Bloomberg

Why Grocers Like Tesco Find Trouble in the U.S. Market

By Marc Levinson - Apr 3, 2013

Any day now, Tesco (TSCO) Plc, the U.K. grocery giant, may announce the closure of the 200 or so Fresh & Easy food stores it has opened in California, Arizona and Nevada since 2007.

When it does, Tesco will join a long list of international grocers that have met their match in the U.S. In every case, these companies wrongly assumed that strategies honed abroad would succeed in America, and they underestimated the resources and management attention required to make headway in a vast and fast-changing market.

The American grocery market has tempted foreigners for almost a century. One reason is the obvious potential: For a grocer that had exhausted the possibilities in its home market, expansion in the U.S. offered a means to boost profits. Many foreign companies have also arrived with a superiority complex, seeing hundreds of small, unsophisticated enterprises that seemed to be easy prey for international entrants with deep pockets and industry know-how.

Ambitious Canadians

Probably the first foreign chain to open in the U.S. was the Canada's Loblaw Cos. Founded in 1919, Loblaw opened self- service Groceteria stores around Toronto before moving into nearby Buffalo, New York, in 1924. By 1940, the Groceteria banner flew as far west as Chicago.

In 1953, Loblaw was taken over by the Canadian baking company George Weston Ltd., which had grand ambitions in U.S. retailing. It secretly acquired another Buffalo-area chain, Bells, to reduce competition, and then in 1956 took control of Chicago-based National Tea Co., which had more than 700 stores. Weston kept adding until its footprint stretched from Alabama to Minnesota. Profits didn't follow. Weston spent two decades extricating itself, finally selling its last U.S. stores in 1995.

While Weston was trying to find an exit, British American Tobacco was trying to enter. Like other cigarette manufacturers at the time, British American Tobacco had amassed a large amount of cash and was looking for ways to spend it. It chose to buy up U.S. retailers, including, in 1972, the Wisconsin department store and grocery company Kohl's Corp. Seven years later, when the German grocer Tengelmann took control of the Great Atlantic & Pacific Tea Co. (or A&P), alarmists warned of the impending European takeover of the U.S. grocery industry.

Both ventures ended badly, however. The founding Kohl family, which at first stayed on to manage its former stores, soon cashed out, and the cigarette guys realized they knew nothing about selling groceries. British American Tobacco sold Kohl's in 1983, a few years before abandoning retail altogether. The buyer was A&P, which went on a spending spree that covered up its deteriorating fundamentals. Tengelmann had badly misjudged A&P's weakness and couldn't escape. It eventually lost its entire stake after A&P filed for bankruptcy in December 2010.

Things went only slightly better for the French grocery chain Casino, which took control of the California grocer Smart & Final in 1984. Smart & Final had pioneered the warehouse-club concept decades earlier, but by 1984 its relatively small stores were already behind the times. Casino was an ambivalent owner, unwilling to invest enough to make the chain a major player but reluctant to give up. Competitive challenges in France eventually forced its hand, and it sold in 2007.

Two other big French food retailers, Groupe Auchan SA and Carrefour SA (CA), faced the same choice. Both brought the hypermarket format to the U.S. in 1988 with stores spanning 250,000 square feet. Their brands, of course, were unfamiliar to American shoppers, and both realized belatedly that making money in the U.S. would consume enormous resources. Carrefour gave up in 1992; Auchan held on until 2003.

Major Missteps

The British arrived around the same time as the French. J Sainsbury (SBRY) Plc bought the Shaw's chain in southern New England in 1987 and later took a stake in the Giant chain in Washington. Neither investment panned out well. As its position back home deteriorated, Sainsbury sold its shares in Giant in 1998 and got rid of Shaw's in 2004. At least Sainsbury made a small profit on its deals. London-based Marks & Spencer Group Plc took a loss on King's, the upmarket New Jersey grocer it acquired in 1988. In 2006, it sold the chain for barely half the price it had paid 18 years earlier.

Even the two largest international players in U.S. food retailing have made major missteps. The Belgian grocer Delhaize Group (DELB), which bought the Food Lion chain in North Carolina in 1974, has repeatedly gone through ill-considered expansions and restructurings. The Dutch grocer Royal Ahold NV, which entered the U.S. market by purchasing two Pennsylvania chains in 1981, has built a strong franchise centered on the Stop and Shop chain in the Northeast, but it stumbled badly expanding in the Southeast, where two of its acquisitions went bankrupt.

Of all the international ventures in U.S. food retailing, only two have unblemished records: Aldi Group, whose small stores offer a limited selection of products at very low prices, and the iconoclastic Trader Joe's, with about 400 stores. Both are in German hands, controlled by separate companies owned by different members of the Albrecht family. Their success may be due, at least partly, to both companies' private ownership. Without nagging shareholders to answer to, their owners were willing to experiment quietly until they found winning formats and then to provide patient capital for the chains to expand. Aldi entered the U.S. market in 1976, but 15 years later it had only about 200 stores, all in the Midwest. Its growth since -- it now has about 1,300 stores -- has been tightly managed to ensure the chain is profitable, not just big.

Tesco didn't enjoy the luxury of private, patient ownership. Every move, from its intensive market research to its construction of a huge distribution center, has occurred in full public view, and its investors are painfully aware that the company has lost perhaps $2 billion on its American adventure. No one is likely to buy Fresh & Easy as an operating business. But Tesco's store sites may end up in the hands of Aldi.

(Marc Levinson is the author of "The Great A&P and the Struggle for Small Business in America." The opinions expressed are his own.)

Read more Echoes columns online.

To contact the writer of this post: Marc Levinson at marclevinson1@gmail.com.

To contact the editor responsible for this post: Timothy Lavin at tlavin1@bloomberg.net.