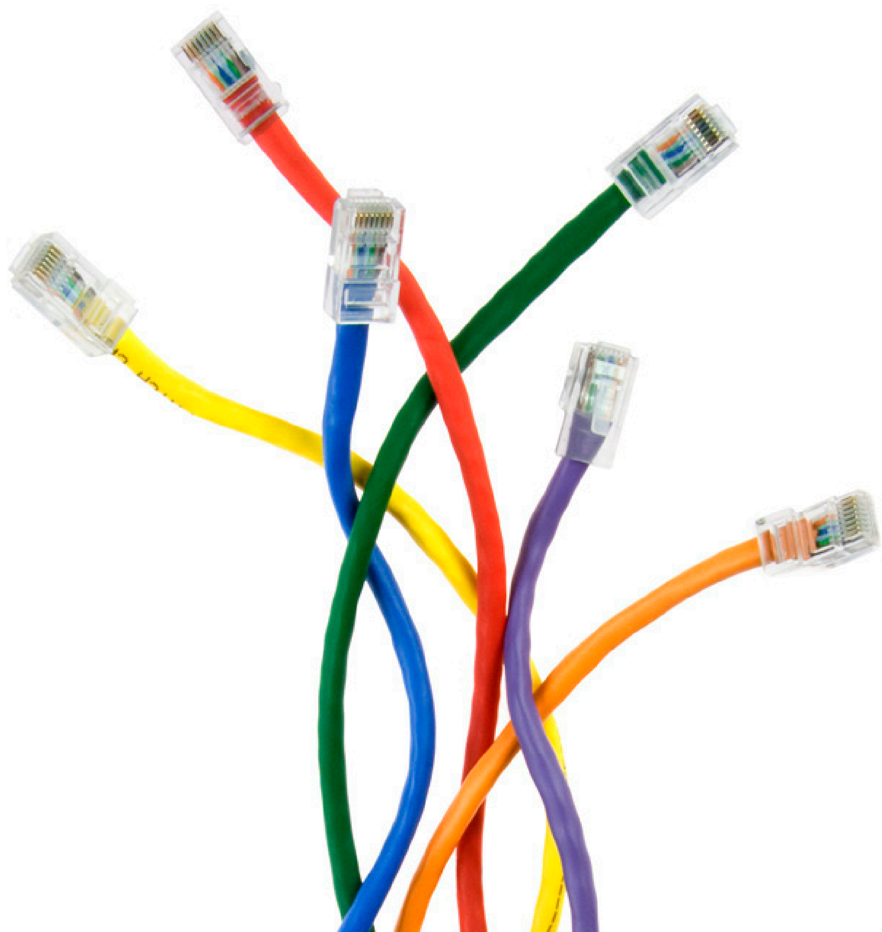
Pricing from ahead

Helping retailers win in the age of the connected consumer



Access to information through digital technology has changed the tide in retail. The traditional image of a customer wandering the aisles of a retail store comparing products and prices is replaced by the "connected consumer" who researches products online, goes to a store for some focused hands-on time (while comparing prices on a smartphone), and then buys the product through an online retailer with a digital coupon, free shipping, and quite possibly no taxes.

This shift is having a significant impact on nearly every aspect of the retail business. However, no area has been more affected than pricing. Advances in technology — coupled with new, low-priced competitor formats — are increasing price transparency, which is driving product commoditization and reducing many purchase decisions down to price alone.

Technology advances are also blurring the lines between market channels. Many of today's consumers can instantly access and share vast amounts of information virtually, making it easy to learn about and compare different brands, products, and prices — even while standing in a store.

Changes of this magnitude create obvious new threats; however they also create tremendous opportunities that may be harder to spot. What can retailers do to differentiate themselves in this challenging environment? From social media and mobile commerce to flash sales and group-buying, companies are trying to find something that works. Yet the efforts are often uncoordinated and missing a core strategy, resulting in nominal results and more insight about what *does not* work than what *does*.

It is important to focus on customer value, while developing new strategies that harness the speed of information sharing to create value both for your customers *and* your business. In particular, you can access an expanded set of data sources and apply advanced analytics to create agile pricing capabilities. This can help your business embrace future market shifts, while continuing to capitalize on many of the foundational strategies that worked well in the past.

Emergence of the connected consumer

The evolution and humanization of technology is connecting consumers like never before. People today are constantly linked to social networks through portable, easy-to-use devices that enable collaborative shopping experiences where consumers greatly influence each other. Smartphone ownership has already surpassed 60 percent among 25 to 34 year olds, and is growing fast in all age categories.[1] Additionally, the number of tablet users has taken off in just the last two years, recently surpassing the 30 million mark.[2]

Meanwhile, social media, as well as price comparison apps, have made it easier than ever for consumers to communicate with each other. People can use their smartphones to compare prices on a product while at a store, and then buy the product from an online retailer for a lower price.

The emergence of the connected consumer has fundamentally altered the retail environment. In order to compete effectively, retailers should become more connected themselves. They should be agile enough to capitalize on advances in technology, anticipating how technological changes are likely to shape social connectivity and consumer behavior. This can help to enable them to engage with consumers in a more compelling way through marketing and product/service offerings that are tightly linked to past patterns of behavior.

1 Nielsen. "Generation App: 62% of Mobile Users 25-34 own Smartphones." http://blog.nielsen.com/nielsenwire/?p=29786. November 3, 2011.

2 eMarketer. "One in Three Online Consumers to Use a Tablet by 2014." http://www.emarketer.com/Article.aspx?R=1008701. November 21, 2011.

Market trends

The rise of the connected consumer is causing three major shifts that are forcing retailers to rethink how they set prices. Although these market trends present clear threats to the *status quo*, they also create opportunities for retailers with the savvy to capitalize on them.

Trend 1: Speed of information sharing

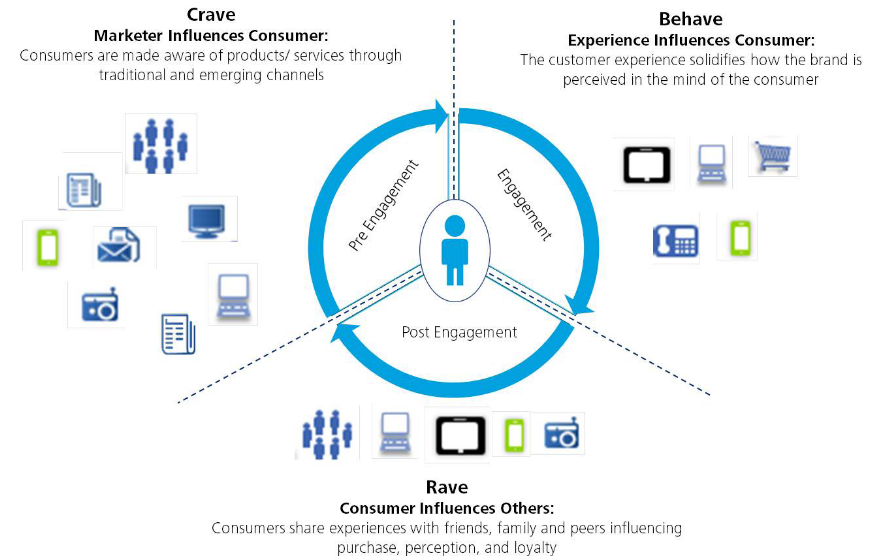
Consumers today can instantly share information across a wide variety of mediums, including social networks and mobile devices. A recent survey found that 28 percent of consumers use common social media platforms to learn about products, and 30 percent use these tools in their purchase decisions.[3] In fact, 10 million microblog posts per day are specifically about a brand or product. What's more, the platforms for product and purchase feedback are expanding, enabling consumers to connect to a larger and more dispersed audience than ever.

To maintain their pricing power, retailers should respond by increasing their own connectedness. That means capturing timely pricing input data, conducting and interpreting analysis, and then responding with competitive pricing decisions. These pricing capabilities should be fluid and responsive enough to account for real-time data shifts.

Consumers now expect immediate access to product and pricing information, and quickly notice if a retailer is not managing its pricing and product messaging in a timely manner.

On the flip side, retailers who harness technology advances to create agile pricing capabilities can find a wealth of valuable insight in the stream of data that connected consumers are constantly providing. The incredible speed of information sharing now allows retailers to make pricing decisions based on real-time input and feedback, while also enabling improved communication with customers before, during, and after the sale.

Figure 1: Example of purchase decision process and feedback loop



Source: Deloitte Consulting LLP

3 Rubin, Courtney. "Shoppers Combine Search, Social Media to Fuel Decisions." Inc. http://www.inc.com/news/articles/201102/half-of-consumers-combine-search-and-social-media-for-help-buying.html. February 25, 2011.

Trend 2: Blurring of market channels

Brick and mortar retailers now see exclusive e-commerce retailers as direct competitors, and in-store pickup of online purchases has become commonplace throughout the industry. In fact, half of all retail purchases or purchase decisions are made through direct, online channels (see Figure 2). This convergence — along with the rise of the connected consumer — is changing the sources of purchasing influence, with greater emphasis on social media and external influencers.

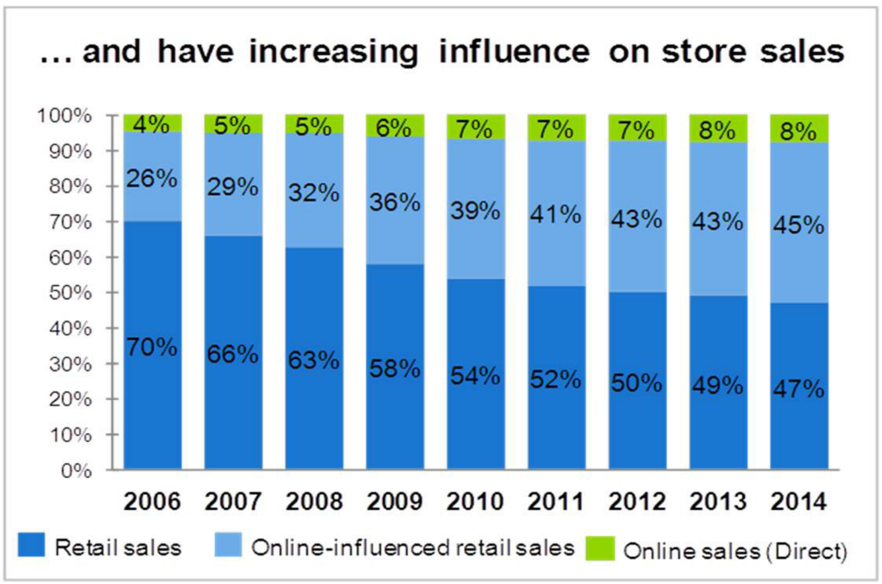
In response, retailers are beginning to adopt an omni-channel growth strategy that can accommodate the social, technological, and behavioral connectivity consumers have come to expect — and can do so more consistently across channels. This strategy improves retailers' ability to shape and interact with sources of external influence.

Yet even in an omni-channel environment, different consumer segments interact differently, which creates challenges for retailers looking to differentiate themselves to multiple segments across multiple channels. To be effective, retailers should consider making selective investments that are consistent with their overall brand and customer experience strategy. This requires an efficient, transparent, and coordinated pricing strategy to improve the shopping experience for multichannel customers and to earn their trust.

One pharmacy retailer has found that its multichannel customers are three times more valuable than single-channel customers. Similarly, a specialty apparel retailer found that multi-channel customers (26 percent of its total customers) represented 57 percent of its annual revenues.[4]

As channel lines continue to blur, retailers can use pricing strategies to increase the relative size of their multichannel customer base. To implement a targeted omni-channel strategy, retailers need effective metrics to help them set prices and evaluate channel performance. They should also look to capitalize on technology to boost sales through channel-specific promotions and product offers.

Figure 2: Influence on purchases



Source: http://www.marketingcharts.com/direct/web-influences-half-of-retail-sales-19730/groupm-web-sales-oct-2011jpg/: Deloitte analysis

4 "Elevating the Multi-Channel Retail Customer Experience." Deloitte. http://www.deloitte.com/view/en_US/us/4a4c8bed57912210VgnVCM100000ba42f00aRCRD.htm. May 26, 2010.

Trend 3: Commoditization of products

The connected consumer's improved access to information has led to a sharp increase in price transparency. Today's consumers can efficiently compare prices for the same or similar products across multiple retailers and channels. Retailers are responding by slashing prices (as a substitute for sustainable brand loyalty), creating a death spiral in which products are increasingly viewed as a commodity. This commoditization trend is further fueled by growth in the variety of product retailers, particularly disruptive price players.

Recent data shows that 21 percent of the shoppers surveyed are extremely interested in using a smartphone to compare prices.[5] To that end, downloads of price comparison apps have surpassed the 30 million mark, and are increasing at a rate of 1.7 million per month.[6]

Connected consumers are less brand loyal and more likely to adopt new retail formats in which price is the main selling point. Recent shopper surveys have noted a dramatic increase in the number of shoppers who use large retail stores as a "showroom," but then ultimately buy their products online through another company.[7] This trend is exacerbated by low customer demand due to a lackluster economy, which compels many retailers to sustain promotion-heavy sales mixes.

5 Xyologic and Deloitte analysis. 2012.
6 Deloitte analysis. 2012.

7 Consumer Electronics Association (CEA) and The Stevenson Company's TraQline shopper surveys. July, 2011.

Building a pricing strategy for the connected consumer

To neutralize the threats and capitalize on the opportunities created by the connected consumer, retailers should re-emphasize their focus on pricing strategy and think beyond only price optimization and price execution.

The first step is to define who you are as a retailer and what pricing capabilities you need. A broad approach to pricing based on traditional factors should give way to targeted efforts focused on customer value, action-oriented data management, and agile pricing capabilities. Questions to consider include:

Focus on customer value

- Who are you? What does your brand stand for?
- What is the value you bring to your customers?
- What do you want the customer experience to be across channels?

Employ action-oriented data management

- Do you know what data you need to set price strategies and prices effectively? Just as important, do you know what data you don't need?
- How will you collect and analyze the data?
- How will you measure channel-specific effectiveness of the strategies implemented?

Build fluid pricing capabilities

- What capabilities are needed to be fluid in setting prices based on channel and market shifts?
- How will you identify and prioritize pricing capability development?
- How can you better understand and leverage the vast new data sources available?

Strategic pricing capabilities can help you capitalize on three new market opportunities that arise from the connected consumer. Each of these opportunities can yield significant benefits for retailers who are prepared to capitalize on them, and flexible enough to continue doing so as these trends evolve.

Opportunity 1: Emphasize speed to value

Data is growing exponentially. From the volume of data and number of data sources to the variety of formats and ease of exchangeability, the data available to connected consumers is almost limitless. Although some businesses find this scary, others are guided by the old adage that knowledge is power. Yes, the explosion of data can empower the connected consumer; but it can also empower the retailer.

Connected consumers generate a wealth of data throughout the purchase decision lifecycle, from pre-purchase product research to post-purchase feedback. However, not all data is created equal. For a retailer, the trick is to determine what data really matters for effective pricing.

Two capabilities are important. The first is the ability to quickly capture, analyze, and interpret new inputs such as consumer sentiment that enable a retailer to go beyond foundational supply and demand principles. These new inputs will likely continue to expand and evolve, so it's imperative that these data skills be agile enough to keep pace. The second is the ability to serve as an active center of communication for connected consumers throughout their purchase decision process — in real time — regardless of their location or channel. This capability can take many forms, from offering individually targeted online promotions, to sending additional decision data to a customer's mobile phone as they walk through a store.

To bring effective speed to value

- Know what data you need — and what you don't
- Develop the skills to capture and interpret relevant data, quickly translating it into pricing decision inputs
- Be agile and adaptive, but avoid falling for hype or pursuing the trend *du jour*

Opportunity 2: Integrate channel strategies

Channel alignment strategies have evolved over time, from independent channels with the store at the center of the retail universe; to channel price alignment with varying degrees of assortment differentiation; to the current approach marked by channel-specific opportunities, increased channel integration, and greater focus on the growing online channel. As these strategies evolved, so did the data used to shape and measure the impact of channel pricing initiatives.

For each channel strategy, it is important to know what data is required and how it will be used. Also, because of differences between channels, you need an action-oriented data management approach to measure channel-specific effectiveness. Outputs feed the entire pricing process, from strategy development through tactical price setting and execution.

One department store recently capitalized on its ability to leverage information within and across channels to create a more effective promotion. The company's customer data showed that Justin Bieber and social media were value drivers for its targeted demographic. So when this retailer launched Bieber's new fragrance, it had him promote the event heavily through his social media accounts. This innovative strategy had customers lining up outside the store to attend the launch, boosting sales for the premium-priced product.

To effectively integrate channels:

- Establish a clear cross-channel pricing strategy
- Know what data you need to shape the overall strategy and specific price offerings
- Define a pricing scorecard that closely accounts for channel-specific nuances

Opportunity 3: Differentiate product pricing

As transparency drives prices down, retailers should consider using every means available to increase differentiation and decrease price sensitivity. This can help a company separate itself from the pack and protect the brand value it worked so hard to build. There are a number of ways to avoid a "race to the bottom."

To increase differentiation	To decrease price sensitivity
• Explore channel- and customer-specific offers	• Identify where price impression matters, and where it is not as crucial
• Leverage new information to gain insights into customer value drivers	• Leverage new information to set more targeted and effective promotions, and to measure promotion effectiveness
• Devise a holistic private label (or exclusive item) pricing strategy	• Develop a competitive price response strategy with clear tactics and rules

These approaches often work in tandem, or even overlap. Historically, many retailers applied them through trial and error (or preferably, test and measurement). Channel-specific promotions were often determined — or specific image items targeted — based on tribal knowledge from the merchandising organization. Although this *experience-driven* approach remains common, social media provides an opportunity for improvement. Social media information is not only valuable for its breadth and depth, but also for its immediacy. In the past, it required several weeks to obtain statistically significant sales data to support a decision or change. Now, new technologies can scour social media sites and blogs to more readily create actionable information. By better understanding what motivates their customers, retailers can leverage pricing and promotional tools more effectively — both for setting price actions and then measuring their effectiveness.

A denim manufacturer and retailer uses its various fan pages to connect customers with products. By allowing people to "like" particular products within its portfolio, this company obtains valuable data on customer preferences. They then use this information to create a unique and personalized customer experience. When a product goes on sale, or is linked to a promotion, they contact users who indicated an affinity for it. Customers get a sense of personalized attention, and often spend more money. This enables the company to recuperate some of its lost margin, shifts the focus away from price, and increases the stickiness of their products with customers.

To effectively differentiate product pricing:

- Find product and price strategies that help your business avoid a "race to the bottom"
- Understand where you can win on price, and where another means of competition is required
- Continually test, measure, and refine your approach

Ready. Set. Go.

The impacts and opportunities arising from the connected consumer can be overwhelming. It is a challenge to know where to focus and where to begin. A good place to start is with an assessment of your company's pricing strategy and capabilities. The primary goal is to gauge the current state of your pricing capabilities, define a desired future state, and then identify any gaps that exist. Retailers can then develop a prioritized roadmap of initiatives to address the gaps based on their potential value, ease of implementation, and risk level.

The connected consumer has been — and is expected to continue to be — a disruptive force in the retail industry. Retailers that take a concerted, strategic approach to building agile pricing capabilities in this dynamic market can capitalize on the opportunities and can achieve results that are real and sizeable. Those that don't may end up pricing themselves into extinction.

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