

Breakaway

From England, Groceries to Your Door

Britain's Ocado is starting to thrive by selling its online shopping technology overseas



In a warehouse an hour west of London, robots zip across a grid of thousands of crates filled with groceries, picking up cartons of milk, heads of broccoli, tubs of lemon sorbet, cans of tomato soup, and whatever else Britons might want for dinner. The hundreds of robots—imagine a cross between R2-D2 and a dorm fridge—pluck the food and skitter over to banks of workers who pack the items into red plastic boxes for delivery to customers' homes. "Designing it all has been immensely complex," says Tim Steiner, chief executive officer of Ocado Group Plc, the fast-growing online grocer that owns the facility. "The infrastructure, technology, and software we needed didn't exist, so we created it."

The system has caught the eye of American supermarket giant Kroger Co., which in May bought 6 percent of Ocado and hired it to build

and operate up to 20 distribution hubs as Kroger takes on Walmart Inc. and especially Amazon.com Inc. in e-commerce. Kroger hasn't settled on details of the rollout but expects to start shipping groceries from an Ocado-run warehouse in two years. "There's no doubt that Ocado's infrastructure is the best way for Kroger to deliver," says Kroger CEO Rodney McMullen.

Coming on the heels of similar contracts in France, Sweden, and Canada for everything from the robots to the software that gets groceries to shoppers' homes within a one-hour window, the Kroger deal marks a breakout moment for Ocado. The company has spent the past five years seeking, and failing to close, such deals with supermarket chains worldwide. Since November, as Ocado has started to look more like a tech company than a marginally ►

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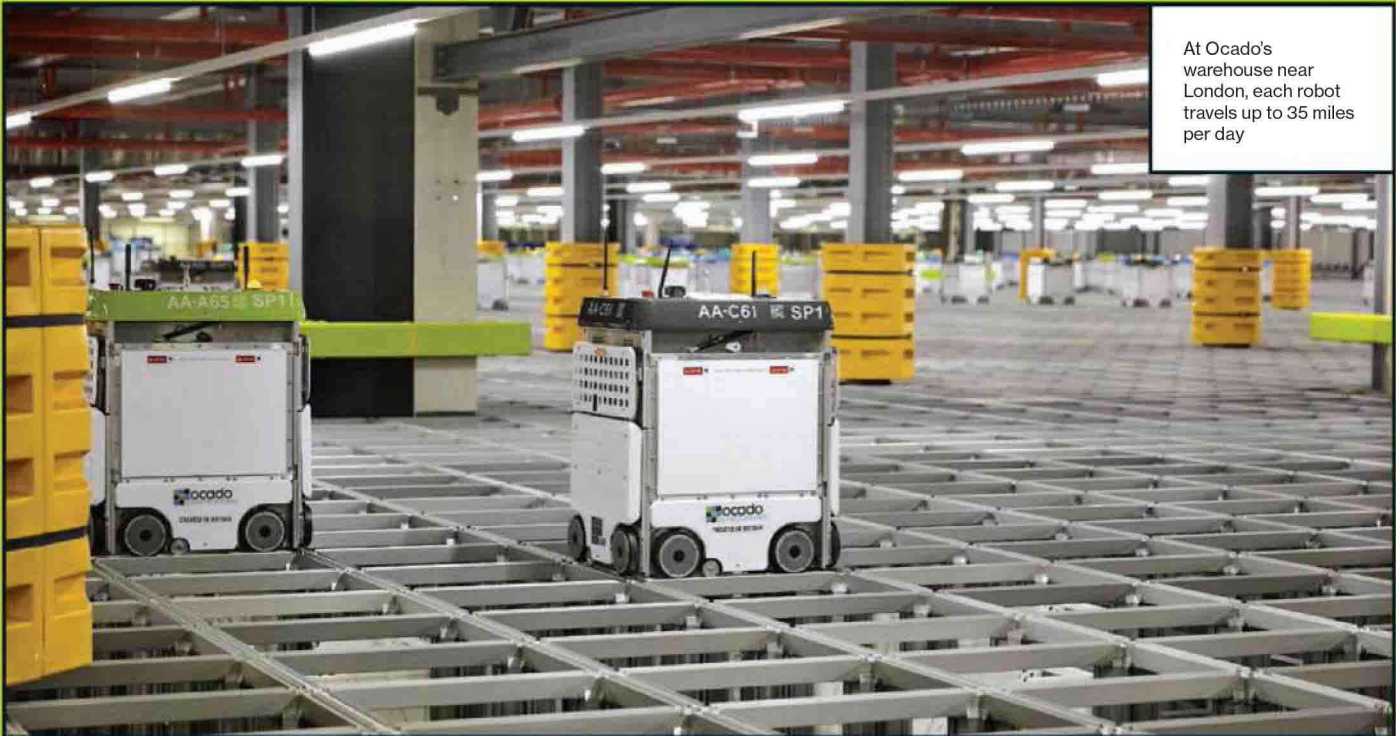
SOLUTIONS

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At Ocado's warehouse near London, each robot travels up to 35 miles per day

◀ profitable grocer, its share price has more than quadrupled. That's catapulted the company into the U.K.'s benchmark FTSE 100 stock index and confounded skeptics who said Ocado was spending too heavily and would never become profitable. "They've proven the doubters wrong," says Richard Bernstein, a fund manager at activist firm Crystal Amber Fund, which holds a stake in Ocado. "Here is a little British company that's managed to do a deal with one of the biggest global retailers."

The turnaround, CEO Steiner says, can be attributed to Amazon's \$13.7 billion acquisition of Whole Foods Market last year. After the purchase, supermarket executives worldwide looked across their aisles of veggies, dairy, and meat and saw the risk of becoming the next Barnes & Noble or Borders Group. "Amazon had previously made no impact in groceries, so grocers were able to sit back and think food is different," Steiner says. "People have realized online is not going to be 1, 2, or 3 percent of their market. It's going to be 10, 20, 30, or maybe even 60 percent."

In 2000, Steiner quit Goldman Sachs Group Inc. to set up Ocado with two fellow bankers. He figured Ocado could expand by licensing its technology to grocers overseas and avoid the expensive international failures of British retailers such as Tesco Plc and Marks & Spencer Group Plc. But Steiner vastly underestimated the complexity of storing, picking, and transporting foods ranging from produce to Popsicles to Pop-Tarts and delivering it all to customers at a specified time. "With the benefit of hindsight, it was insanity," he says. "It would have just been easier to stay at Goldman trading bonds."

For the past 18 years, Ocado has battled Tesco and

Walmart's Asda to win web shoppers in Britain, where more than 7 percent of grocery sales are online, about four times the share in the U.S., researcher Kantar Worldpanel estimates. Ocado gained a reputation for reliability and upmarket fare that lured young, affluent customers, but building its system was expensive: Although grocery revenue last year grew 12 percent, to £1.3 billion (\$1.7 billion), Ocado has logged £847 million in capital expenses since 2011, and in 2016—its best year—it saw just £12 million in pretax profit. Around the time of its initial public offering in 2010, Philip Dorgan, an analyst at brokerage Ambrian Partners, said, "Ocado begins with 'o,' ends with an 'o,' and is worth zero."

With backing from the likes of Swedish billionaire Jörn Rausing and former George Soros associate Nick Roditi, Steiner managed to keep spending. But even as shareholders have cheered the Kroger deal, it's provided more ammunition for detractors as Ocado has declined to offer forecasts of the financial benefits for fear of compromising negotiations with other prospective partners. "There's very little visibility on the details," says Clive Black, an analyst at Shore Capital Group Ltd. in Liverpool. "What history has taught us about Ocado is don't expect much on the financial side." Steiner brushes off the criticism, saying Ocado is growing faster than ever and he's getting calls from around the world. "No one has put together what we have," Steiner says. "Once people understand the economics, the question is, 'Can I have it?'" —*Sam Chambers*

THE BOTTOM LINE As Amazon steps up its focus on groceries, Ocado has inked deals with Kroger and other overseas supermarket chains after years of struggling to sell its distribution systems abroad.