
Best Practice

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Tesco.com

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Abstract

Tesco has been established in the UK grocery trade for many years, and assumed market leadership five years ago. Tesco Direct was launched in 1996, offering home delivery of groceries. The service was rolled out across England and Wales, and into Scotland, by late 2000. Initially ordering by telephone, fax and Internet was offered — but the Internet provided the best business model. Tesco.com was formed in April 2000, to include the Tesco Direct operation, plus Tesco Home Shopping (a 60:40 venture with Otto Versand, offering electricals, homeware, clothing, gifts, books and CDs) — plus Tesco Personal Finance. Thus a very wide merchandise range can be offered, without the need for expensive (and time-consuming) physical store development. Tesco has leveraged its existing consumer franchise to become the largest online grocer in the world; and has shown the majority of dot com start-ups a clean pair of heels in terms of fulfilment expertise and profitability.

Keywords: dot.com, bricks and mortar, loyalty card, fulfilment, e-commerce, 'virtual store', ambush marketing

Threat to traditional retailers from dot.coms

Introduction

At the height of the dot.com hype, it was being suggested that traditional retailers were under threat from start-up dot.com operations, which would effectively steal their business. As we know, the more extreme dot.com bubble burst in spring 2000 — but how does this scenario look a year later?

In the USA, where the Internet revolution started, the Peapod online grocery shopping organisation was held up as a pioneer in one-to-one marketing (it was used by Don Peppers as one of his case studies when he addressed conferences in the UK in 1995). In the event, Peapod has struggled; consumer membership still only numbers some 100,000 (after ten years) and, after a problem with financing in March 2000, Peapod has sold a majority stake to Royal Ahold. Also in the USA, Webvan gained a very high profile (in 1999, Webvan was expected to take the US market by storm); but this year, Webvan's losses are expected to amount to £45m on sales of £7.4m and its share price has collapsed. In New York, Urbanfetch and Kozmo, who promised one-hour delivery of convenience foods, CDs and videos, have seen their early promise collapse, and they have retrenched into business courier services in Manhattan.¹

Meanwhile, Tesco, a traditional retailer if ever there was one, has developed what is by common consent the most successful online grocery retailer in the world. Even in the USA, there is praise for Tesco's operation; Gomez, the Chicago-based Internet quality measurement company, said 'There are executives at a lot of US retailers wishing they

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knew how Tesco has done it, with its 750,000 registered customers and 60,000 online orders per week.’²

Transformation of Tesco stores

Background

To say that Tesco stores have been transformed over the last two decades would be a massive understatement. Going back even further — to the late 1960s, in fact — the author’s first-hand experiences as a supplier to Tesco (at the sharp end) were probably typical. Doing a marketing apprenticeship at Cavenham Foods, the writer spent the regulation period in the salesforce, selling to the grocery trade. The supermarket sector was relatively small, both in the sense that independents and Co-ops were still a major force, and also in the sense of absolute store size. Multiples like Tesco, Victor Value and Fine Fare were typically 2,000 square feet, as against the 20,000 square feet that is the norm today. Tesco stores followed Jack Cohen’s dictum of piling it high and selling it cheap — they were generally untidy jumbles of stock, plastered with dayglo price stickers and promotional messages. But the worst aspect, to a young trainee rep, was the store managers. A popular opinion among grocery reps was that the only criterion Tesco used in choosing managers for their stores was to find the biggest bully (other descriptions are not fit for the pages of this august journal). The ones the author met could certainly not be accused of being professional.

Checkout launch in 1977

Ten years on, in 1977, the author witnessed the dramatic launch of Tesco’s Checkout from the vantage point of another grocery supplier, RHM Foods. Over the intervening ten years, Tesco had moved on — but not dramatically. But the Checkout launch, involving the dropping of Green Shield Stamps and the implementation of a low-price strategy, also heralded a much more fundamental change to Tesco, masterminded by Ian McLaurin. Tesco became much more professional — but developed its strategy in an intriguing way. Without losing its traditional price-conscious shoppers, it traded up its offer to appeal to a middle-class audience in addition. It still sold ‘value’ lines at low prices, but its range was extended to include higher-quality, more aspirational products at higher prices.

Back in 1977, Tesco and Sainsbury were poles apart, in almost every sense. Sainsbury was solidly middle class, carrying forward the imagery of the marble-topped grocer’s stores of a decade earlier; Tesco was working class, cheap and cheerful. Over the 18 years to 1995, Tesco up-traded gradually, until at the point when it seized market leadership on the takeover of William Low, it seemed quite natural that Tesco should be market leader. It sneaked up on Sainsbury without the latter apparently noticing. In the five years since, Tesco had retained the initiative, and the margin of its lead has increased each year. Even the entry of Wal-Mart into the UK market, via its takeover of Asda, has not noticeably impacted on Tesco; indeed Tesco’s chief executive, Terry Leahy, commented ‘We’re not in the least scared of Wal-Mart. We’re very, very proud of what we do. We’ll enjoy competing with them.’

Launch of clubcard

Tesco launched its Clubcard loyalty card in the same year that it gained grocery market leadership; this may have been a coincidence, but then

Use of clubcard database for cross-selling

again, there is no doubt that it wrong footed Sainsbury (who can forget Sainsbury's scornful comments on news of Clubcard's launch, to be followed some months later by Sainsbury's me-too loyalty card?). Tesco seems to have gained first-mover advantage with Clubcard — although it clearly carried a substantial cost, the fact that Tesco has been able to use the Clubcard data to develop customer segmentation, and promote to these segments, suggests that Clubcard has become a central plank in Tesco's marketing strategy. The Clubcard database is also a very valuable tool from which to cross-sell new products and services, such as its credit card and Tesco.com (see later).

Clubcard acts as a reward to regular shoppers (which is, of course, its customer-facing function), but it also facilitates detailed analysis of customer transactional behaviour, the make-up of 'shopping baskets', and the purchase of other products and services from Tesco. Given Tesco's stated aim as expressed by chief executive Terry Leahy, 'We work towards one core purpose: to create value for our customers, to earn their lifetime loyalty',³ while true loyalty will be created by the Tesco 'product' itself (the combination of products, service, price and shopping experience), the role of Clubcard is to aid Tesco's understanding of its customers, and to facilitate cross-selling and upselling.

In addition to Tesco's success in the UK grocery market, it has expanded internationally, particularly in the former communist countries of Central Europe, and in Asia; it has publicised its aim to be 'as strong in non-food as in food'; it has moved into financial services; and, from a standing start in 1996, it has grown the world's largest Internet grocery business.

Initial launch of Tesco Direct

Tesco Direct was launched in 1996, initially in the south-east of England, offering home delivery of grocery items. The initial model used telephone, fax and Internet ordering, but it became clear at a fairly early stage that telephone and fax ordering were tricky in operational terms, so the service was developed as Internet only. The service was rolled out gradually across the rest of England, served by batches of stores (fulfilment of Internet orders is from stores, rather than from specialist warehouses). Tesco Direct moved into Scotland in early 2000.

As in any new venture there were initial teething troubles, as Tesco subsequently admitted. Product availability, system downtime and mistakes in order fulfilment (plus some goods damaged in transit) were some of the early complaints; and, a particular bugbear, unacceptable waits for delivery slots. The company worked hard to iron out these problems, and to persuade early triallists who were put off by these problems to try the experience again. Particular efforts have gone into the capacity and timing of grocery fulfilment, even including the mobilising of delivery vans for 12-hour periods on Sundays in trial areas.

Starting singlemindedly with grocery, Tesco Direct then moved into other merchandise areas. Tesco formed a joint venture with Grattan (the latter now owned by Otto Versand, the largest catalogue retailer in Europe) called Tesco Home Shopping, which offers five 'departments': mother and baby, home furnishings, clothing, gifts and electricals. The

Fulfilment from Tesco stores

Move into non-grocery merchandise

electricals offer was launched as recently as September 2000, and is apparently 'exceeding expectations'; prices are very keen, as the direct-sell operation benefits from the Tesco branding without attracting the overheads that are 'enjoyed' by store-based retailers. Other non-food departments — entertainment and books — are sourced directly by suppliers. In fact, Tesco.com is now a very broadly based business, and by no means 'just' the Tesco store offer.

Tesco.com — The business

Tesco.com was formed in April 2000 to include:

- Tesco's online grocery business, formerly Tesco Direct;
- Tesco Home Shopping (a 60:40 joint venture with Otto Versand);
- TescoNet ISP (Internet service provider);
- Tesco Personal Finance (a 50:50 joint venture with the Royal Bank of Scotland).

Contrast with dot.com start-up

It is interesting to note the fundamental difference between the formation of Tesco.com and the typical dot.com start-up. Tesco.com was spawned by a business that had already demonstrated major success, and had already trialed (if not quite perfected) home delivery. Tesco.com has *not* spent heavily on advertising — far from it — but has cross-sold from its existing operation. Tesco has a very strong track record in logistics and supply-chain expertise. And the typical dot.com start-up? Enough said.

Putting some numbers to the current Tesco.com offer, by early December 2000 the service:

- had over 750,000 registered users
- received over 60,000 orders per week
- was available to 90 per cent of the UK population
- was forecast to achieve a turnover of £200m in the current financial year.

The product/service offer includes:

- grocery — over 20,000 products available
- books — over 1.2 million titles available
- entertainment — over 160,000 CDs, plus a wide range of videos, computer games and DVDs
- electricals — over 1,000 electrical products, both brown and white goods
- clothing — a range of workwear, sportswear and leisurewear for children and adults
- home — products ranging from furniture to drinks accessories
- gifts — over 1,000 Christmas gift ideas
- mother and baby — hundreds of products for babies, toddlers and expectant mums
- personal finance — a range of loans, mortgages, credit cards, savings products and insurance policies.

Tesco Personal Finance now has 1.7 million customers, and has just broken even. At the time the half-year results were published (September 2000) Tesco.com had incurred a loss of £6m on a turnover of £85m as it continued to expand geographically; the grocery offer was being fulfilled from about half of the chain's 669 UK stores. It was announced in the half-yearly report that the home delivery service had completed its millionth order, and was available to 90 per cent of the UK market.

Rationale for Tesco.com

Given Tesco's success as a 'bricks-and-mortar' retailer, and its impressive expansion overseas, why did the company decide to venture into e-commerce? Was this not a potential threat to its core business? Part of the rationale can be seen in a key plank in Tesco's group strategy — 'follow the customer' by embracing new products and services, respond to changing customer shopping habits, and, where possible, anticipate them. So there was clearly a segment of the UK shopping population that was interested in home shopping; there was also a potential for e-commerce, which proved to be the most efficient way to offer home shopping. When Tesco 'got into the Internet' seriously, there was a general uncertainty as to just how big e-commerce would be, and over what time scale. John Browett, Tesco.com's chief executive, was quoted as saying 'it's difficult to know whether its going to be 2 per cent or 50 per cent, or whether it is going to happen in three years or 20'.⁴ Hence Tesco's approach of 'setting up a sensible business which we can very dramatically expand if demand takes off'.

Pragmatic approach

Another key part of the rationale was the opportunity presented by e-commerce to get into non-foods in a much bigger way, *without* the need to build more stores in the short to medium term. Tesco's current share of the UK non-food market is 3 per cent, and it aims to double this to 6 per cent over the next three years. While there is a considerable non-food range in the stores, particularly larger stores and hypermarkets, planning restrictions and investment requirements limit the degree to which Tesco can expand physical store size, whereas Internet shopping has no such constraints. As mentioned earlier, fulfilment of most non-foods by Tesco.com is undertaken by Grattan, and the remainder by suppliers directly, so there is no impact on Tesco stores. Large electrical appliances represents a good illustration of a merchandise area where Tesco.com's 'virtual store' is able to compete profitably with the existing electrical retail giants.

'Virtual store'

The Internet is an efficient way for Tesco Personal Finance to trade, and a growing share of the financial services market is moving in this direction. Again, Tesco can provide what a sizeable segment of its customer base wants by making Internet transactions available. Clearly, the Tesco Personal Finance credit card is a good mechanism for paying for online transactions, keeping the value within the Tesco organisation.

Tesco is rapidly expanding its international operation, and an Internet offer — in addition to physical stores — could significantly enhance its opportunity. A trial in Eire started in Dublin and Cork in October 2000 (through tesco.ie), and the emerging economies of Taiwan and South

Korea — where Tesco is enjoying spectacular growth — might offer tremendous scope for Internet shopping. South Korea, in particular, has high Internet penetration and high housing density. According to Russell Craig of Tesco Corporate Affairs, speaking in December 2000, at present, Tesco are looking at overseas markets for Tesco.com, but have not expanded it any further than southern Ireland and the UK

Website and fulfilment

The Tesco.com website is ‘a very impressive, well laid-out site’ according to a survey compiled for *Marketing Week* by BrandNet; the Tesco.com site came top of a list of the top 50 UK retailers based on advertising spend.⁵ The survey also commented on the interesting content and secure online buying offered by the site. The author has been similarly impressed by the site; it packs in a great deal of intriguing promotional information, while still managing to appear uncluttered. And it is very easy to navigate. The only problem encountered was a failed attempt to locate a particular book on the ‘quicksearch’ facility, although the (new) advanced search feature found it instantly. All the components of Tesco.com appear on the homepage, all seem appealing (see Figure 1). The Tesco.com site won a Yell UK Web Award for the ‘Best business to consumer e-commerce site’ earlier in 2000.

Impressive website

There is an option, when ordering groceries, to utilise a free CD-ROM disk which enables orders to be filled out offline before sending the order to the website. Tesco’s grocery fulfilment — picked from stores for home delivery — has come in for much comment. Its competitors have adopted the more usual practice of picking orders from dedicated warehouses. Tesco’s rationale for its chosen method seems to have been entirely pragmatic: store-based picking gave the company the twin advantages of speed to market (they could roll out the service around the country from their existing store network), and no need to construct purpose-built warehouses at high cost unless and until the demand proved to be there. A recent *Sunday Times* article⁶ contains some useful insights from John Browett, chief executive of Tesco.com: ‘Three years ago we were sitting around wondering why everybody else was going for picking centres when the economics just did not make sense for us’; and later ‘We are not against picking centres. It is just that you need the volumes to justify them.’ Given the potential problems with grocery fulfilment, Tesco has developed a system to optimise its operation; partly by managing customer expectations, and partly by sophisticated journey scheduling. Delivery time-slots now run from 8.00am to 10.00pm, seven days a week. When customers go online, they can see which slots are available — they must complete their order at the same time as booking a delivery slot. Slots are allocated on a first-come, first-served basis, and customers can normally order two or three days in advance. The website suggests possible substitutes on the electronic order form — ‘we want to get customers into the mindset that there may be some substitutions’, says Russell Craig. ‘Naturally, substitutions do happen, but it’s the same in-store, or in a warehouse; while we aim to minimise it, it’s a fact of life in grocery retailing.’ Journey scheduling is arranged on a store-by-store

Economics of picking centres vs. stores

TESCO home shopping news & features talking Tesco register & sign in help

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Videos & DVDs
Computer Games
Baby & toddlers
Homeliving
Electrical
Wine Deals
Tesco Vin Plus Calais
Clubcard
What's in store
Organics
Tesco Personal Finance
iVillage UK New!

welcome
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Figure 1: www.tesco.com

basis. A GIS system analyses customers' home postcodes to establish locations, and then plots circular delivery routes, based on delivery time-slots. The system can take local road conditions into account.

The larger part of Tesco.com's non-food offer is supplied via the joint venture between Tesco and Grattan. So Grattan — with its existing high-tech warehousing and distribution operation — supplies the fulfilment for mother and baby, home furnishings, clothing, gifts and electricals. These items are also available via in-store catalogues. The other non-food departments (eg entertainment and books) are fulfilled directly from the suppliers, and the relationship is managed by Tesco.com (Figure 2).

An experiment is currently being conducted (December 2000) with store pick-up by customers; that is, customers order online but pick up their own groceries from the store. Presumably, some customers will welcome the removal of the need to shop in the store, but will be prepared to pick up their order rather than having to be at home for a specified delivery slot. The trial commenced in October with one store, and is now

Experimenting with store pick-up by customers



Figure 2 Tesco.com electrical

being conducted in ten stores; but as yet the results have not been analysed. Interestingly, Sainsbury had trialled a similar scheme, but abandoned it because they found little demand.

Marketing

The importance of Clubcard to Tesco — and as a recruitment tool for Tesco.com — has been mentioned previously. Promotional leaflets for Tesco.com are inserted in quarterly Clubcard mailings, and explain in very straightforward terms how easy it is to shop online and how to get started. Special offers from each department are promoted in the leaflets, thus accentuating the range of products available from Tesco.com.

Clubcard points can be gathered online, so Tesco regulars are able to accumulate additional points by shopping at Tesco.com. A new e-Clubcard scheme is currently being trialled; it is possible to redeem Clubcard points through this mechanism, and Tesco.com will award bonus points for shopping at the sites of online partners. In mid-November 2000, Tesco.com announced distribution deals with both MSN.co.uk and Yahoo.co.uk; this entails Tesco.com featuring on ads on

e-clubcard trial

MSN and Yahoo, and developing other links to the Tesco.com site. Thus Tesco.com's profile will be raised on two the Web's most visited destinations, and the range of Tesco.com's products will be promoted across both sites.

Promotional activity

Because of its existing high awareness and usage, Tesco does not need to spend heavyweight advertising money on Tesco.com — unlike start-up dot.coms. The current Tesco shoppers' audience is sufficient to get Tesco.com off to an excellent start — especially when cross-promoted via Clubcard mailings and pushed out to conventional media via the Tesco PR machine. Online advertising (and links such as those mentioned above) drives traffic to the Tesco.com website; clearly, other Internet users (other than Tesco store users) are potential customers for Tesco.com. Interesting statistics from recent statements: John Browett was quoted in September 2000 as saying 'Fifty per cent of the sales which come through on the grocery business are new to Tesco', and in October Terry Leahy, chief executive of the Tesco Group, said 'about 30 per cent of our customers shop nowhere else online'. Carolyn Bradley, chief operating officer of Tesco.com, said in October 2000 that the service was recording an average basket size four times the average recorded in Tesco stores.

Joint venture with iVillage

The latest marketing initiative from Tesco.com is a link to iVillage.co.uk. Although this was announced in July 2000, it actually went live at the end of November. The parent company of the new iVillage.co.uk is iVillage.com, which was founded in the USA in 1995; iVillage.com is the leading women's portal in the USA, with 10 million individual users per month, over 3,000 message boards, and a 2,000-strong team of 'community volunteers'. Thus, it seems to have achieved a virtual 'women's magazine on the Web' status, with strong editorial content and a strong sense of community. iVillage.co.uk is setting out to replicate that in the UK, and clearly Tesco.com wants to share in that aim, having taken a 50 per cent joint-venture stake in iVillage.com. Tesco has recognised that the 'content' skills required to succeed in online publishing are very different from Tesco's undoubted retail skills; as John Browett said in November,⁷ 'iVillage does something that we find very hard to do'. Tesco do not want to 'control' the venture — they accept iVillage's publishing expertise. So the Tesco.com online offer will be integrated into some, but not all, of iVillage.co.uk's channels (one example being the cookery section, where recipes will feature a 'click-to-buy' purchase mechanism that puts the specified ingredients into the customer's Tesco.com shopping basket). This joint venture could prove to be a very powerful partnership, given Tesco's existing consumer franchise and the proven expertise of iVillage in creating a women's community online.

Competition

The UK online grocery market has already seen casualties; both Budget and Somerfield (the latter with its 24/7 offer) have already pulled out, declaring it non-viable. Waitrose has taken a different tack, delivering to people at their workplace, and seems to have been relatively successful given Waitrose's small share of the overall UK grocery market (around 2

UK online grocery casualties

per cent, versus Tesco's 15.6 per cent). Sainsbury, now the UK's second largest grocer, is developing its online service, but seems to be moving much more slowly than Tesco. This may in part be due to Sainsbury's decision to distribute through dedicated warehouses, rather than stores (it opened a new 185,000 square foot picking centre in Park Royal, north-west London, in autumn 2000). Clearly, it takes time (and money) to develop such facilities; Sainsbury's expect that the online grocery market will be huge (£7.5bn by 2005⁸). Asda, the third largest player in the UK grocery market, is also developing its online offer, as is Iceland; the latter has hyped its online operation very successfully, even changing its store fascia to Iceland.com. Hard figures are difficult to come by, but indications are that Tesco has a strong lead over all its rivals (Tesco is not shy about quoting numbers, claiming 750,000 registered users and over 60,000 orders per week).

Recent developments

Apart from the recently launched experiments mentioned above (e-Clubcard, and store pick-up by online customers), Tesco.com is trialling MyWeb software from Autonomy. MyWeb, which is included on the CD provided by Tesco to facilitate offline order compilation before going online, alerts users of any retail site to better offers on the Tesco.com website. A message pops up while the user is on a competitive site — ambush marketing! This initiative was launched in October; when asked about progress in early December, Russell Craig of Tesco Corporate Affairs explained that customer feedback was still being gathered on usefulness, so no further information is available at this stage.

Ambush marketing

A revamp of the Tesco.com website in October 2000 added a personalised express shopping feature which enables the online shopping order to react 'intelligently' (for example, a customer typing in 'potatoes' would be offered a drop-down menu showing their usual order type), plus other features such as personal recommendations and a personal recipe book, with a facility to add ingredients to the shopping basket automatically. The express shopping search engine can retrieve the price and name of every brand of a product, making online shopping simpler.

In November, Tesco.com announced that it will be selling cars online from early in 2001. Sainsbury's already sells cars online (as do other, more traditional, auto retailers, of course) and is believed to sell about 100 cars per month. No doubt Tesco will wish to exploit its current online success by moving into other merchandise areas, even areas as distant from its current offer as the motor sector. Where next?

Factors for success

How and why has Tesco.com become the world's most successful online grocery retailer?

- By being a very successful 'offline' retailer first; its brand, product offer and consumer franchise were already very strong before it ventured online.
- By having very high awareness and saliency from its bricks-and-

**Relating store
purchases to online
purchases**

- mortar operation — it did not need to spend a fortune on advertising for Tesco.com.
- Because it had developed Clubcard into the leading grocery loyalty card, Tesco was able to leverage this into a strong online presence via cross-selling, and was able to relate customers' store purchases to their online purchases.
 - By fulfilling grocery orders from stores, it was able to roll home delivery out across the country rapidly, and, despite early teething troubles, was able to grow and consolidate this business to reach critical mass faster than its rivals.
 - By partnering with Otto Versand/Grattan, it was able to offer an 'instant' non-food capability, complete with efficient fulfilment. By partnering with iVillage, Tesco.com gains instant editorial credibility and expertise, a very different skill set from that of retailing.
 - Thus, by being pragmatic and ambitious in equal measure, Tesco has taken a lead in the UK market, and is well positioned for international expansion.

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