Designing Effective Pricing and Promotion Strategies
Optimizing the pricing and promotion of strategy for a large brand is a challenging topic:

- A myriad of different variables, market situations, channel influences, etc. cloud the cause / effect relationships
- Existing data sometimes is not very precise and/or necessary information may be missing making it difficult to draw meaningful conclusions
- Often, people in an organization hold strong, sometimes opposing beliefs on this topic and there are few explicit, and commonly held strategies

As a result, despite their obvious importance and the intense attention they receive, pricing and promotion strategies in many leading consumer products companies are made primarily on the basis of gut feel, perceived necessity, and the dynamics of a deal.

Our experience suggests that pricing and promotion decisions at the strategic level can be significantly improved by examining some of the underlying factors that determine the outcome of different pricing and promotion strategies.
Three Different Aspects of Pricing and Promotion

- As a way to structure the many variables affecting pricing strategies it is useful to explore three different, but interrelated aspects:

<table>
<thead>
<tr>
<th>Optimizing Volume and Profit Trade-offs</th>
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</thead>
<tbody>
<tr>
<td>Price changes often have impact on the volume purchased and/or consumed and the market share. The result on profits can be positive or negative. What are the dynamics that determine these trade-offs?</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Optimizing Price Realization and Value Perception</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumers perceive, assess and trade-off the perceived benefits relative to the price of different product bundles. Shares may change if consumers prefer the benefits of one product, even if prices are the same. How should you manage your benefit bundle and position the brand for optimal price realization and value perception?</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Managing Pricing &amp; Promotion Strategies Across Channels &amp; Markets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pricing and promotion strategies are often designed and executed for one retailer, channel, or local market at a time. How does the competitive position in a channel or market affect pricing options? Can you manage local markets and channels as a portfolio in order to optimize resource allocation and maximize volume and profit at a higher level?</td>
</tr>
</tbody>
</table>

- The remainder of this document introduces some concepts that have proven to be helpful in examining these aspects. The document is structured to introduce several frameworks of analysis and then present some selected data to show their application.
Optimizing Volume and Profit Trade-offs

- A key task is to understand the implicit trade-offs involved in pricing and promotion strategies. The following concepts can be helpful in attempting to optimize volume and profit trade-offs.

<table>
<thead>
<tr>
<th>Price Elasticity</th>
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</thead>
<tbody>
<tr>
<td>A change in price affects volume. The size of price reduction necessary to obtain sizable and profitable volume gains can differ from product to product. Different consumer segments may vary in their response. How do you best manage the price/volume/profit relationship?</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Promotional Intensity</th>
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<tbody>
<tr>
<td>Promotions have a significant impact by creating a volume lift. However, increasing promotional intensity (e.g., multi-brand, multi-package promotions) may have diminishing returns. How do you structure promotions to get the most lift at lowest overall cost?</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Category Profit Management</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pricing strategies for one product or brand impact the total category volume and profit of the retailer. How do you optimize the profit for both retailer and brand manufacturer?</td>
</tr>
</tbody>
</table>

- The following pages discuss these concepts in greater depth and highlight examples of data analysis that can answer some of these questions.
Price Elasticity

- Price elasticity explores the relationship between price changes and their impact on volume. A thorough understanding of these dynamics can lead to significant improvements in profitability.

**Example 1: Different slopes.** The responsiveness of consumers to purchase and/or consume more at lower prices obviously can vary among categories. Less well-known is the fact that the slope also may vary between two product forms or packages of the same brand. For example, an analysis of two package types for a leading brand manufacturer showed that package Y provides much greater volume lift for a price change than package X.
Price Elasticity, con’t.

**Example 2: Trigger Points.** The volume change often is not proportional to the price change. As a result the profit at different price points can vary dramatically. Many products may have only a few price points which provide the volume lift necessary to justify the price reduction. At intermediate price points the net profit impact often is negative.

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**Package X Unit Volume by Price Point**

<table>
<thead>
<tr>
<th>Average Weekly Price Points</th>
<th>Unit Volume</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>105,861</td>
</tr>
<tr>
<td>B</td>
<td>100,459</td>
</tr>
<tr>
<td>C</td>
<td>88,097</td>
</tr>
<tr>
<td>D</td>
<td>76,448</td>
</tr>
<tr>
<td>E</td>
<td>23,734</td>
</tr>
<tr>
<td>F</td>
<td>23,667</td>
</tr>
</tbody>
</table>

**Package X Dollar Volume At Selected Price Points**

Net Dollar Loss at A vs. B = ($10,067)
Example 3: Volume Shifts Among Brands. Price changes of one brand within a category not only affect the overall demand but also the shares of competing products within the category. Typically, the price/share shifts among national brands follow a different pattern than those between national brands and retailer brands.
Promotional Intensity

- Promotions have a significant impact by creating a volume lift, i.e., volume increase over the base volume. This volume however tends to diminish as the intensity of the promotion increases. In addition, dollar volume may actually decrease for some promotional combinations.

- This principle can be illustrated as follows:

- More specifically, our analysis suggests the following observations:
  - Multiple week promotions tend to generate less volume lift than an equivalent number of single week promotions
  - The volume lift appears to be lower when competing brands are also on deal than when they are off
  - When multiple packages are co-promoted, the net effect on lift may be less beneficial than the combined effect of promoting each separately

- These findings suggest that a national brand manufacturers could achieve the desired promotional volume lifts with significant savings by optimizing discounting and promotional intensity.
Alliance analysis of the pricing and promotion patterns in a large category suggest the following:

- **Prolonged Promotions Become Less Effective**
  - Unit Volume (000) vs. Price ($0 to $4.50)
- **Volume Lift is Lower When Competing Brands Are Also on Deal**
  - Unit Volume (000) for A only, B only, A & B, A & B & PL
- **The Net Affect On Volume and Dollar Lift of Multi-package Promotions May Be Unattractive**
  - Dual Pkg X & Y, Single Pkg X, Single Pkg Y, Base Volume
  - Cost Breakdown: $107, $139, $244, $230
Category Profit Management

- The pricing and promotion strategies for one product or brand also impact the volume and profit of the total category for the retailer. Successful brand strategies recognize the retailer’s objectives for the category and design pricing and promotions to provide sufficient category profits.

![Price Range of Products within Category]

**Examples of Retailer Objectives for Category**

- Desired category role is to e.g.,
  - Generate traffic
  - Generate profit
  - Enhance image
  - Differentiate from competitor
  - Increase loyalty
  - Etc.
Category Profit Management, con’t.

Retailer Brand Example

- Retailers are actively managing categories against the goals they have set. Retailer brands typically are managed with very specific objectives in mind. In general, the objectives of a retailer brand program are to:
  - Grow the category and increase profitability
  - Increase store traffic and attract the “right” kind of buyer
  - Enhance retailer differentiation and increase consumer loyalty

- However, retailers may have an incomplete understanding of how their own pricing and promotion of retailer brands affects the profitability of the category. In many instances, retailer brands actually reduce overall category profits because they e.g.,
  - Lower category dollar/volume share
  - Drive away customers to competing retailers
  - Trade down buyer baskets to lower retail dollar sales
  - Lower overall category profitability

- An important task for national brand manufacturers is to understand the true profit impact of the retailer’s brand on their category and where appropriate to educate retailers about the negative impacts these products can have.
Category Profit Management, con’t.

- A comprehensive analysis of the total profit impact of a retailer brand on a key category was instrumental in convincing the retailer to adjust the role of its brand relative to the leading national brand. Alliance analysis supported the following key arguments:

**Dollar and Volume Shares Decline After Retailer Brand Introduction**

**Competing Retailers Gain Most of Retailer’s Lost Volume**

**Retailer Brand Buyers Make Fewer Shopping Trips and Spend Less**

* Mass Merchandisers, Warehouse Clubs, Drug Stores

Note: Pre-period = Time period prior to introduction and emphasis of retailer brand
Post-period = Time period after introduction and emphasis of retailer brand
Optimizing Price Realization and Value Perception

- Products offer benefit “bundles” that consumers compare to competing products. Consumers perceive value by assessing and trading-off the benefits relative to the price of different product bundles. National brand manufacturers must carefully manage their product’s benefit bundle to optimize both price realization and value perception. The following concepts can be helpful when trying to balance the two objectives.

A. Value line: Products generally gain market share if consumers perceive they offer a better relative value than competing choices, and vice versa. A rigorous understanding of how consumers perceive quality or performance and price of different product bundles is critical. The value line can display the results of this analysis.

B. Consumer Segmentation: Consumers can be segmented by their primary purchase motivation. Benefit bundles offered by national brands should effectively target the appropriate consumer segments in order to maximize price realization.

C. Relative Costs and Segment Mobility: The ability and costs of each competitor to provide different levels of quality may vary significantly. Knowing your own and your competitors’ capabilities to move up for down the value line can guide successful repositioning strategies.

- The following pages discuss these concepts in greater depth and highlight some key examples.
Consumers perceive, assess and trade-off the value of different competing products. Value perception often can be disaggregated and analyzed around four different types of desired benefits.

### Value Line

#### Benefit Types

- **Tangible Benefits**: All physiological consequences a consumer wants to achieve or avoid by using the product.
- **Intangible Benefits**: The desired consequences a consumer wants to achieve at the personal level (i.e., feelings or thoughts consumer will have about herself) and the social level (i.e., feelings or thoughts others should have about the consumer as a result of her using a particular product).
- **Price/Value Benefit**: The perception that the price paid is the best available trade-off. Consumers will vary in the relative importance they attach to tangible and intangible benefits vs. price.
- **Situational Benefit**: Other considerations that are important in a specific purchase of usage situation. They typically are the reason the consumer does not pursue her first choice in a given situation. (e.g., availability, right package).

These benefit types vary in importance across different product categories and for different consumer segments.
Value Line, con’t.

- The interaction of the four benefit types on consumers’ value perception can be captured using the value line framework.

- Analyzing the market with this framework generally reveals that products gain market share if consumers perceive they offer a better relative value than competing choices, and vice versa. More important, the analysis highlights which specific types of benefits are driving these perceptions. The analysis is particularly useful in categories with several price points and differentiated products.
National brand manufacturers must not only be aware of where their products fall relative to others along the value line, but also understand how the consumers’ value perceptions change and reshape the value line.

In one category a distinct shift in consumer preferences had occurred. The higher quality end was no longer valued as highly after the lower end products had moved up to the middle spectrum.
A Framework for Analysis

Knowledge and Analysis Required to Develop Such a Strategy

<table>
<thead>
<tr>
<th>Company Related</th>
<th>Customer Related</th>
<th>Consumer Related</th>
</tr>
</thead>
</table>
| ▪ Customer Segmentation  
  – Recognize the different needs, economics, and opportunities for building advantage for various customer segments | ▪ Customer Need Analysis  
  – Examine which bundle of products, service, and funding is currently provided to different customer groups and how well it meets their needs relative to competition | ▪ Consumer Purchasing Needs Analysis  
  – Understand how the needs of different consumer segments and shopping occasions can best be met by different retailer channels |
| ▪ Value Chain Economics  
  – Understand the true economics, cost to serve, system profits, etc. by channel and customer segment, today and under potential change scenarios | ▪ Customer Related Business Process and Competitive Analysis  
  – Examine how system serves different customers, what strengths and weaknesses in meeting their needs are, how performance compares to competition, and how the overall supply chain could improve its relative efficiency and effectiveness | ▪ Pricing and Promotion Analysis  
  – Examine how pricing and promotion strategies can be improved to create traffic, volume growth, and satisfactory products |
| ▪ System Analysis  
  – Collect the “best practices” and ideas of the company to deal with customer strategy issues and internal competence development | | ▪ Retail Industry Analysis  
  – Understand competition among retail channels, future winners and losers, and how the company can guide retailers to pursue constructive strategies within a local market |
Consumer Segmentation

**Purchase Motivation**

- The purpose of this analysis is to segment consumers in each relevant market area according to their primary purchase motivation. Three broad groups typically emerge.

<table>
<thead>
<tr>
<th>Primary Purchase Motivation</th>
<th>Explanation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Intangible Benefit Seekers</strong></td>
<td>These consumers primarily buy because they identify with or like the brand message. Their product performance perceptions may be strongly influenced by the brand’s equity. Large parts of this segment appear to be immune to traditional private label. However, retailer brands with acceptable taste or performance and marketed with as much message and flair as “President’s Choice” or with a new message, e.g., “environmentally friendly,” can carve a growing niche out of this segment.</td>
</tr>
<tr>
<td><strong>Tangible Benefit Seekers (e.g., taste, packaging)</strong></td>
<td>These consumers are not loyal to the brand’s intangible equity but choose a product primarily because of perceived performance. They may switch to a retailer brand if it offers acceptable performance. This segment is most susceptible to retailers’ premium brands which have been improved to achieve performance parity with national brands. Value-oriented brands, particularly if the retailer’s product brand or its store equity has created a quality/value message, appeal to this segment as well.</td>
</tr>
<tr>
<td><strong>Serving Customers More Efficiently</strong></td>
<td>These consumers buy the lowest priced product largely independent of its performance. They probably make up most buyers of traditional private label products.</td>
</tr>
</tbody>
</table>
Determining the size and purchasing patterns of consumer segments allows the national brand manufacturer to understand which consumers are the most relevant to their products. For example, as national brand manufacturers develop strategies against private label, they must understand which consumer segments are purchasing private label. Some initial research suggests that “price” buyers continue to purchase a disproportionate amount of private label.

Purchase Motivation

- Intangible Buyers ("Infrequent PL Buyers")
- Tangible Buyers ("Occasional PL Buyers")
- Price Buyers ("Heavy PL Buyers")

Source: Total Supermarket Private Label Sales; Figures vary significantly from category to category
A.C. Nielsen Private Label Magazine
November/December
Consumer Segmentation, con’t.

**Benefit Proposition**

- This analysis examines how different competitors and private label suppliers attempt to bundle their proposed benefits to target specific consumer segments. Two of the most important desired benefit types typically fall into the following categories:
  - **Tangible benefits offered**
    - Low: product performance *inferior* to leading national brands
    - High: product performance *equivalent* to leading national brands
- The benefit proposition of different competitors can be displayed in the following matrix:

```
<table>
<thead>
<tr>
<th>Intangible Benefits</th>
<th>Premium</th>
<th>Value</th>
<th>Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>High</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Tangible Benefits
```
The benefit proposition of different competitors can then be placed on a value line chart to assess how effectively different consumer segments have been targeted.

Competitors A, B, and C have different benefit propositions...

...and capture different market shares

-- market share
The repositioning of different private label products offers an example of this dynamic. Within the same category, Chains A, B, and C (in different markets) reformulated their private label product (added tangible value) to match the national brand leader in blind performance comparison. Only C repositioned the private label to a new retailer brand with appropriate marketing support (also added intangible value). The consumer perceived Product C as a much higher value as evidenced by the sizable share gain.
Relative Costs and Segment Mobility

- Price changes often are explored in the context of repositioning a product, e.g., by adding new performance features, or other benefits. In this context it is important to examine the ability and the costs of each competitor to provide a similar or better bundle of benefits. This analysis also needs to explore whether a competitor could move its product offering successfully up or down to obtain a better relative position on the value line.

- In the example below, manufacturer A positioned its product at a point that optimizes the capabilities of its equipment. B has chosen to position its product at a point where its incremental cost of adding quality are higher than the rewards B receives in the market. C, on the other hand, could improve its relative positioning by adding further quality.
In 1999 Softwipe and Strongwipe were beginning to lose share to Private Label and Superfluff. By 2004 the situation had worsened. The analysis revealed that both Private Label and Superfluff repositioned their products to exploit the relative advantage of their processes. As a result the relative value offered by Softwipe and Strongwipe declined.

Market Share:

- Gaining
- Losing
- Stable
Market analysis revealed that consumers perceived a “minimum threshold” of quality, below which the perceived value rapidly dropped. By repositioning Strongwipe downward Private Label was forced to move below the threshold in order to maintain the necessary price discount. Many consumers now switched back to Strongwipe.
Managing Pricing and Promotion Strategies Across Markets and Channels

- Pricing and promotion strategies are often designed and executed in “isolation” (i.e., focused on only one market, channel, or retailer.) Markets and channels should be managed as a “portfolio” in order to optimize resource allocation and maximize the impact of pricing and promotion strategies. The following concepts should be considered when designing overall pricing and promotion strategies.

1. **Market Leadership Price Premium**: In markets where a national brand has a sizable share advantage over its competitors, the brand typically can maintain a price premium relative to its competitors while holding share. National brand manufacturers’ pricing strategies impact relative market shares and the potential to exploit this principle.

2. **Channel Dominance Price Premium**: In channels where a national brand has a sizable share advantage over its competitors, the brand typically can maintain a price premium relative to its competitors while holding share. National brand manufacturer’s pricing strategies impact relative market shares and the potential to exploit this principle.

- The following pages discuss these two concepts in greater detail and highlight key examples and exceptions.
Market Leadership Price Premium

- In markets where a national brand has a sizable share advantage over its competitors, the brand can typically maintain a price premium relative to its competitors while holding share. This fact can guide marketing strategies towards prioritizing and targeting key local markets.

- For example, in markets where Brand A has a sizable share advantage over Brand B, Brand A can maintain a price premium relative to Brand B while holding share. The reverse is true for Brand B in its leading markets.

- This principle can be displayed in the following way:

```
Brand A Price Relative to Brand B at Stable Share

Brand A Share within a Market Relative to Brand B
```

<table>
<thead>
<tr>
<th>Brand A Share</th>
<th>Lower</th>
<th>Same</th>
<th>Higher</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brand A Price</td>
<td>Lower</td>
<td>Same</td>
<td>Higher</td>
</tr>
</tbody>
</table>

**Higher**

**Same**

**Lower**
Market Leadership Price Premium, con’t.

- Analysis of a number of different local markets shows that a certain relative market share must be reached before a price premium can be maintained. The relationships may be clouded by the changing prices and promotions.

Note: Each point represents one Nielsen period
Market Leadership Price Premium, con’t.

- There are other exceptions to this principle. In one category, Alliance examined aggregate market level data which seemed to deviate significantly from the postulated relationship.

- An analysis of the leading national brands across markets revealed three general types of exceptions to the expected relationship.

![Diagram showing the relationship between Brand A's share within a market and Brand A's price relative to Brand B.](image)

- **Brand A Price Relative to Brand at Stable Share**
  - Higher
  - Same
  - Lower

- **Brand A Share within a Market Relative to Brand B**
  - Lower
  - Same
  - Higher

<table>
<thead>
<tr>
<th>Category</th>
<th>Stable Share</th>
<th>Relative Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lower</td>
<td>Lower</td>
<td>3</td>
</tr>
<tr>
<td>Same</td>
<td>Same</td>
<td>1</td>
</tr>
<tr>
<td>Higher</td>
<td>Higher</td>
<td>2</td>
</tr>
</tbody>
</table>
Further analysis at the market level explained these three exceptions:

<table>
<thead>
<tr>
<th>Exception 1 - The Overeager Discount Response</th>
<th>Exception 2 - Brand A’s Market Leadership not Real</th>
<th>Exception 3 – The Milking Markets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brand A did not exploit the opportunity to maintain a price premium commensurate with leadership position. Brand A was responding too eagerly to every price reduction and promotion of Brand B.</td>
<td>The market share advantage of Brand A in these markets is not based on a stronger brand franchise but on the fact that Brand A is buying its share leadership from Brand B. Consumers in these market are, or are encouraged to become, highly price sensitive which implies that discounting and promotions drive volume and share changes more dramatically than in other markets. This tends to create a prisoner’s dilemma in tempting to both brands to discount, proactively or defensively.</td>
<td>In some markets, Brand A appeared to be milking a weak share position by maintaining a price premium. In others, Brand A was experiencing aggressive underpricing by Brand B because Brand B was “buying” its share leadership in these markets. This was the mirror image of Exception 2.</td>
</tr>
</tbody>
</table>

**Diagram:**
- Brand A Price Relative to Brand at Stable Share
- Brand A Share within a Market Relative to Brand B
- Higher, Same, Lower

**Legend:**
- Exception 1: The Overeager Discount Response
- Exception 2: Brand A’s Market Leadership not Real
- Exception 3 – The Milking Markets
Channel Dominance Price Premium

- In channels where a national brand has a sizable share advantage over its competitors, the brand can typically maintain a price premium relative to its competitors while holding share. This fact can guide a manufacturer’s strategy towards prioritizing certain advantages retailer channels. Focus can lead to share advantage and be rewarded with a price premium.
- The principle can be displayed with this matrix

![Graph showing the relationship between Brand A's share within a channel relative to Brand B and Brand A's price relative to Brand at stable share.](image)
Channel Dominance Price Premium, con’t.

- In reality, not all channels in all markets conform to this principle. A review of available information for a leading, national brand manufacturer suggested that for the majority of channels, the price premium or discount was strongly correlated to relative share position, but with two typical exceptions.
Channel Dominance Price Premium, con’t.

These exceptions were explained by the following market occurrences:

- Brand A used this channel to “buy” volume and a higher than average share position.
- The channel used product as a loss leader and gave preferential treatment to the lowest priced supplier.

These exceptions were explained by the following market occurrences:

- Brand A used this channel to improve margins by “milking” its overall market position.
- The Channel itself operated at a higher price point than the rest of the market.
- Brand B used this channel to buy volume and A did not follow.
Summary Comments

- The preceding examples show some of the issues involved in developing successful pricing and promotion strategies for national brands in important categories. Our experience with several large, well managed, and successful consumer goods companies suggests that there is significant profit potential in fine tuning or reexamining pricing and promotion strategies.

  - We have also found that often there are organizational barriers to such a reassessment, typically based on some of the following beliefs.
  - “We have only a narrow degree of freedom in pricing. Competition dictates what we can do.”
  - “We don’t have the data to do a meaningful analysis of all relevant relationships.”
  - “If we could raise our price without damage, we would already have done it. We try it often enough.”
  - “A significant price change would require a fundamental reformulation and repositioning of the brand. We do not have consensus on whether or how to do it.”
Summary Comments, con’t.

- An attack from private label or discount brands rarely can be thwarted with just pricing and promotion. Our experience suggests that other activities may be equally important, for example:

  **Reexamine the consumer franchise**

  As new products with very different benefit bundles (e.g., high quality but no brand imagery) are offered, the traditional consumer segmentation criteria may no longer be appropriate, particularly if they are based on demographics. A more insightful consumer analysis may explore a segmentation based on “mindsets,” i.e., the beliefs and attitudes different consumers hold about their desired benefits (e.g., tangible, intangible, price/value, situational) and how they are met by the competing offering.

  **Reexamine the customer strategy**

  In the past decade, major changes which are altering the role of channels and the nature of their relationship with national brand suppliers have occurred and are continuing at an accelerated pace. These changes present new challenges and opportunities.

  **Reexamine key business processes**

  An effective strategic response to retailer brands may increase the complexity of the business, e.g., through more product extensions, a more segmented approach to retailers, etc. Does the organization have the skills, systems, and processes to operate at a higher level while also reducing costs?