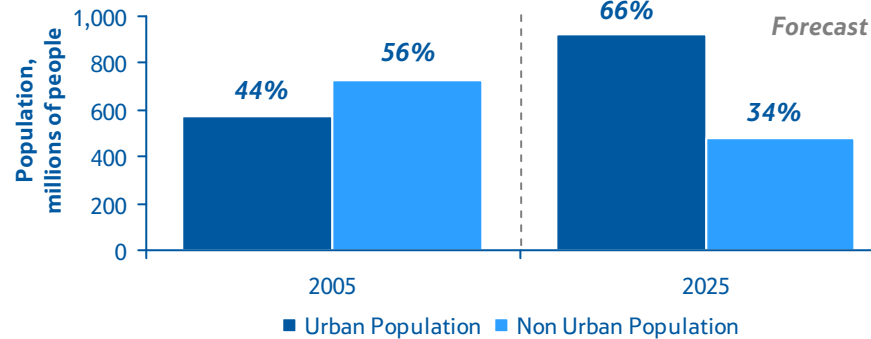


Source: Planet Retail

- c.10% growth rate projected for foreseeable future
- Low inflation outlook – stability projected
- Set to be world's largest economy by 2030

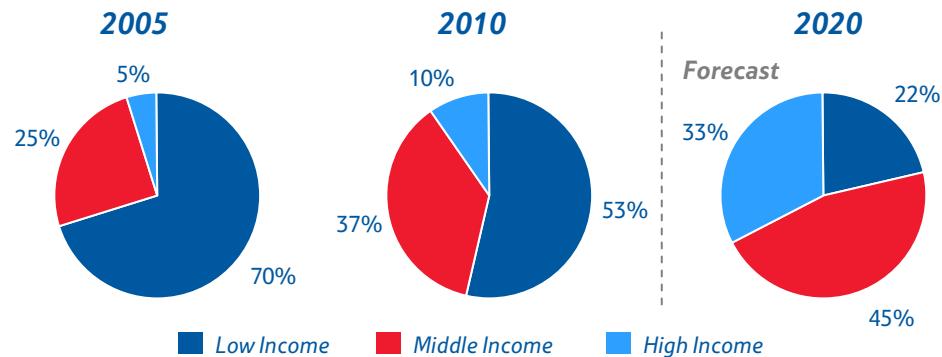
Growth of the urban middle class

Growth in Urban Population, 2005-2025



Source: McKinsey Global Institute China

% of Households Grouped by Income



Source: Euromonitor

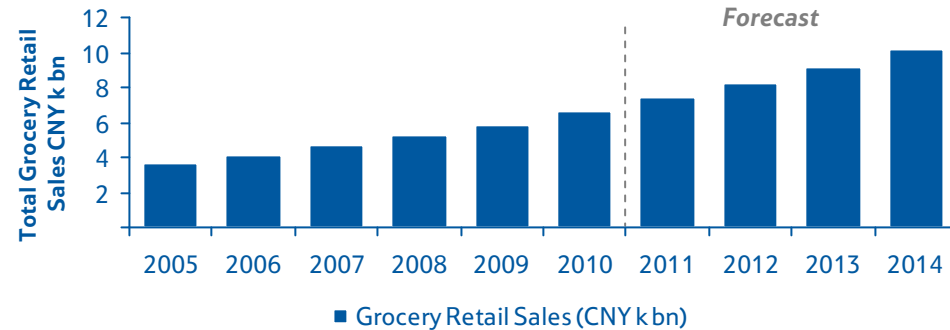
Annual disposable income at constant FX rates

Low: <=US\$5,000; Middle: >US\$5,000-US\$15,000; High: >US\$15,000

- Steady growth in urbanisation
- 221 cities of >1m population by 2025
 - 35 in Europe currently
- Growing urban middle class
- Booming car ownership
 - 85m cars in 2010
 - 390m cars by 2030

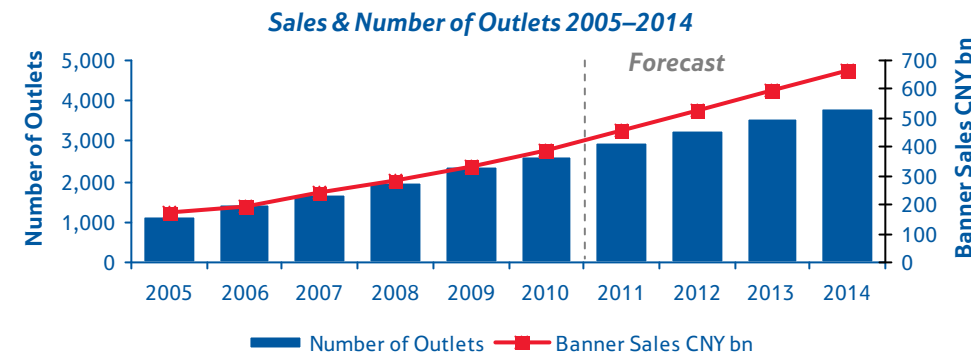
Economic and demographic trends are driving a rapidly growing, modern retail sector

China: Grocery Retail Sales 2005-2014



Source: Planet Retail

China: Hypermarkets & Superstores



Source: Planet Retail

- £600bn grocery retail sales in 2010
- Forecast for continued growth
- Rapid development of hyper and superstore channels
 - 2005: ~1,000 outlets
 - 2010: ~2,600 outlets
 - 2014: ~3,800 outlets

Our vision: best retailer in China

Regional strength and responsiveness



Leveraging the Group Operating Model



High quality new space enabling organic growth

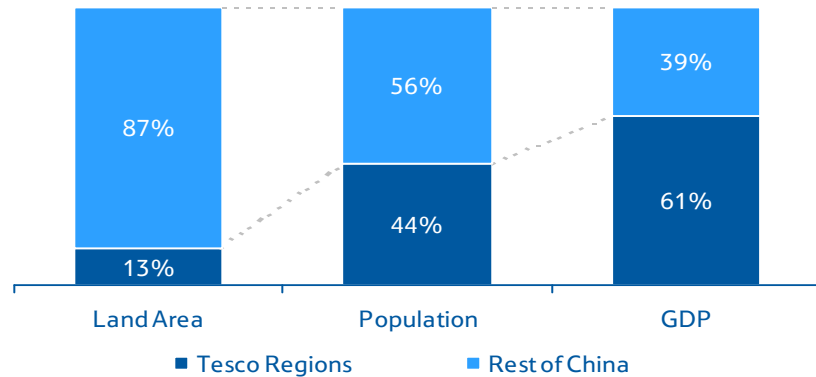


Integrated supply chain and distribution network



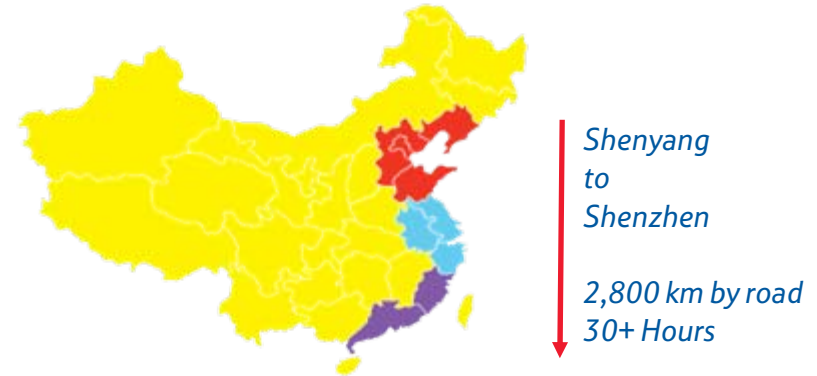
Focusing on our Strategic Provinces

Our approach focuses us on the best of China

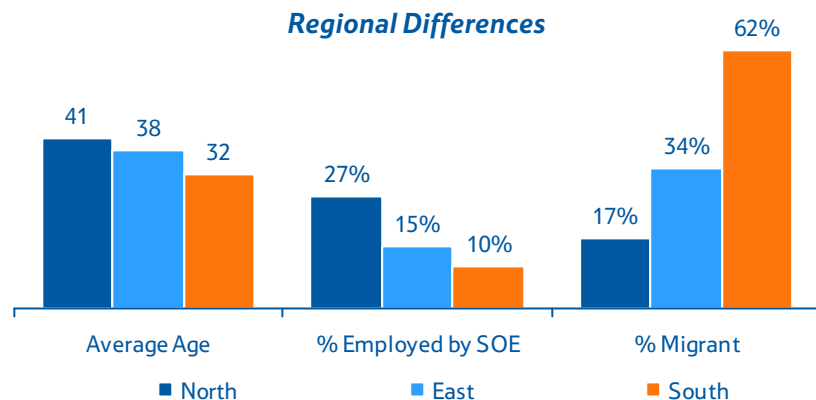


Source: 2009 China National Statistical Yearbook

Regional teams required to address China's scale...



...because customers are different in each region...



Source: Tesco Exit Surveys

... and because suppliers are regionally structured

Coca-Cola's Regional Approach: Agents across China



How the Central and Regional Structure works

In the Centre

⇒ Policies, Systems, Processes, Service Centres, Leveraging Scale, First Among Equals

⇒ As much as can be the same

- Financial control and reporting
- Commercial: Hardlines, Electronics, Clothing and national FMCGs
- Marketing: Insight, Membercard, Trade Planning and Customer Comms
- Development/deployment of Operating Model
- Ordering, IT, Distribution and Supply Chain
- Property Services and Management
- Leasehold Mall Management
- Human Resources

In the Regions

⇒ As different as it needs to be

- Tailoring our offer for local customers
- Commercial: local suppliers and regional divisions of FMCGs
- Marketing: local Trade Plan
- Operating our stores to deliver a consistent Shopping Trip
- Finding and developing the people to enable our growth

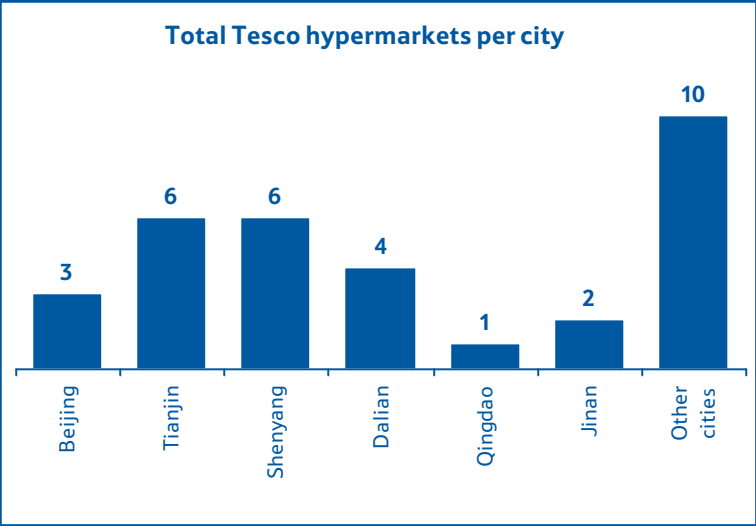
North Region (Richard Baker, Vice President)



North China

- 236m people – 75% of US population
- 522k sq km – bigger than Thailand
- GDP similar to India
- 34 of the Top 100 cities in Tesco's regions

In 09/10 opened most space of key international retailers – 36% of total ¹



¹ Source: Tesco Site Research



North Region: building on growing scale and maturity

Progress since 2008

- Increased store numbers by 70%
- Opened four Lifespace Malls
- Established team in Shandong province
- Opened first Fresh Food Distribution Centre; second to open in December
- A deeper understanding of the differing needs of customers within the region's five Provinces
- Improving Trade Plans and growing like-for-like sales

Priorities

- Being the best for Fresh Food
- Further improving the local part of our offer, particularly on the Deli
- Being No. 1 in every city
- Developing the structure and capability of the team
- Opening Blueprint Distribution Centre

East Region (Gordon Reid, Vice President)

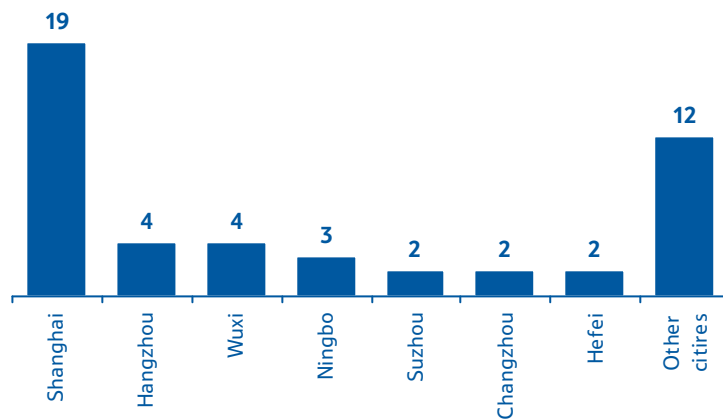


East China

- 208m people – bigger than Brazil
- 361k sq km – same as Germany
- GDP similar to Russia
- 14 of Tesco regions' 20 most affluent cities

15% of key international retailer space ¹

Total Tesco hypermarkets per city



¹ Source: Tesco Site Research



East Region: customer loyalty, maturity and leveraging scale

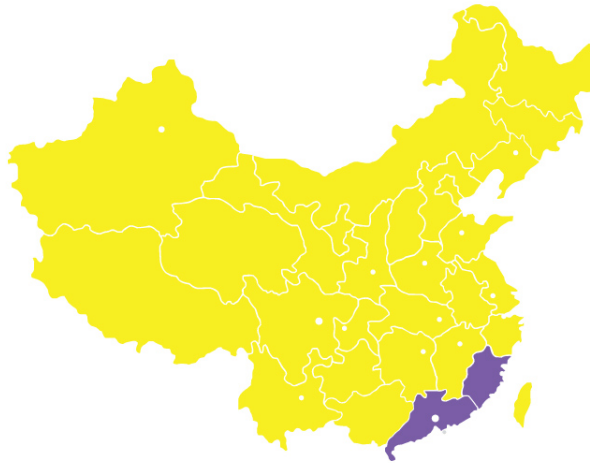
Progress since 2008

- Increased store numbers by 50%
- Opened first stores in Anhui Province
- Investing in refits to improve our older stores in Shanghai
- Improving the customer shopping trip
- Improvements on Fresh, particularly Meat, Produce and Bakery

Priorities

- Market leading growth, building on existing strong positions
- Leveraging the supply chain and Operating Model
- Leading a high performing team
- The best shopping trip for our customers

South Region (Winnie Liu, Vice President)

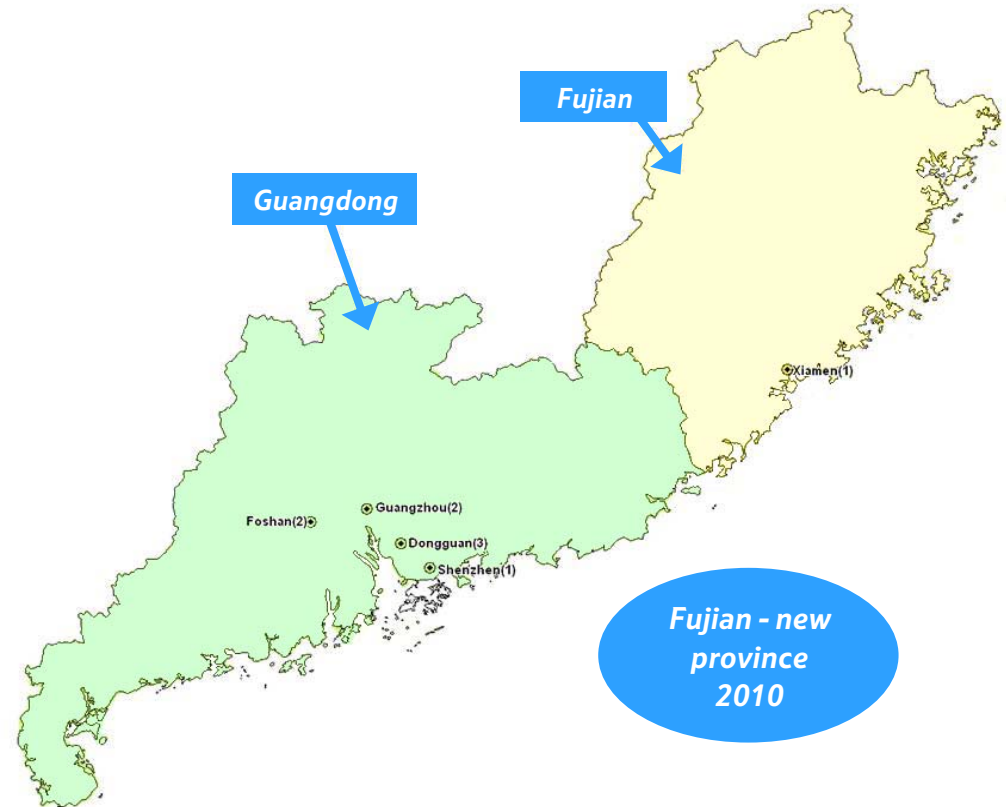
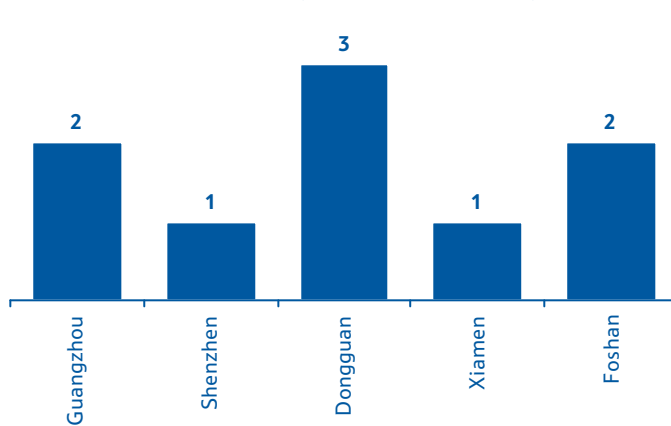


South China

- 131m people – as big as Japan
- 304k sq km – as big as Poland
- GDP similar to Turkey
- 22 of the Top 100 cities in China's regions

9 stores by 2010, with footholds in all major cities

Total Tesco hypermarkets per city



South Region: strong growth as first stores start to mature

Progress since 2008

- Increased store numbers by 80%
- Achieved market leading growth
- Successfully entered Fujian Province
- Opened Fresh Food distribution centre and step-changed Fresh quality
- Made key additions to senior team

Priorities

- Increasing new store programme including LifeSpace Malls
- Building on strong growth
- Earning trust in the Tesco brand
- Best for Fresh Food in every store
- Developing the supply chain
- Building the capability of the team

We know our customers

We understand our customers and their changing needs



We are earning their loyalty

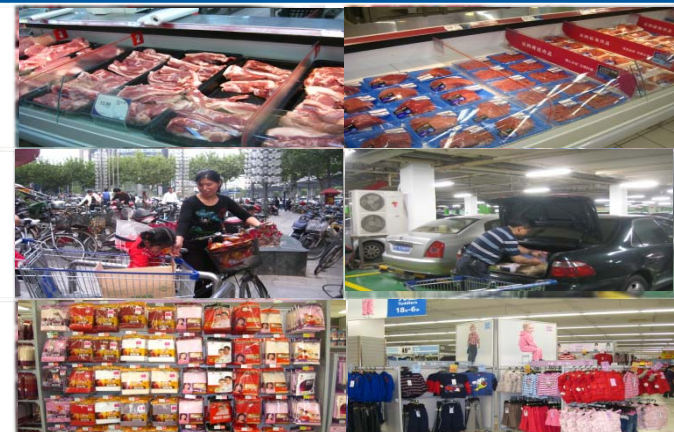


* New members shopping within 120 days and existing members shopping within 370 days

Improving the Shopping Trip



Providing Broad Appeal



We are building our skills

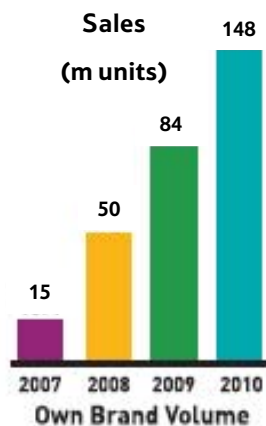
Commercial Capability



Direct and International Sourcing



Own Brand



Category Management



Our experience in other markets has taught us the importance of investing in high quality assets



Despite being in Tier 2 and 3 cities, our hypermarkets in Lifespace malls have similar sales levels to stores in Tier 1 cities

Our supply chain is strengthening...

Centralised, Tesco-managed supply chain



Demand driven replenishment



Space, range & display helps efficiency of supply chain



Efficient Consumer Response utilising data and insight



... and our physical network is improving

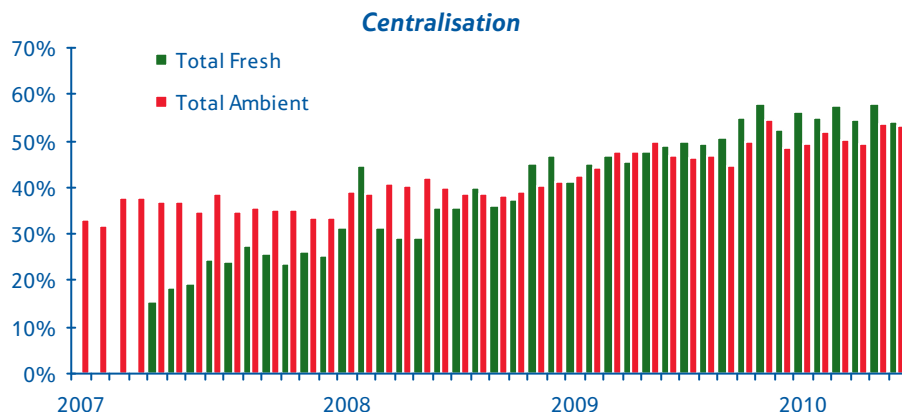
To-be network 2014/15



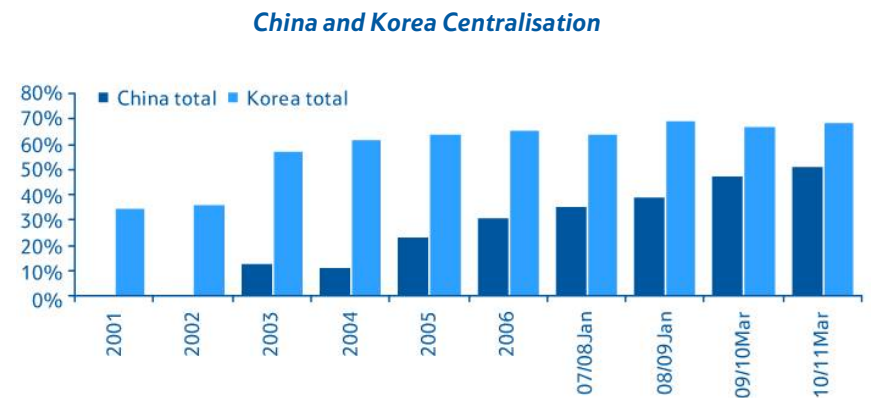
Our first freehold blueprint green logistics centre



Distribution centralisation



Proven global model



Community and Corporate Social Responsibility

An important part of what we stand for



Carbon Emissions Reduction



Get Active and Nutrition



Customer and stakeholder recognition



Government as a Stakeholder

Our priorities are aligned

- Grow Domestic Demand
- Carbon Emissions Reduction
- Food and Product Safety
- Foreign Direct Investment
- Develop Local Talent
- Modern Supply Chain



Relationship Building



Advisory Board

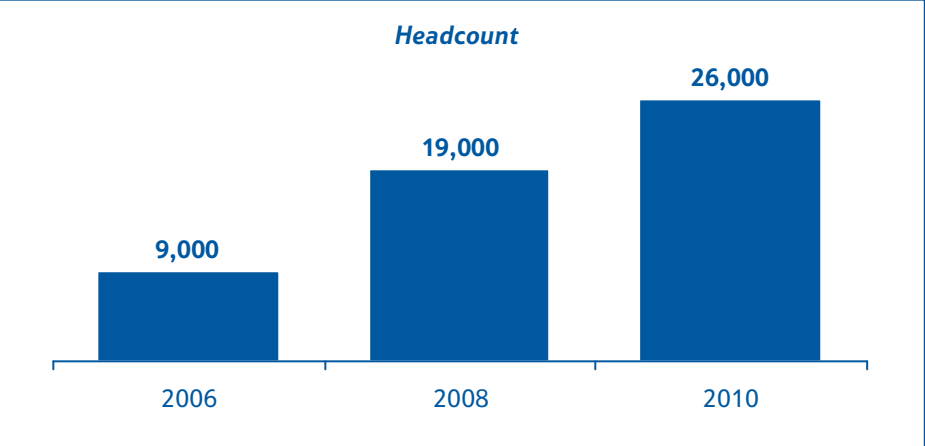


Making important progress

- MoU with Ministry of Commerce
- Tesco Climate Change Seminar
- MoUs with Anhui and Shandong governments

Our Team

A growing team



Developing Talent



Earning Loyalty

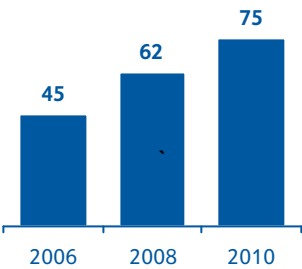


One of the best retail employers in China

No one tries harder for customers
Understand customers
Be first to meet their needs
Act responsibly for our communities

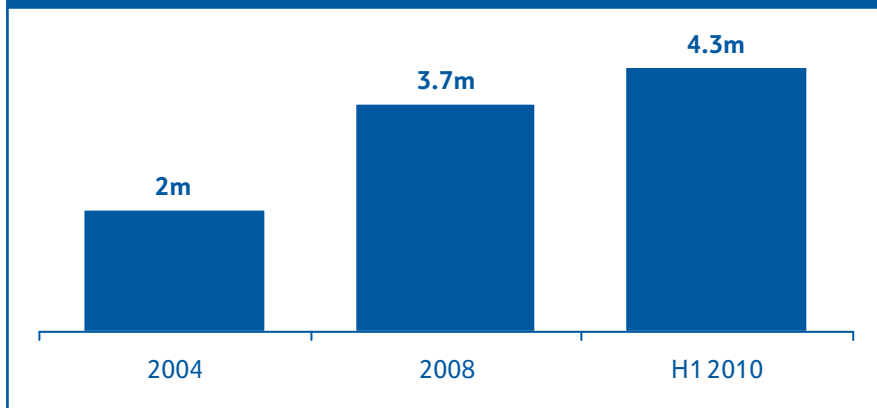
Treat people how we like to be treated
Work as a team
Trust and respect each other
Listen, support and say thank you
Share knowledge and experience
... so we can enjoy our work

Viewpoint:
Overall Employee Satisfaction %

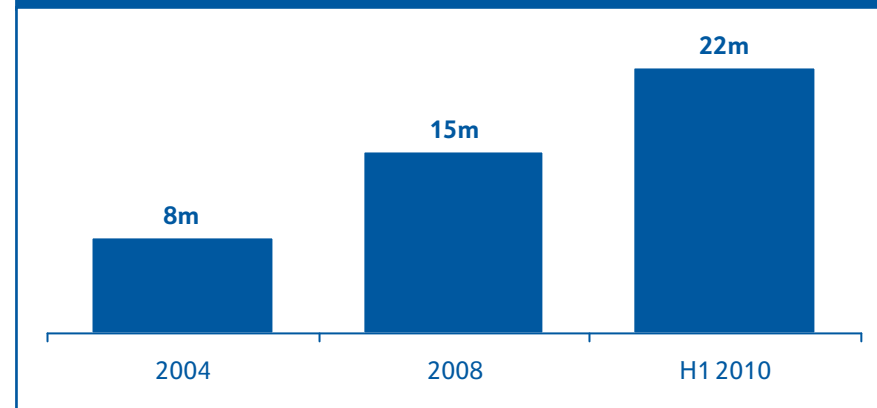


We've made strong progress so far

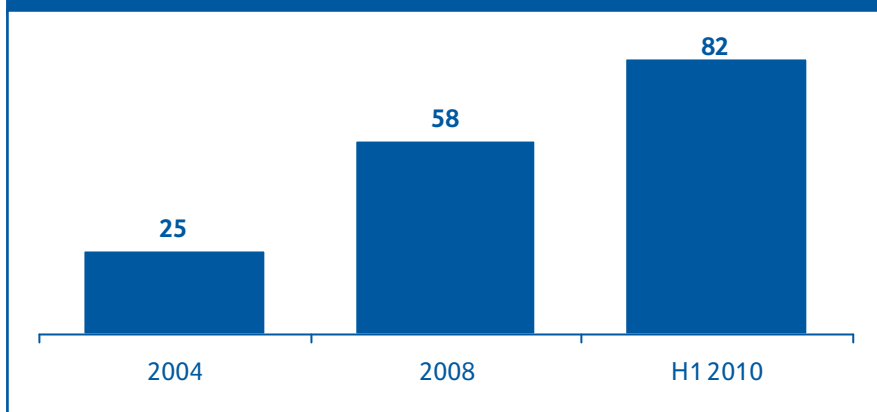
Customers per week



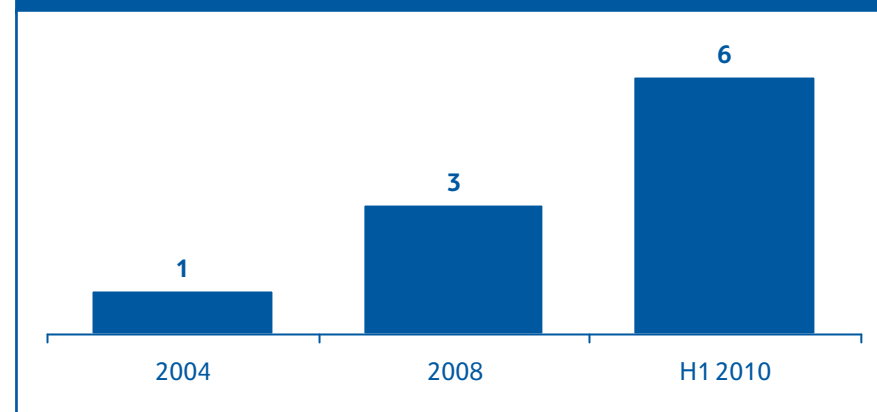
Sales per week – GBP ¹



Hypermarkets



Distribution Centres



¹ Sales at actual exchange rates

Foundations for long-term profitable growth (Richard Holder, CFO)

Over the next five years (by 2014/15) we plan to...

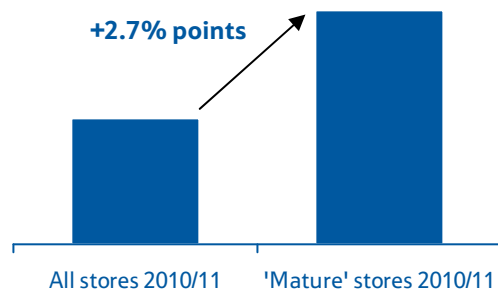
- More than **double** the number of hypermarkets to over 200:
 - Similar to the number of Extra stores in the UK today
- Almost **triple** the number of customers per week to c. 12m:
 - Still less than 4% of the urban population of our three Regions
- **Quadruple** sales to c. £4 billion p.a.:
 - Similar to Korea today
- Deliver significant levels of profitability and returns:
 - As stores mature and economies of scale are realised

The road to improved profitability is clear

'Mature' stores already at good levels of profitability...

- Similar 4-year maturity curve to other countries
- Rapid growth in new stores will mean high proportion of immature space for the foreseeable future

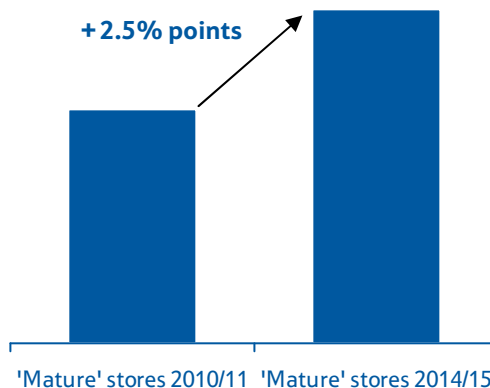
Store profitability (%)



... which we expect to improve further as the business matures

- Improved profitability from:
 - Investment in centralised distribution
 - Own-label
 - Direct sourcing
 - Data & insight: dunnhumby
 - Superior formats and locations

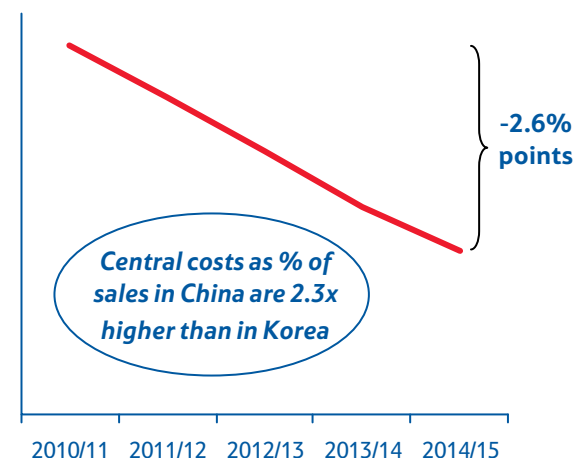
Store profitability (%)



Growing scale will bring cost efficiencies

- Central costs as % of sales planned to fall 2.6% points over five years due to:
 - Rapid growth in space & sales
 - Tesco Operating Model
 - People capability
 - Organisation structures

Central costs as % of sales



With our low-capital leasehold model, we expect returns to increase rapidly as profitability improves with scale

The building blocks towards greater success

- Customer insight
 - using dunnhumby to respond first to changing customer needs and lifestyles as incomes rise
- Regional structure
 - succeeding in a country the size of a continent requires local customer and operational focus
- Integrated supply chain
 - provides a unique competitive advantage, bringing scale and infrastructure to deliver great products and prices for customers
- Operating Model
 - proven, efficient and effective Processes, Systems and Organisational Capability to enable rapid growth at lower cost ratios
- Local leaders
 - the winning combination of in-depth local market knowledge coupled with Tesco Values, leadership and operating skills
- Focus on delivering over the long term
 - investment and decisions that will provide a strong base for generations of customers
- High quality property
 - a unique strategy for future-proof retail developments