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CLEARDEMAND

How Low Should You Go?

Navigating the ever-more-complex world of pricing

by LEN LEWIS

Pricing remains a cat-and-mouse game between retailers and consumers — a race to the bottom affected as much by consumer attitudes as the state of the economy.

"It was worse than ever last year and it started earlier," says Paula Rosenblum, managing partner with RSR Research. "You know you're in trouble when the biggest shopping day of the year is the day after Christmas."

James Sills, CEO of pricing and promotions management firm Clear Demand, notes that the 2014 holiday season is a good example of the continuing conundrum. Some retailers even priced below Walmart and Amazon, "But you have to ask yourself, 'How can you make money when you're virtually giving away product?'" he says. "It's simply not a sustainable position."

The question among retailers is not "How low can you go?" but "How low should you go?"

IDENTIFYING VALUABLE CUSTOMERS

The solution, while not assured, will require retailers to adopt multiple strategies and tactics, according to industry experts. Among them are analyzing customers' needs, basing prices on product value and benefits, evaluating costs so items aren't priced too low, personalizing promotions and prices, focusing on customer loyalty and engagement, and adjusting prices based on margins rather than just sales.

In an online survey of over 5,000 consumers conducted in October by RSR Research, respondents were asked about the factors influencing shopping behavior. The thrill of finding the best deal was most often the reason given for purchase.

"If your promotions are utilitarian money-saving offers, you're singing the wrong song," says RSR managing partner Nikki Baird. "As the economy improves, people aren't cherry picking to help the budget. They're cherry picking because it's fun. Either you need to make promotions less fun in order to wean them off it, or consider ways to feed the beast — let them feel like they won."

Lowball pricing can be a worthwhile tactic for driving traffic with the intent of building the basket, says Sills, but many retailers are needlessly giving away money. "There are ways to segment and incentivize people to come to your store and identify the most valuable customers."

Jenn Markey, vice president of marketing for price monitoring firm 360pi, says the recent holiday season saw less price volatility and fewer "kneejerk" reactions by some retailers, generally because deals started earlier and promotions were spread out over November and December. "However, I agree that a low price is not necessarily what consumers want all the time," she says, "and not necessarily where retailers should make their margins and revenues."

Retailers need a better understanding of how their prices are perceived in the market, what their brand promise is and how it translates to pricing.

"If you want to look at an extreme case, I think Nordstrom and Walmart would be horrified if either one was perceived as having the price strategy of the other," Markey says. "Retailers that don't want to be the low-cost provider in the market don't necessarily need to offer the lowest prices. It wouldn't be true to their brand promise to consumers."

Even retailers that want to have a low-price image don't have to be the lowest on every single item out there, she says. "Retailers should look at carrying a unique assortment of nationally branded items. This could mean increasing their level of private label to compete."

GOING LOCAL

Markey says it's also important to recognize the role that different purchases play in the shopper's life. "You have to understand which items are trip drivers, either to the stores or online. If it's a trip driver, you want to be the low-price leader in the market and have a firm understanding of price ranges."

And in many instances price ranges themselves have shrunk over the past five years. "In some areas, where the price range on an item might have been 50 percent, it may be down to 5 percent."

On the other hand, you don't have to be the low-price leader for impulse purchasers, even if that's the perception a retailer has built up among consumers.

"If you want to be the low-price leader in electronics you need to have the best price for TVs, which everyone is comparing online. But it doesn't mean you have to be the lowest for all the accessories," Markey says. "It's a matter of presenting customers with a good offer for a basket of goods. It's important to understand the different roles that individual items play in achieving a low priced perception."

Localization could also bring back some stability to retail pricing. "When e-commerce started everyone defaulted to the average national price," she says. "Now, there's more opportunity for zone-based pricing. It's a way for retailers — even low-price leaders — to increase revenues and margins."

In a move designed to optimize local pricing recommendations, 360pi recently partnered with JDA Software to integrate 360pi's zone-based pricing intelligence for national and store brands with JDA's rule-based strategic pricing solution. It will convert 360pi's competitive pricing intelligence into internal pricing rules which retailers can use to "right price" their assortment.

Ace Hardware is doing very well with this strategy through its franchisees, Markey says. "They have good prices but not necessarily the lowest. They've adopted localized assortment, zone-based pricing and developed a strong private label. They understand what the acceptable price range is for items and don't try to be the low-price leader. They are doing everything right and producing record results."

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> **-Jim Sills, CEO, Clear Demand**

HONING CUSTOMER SERVICE

Sills agrees that lowball pricing is not necessarily the answer. "It's largely a matter of retailers staying within a specific price range … for example, be just 5 percent above or below a competitor's [price].

"It all depends on how sensitive consumers are to price gaps," he says. "We have the ability to measure how unit sales vary as a function of that competitive price gap. We can now optimize what that price gap should be by product and by category."

This type of dynamic pricing, more strategic than tactical, guides retailers on how fast they should reply to competitor prices and how unit sales will vary at different price points. "In the past a retailer would identify a like item at a competitor and set his prices relative to that," Sills says. "But today you can have 21 variations of Tide, and not every retailer carries the same things. … You have to understand all the substitutable products that competitors carry."

This requires an enterprise attribution framework. "There's too much pressure, too many variables, channels, competitors and products to continue standard pricing and merchandising practices," Sills says. "Leveraging intelligence is about depth, precision, agility — immediate access to information across all channels, all the time."

As to price transparency created by e-commerce sites: "The more that data scientists delve into [some online discounters'] pricing practices, they find that they've raised prices before Black Friday so they can lower them again," Rosenblum says. Amazon's challenge is not so much around its top line or gross margin on merchandise as it is around shipping costs.

"If you can provide adequate service, people will accept minor fluctuations in price," she says. "No one is going to quibble over $10 on the price of a TV at retailers who hone their customer service offering."

However, the so-called "dynamic pricing" practiced by some online retailers is simply not an option for traditional retailers — either online or in stores. "Consumers don't want to figure out what time of day to buy," Rosenblum says. "If you're an online retailer, there's nothing to stop you from changing prices nine times a day. All you have to do is flip a switch.

"There used to be a lot of talk about 7-Eleven in Japan changing shelf prices in the stores depending on time of day and traffic. My position is that the first time I'm standing in front of an electronic shelf label and the price goes up — it'll be the last time I'll shop that store."

In general, Sills believes pricing ties directly into value creation. "To make money, retailers have to differentiate themselves," he says. "Shoppers recognize value and the retailers that deliver it will be rewarded. Customer loyalty is about trust — not just price. But if your strategy and marketing claim you're a low-price leader, that trust is undermined when you're not.

"The question is, 'At what price does the consumer recognize that you're fulfilling that trust?' And if you're a premium or high service provider, what's the shopper's expectation on where you should be in terms of dollars and cents?" **STORES**

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